



INTERIM REPORT

Three and nine months ended September 30, 2011



LETTER TO THE SHAREHOLDERS

The third quarter of 2011 was the busiest in the history of Arcan Resources Ltd. ("**Arcan**" or the "**Corporation**"). Arcan significantly accelerated its drilling and completion programs and secured critical services including acid blending and stimulation. The successes experienced during this quarter puts Arcan on track to achieve its 2011 year-end exit rate of 6,000 barrels of oil equivalent ("**BOE**") per day. Arcan's 2011 activities to date were highlighted in an independent reserves evaluation, dated November 4, 2011 and effective September 30, 2011 (the "**GLJ Update Report**"), which shows a 67 percent increase in Arcan's Proved plus Probable ("**P+P**") reserves and a 29 percent increase to \$7.17 in net asset value per share. The GLJ Update Report was prepared by GLJ Petroleum Consultants ("**GLJ**"), Arcan's independent qualified reserves evaluator for 100 percent of Arcan's oil and gas properties.

Over the third quarter of 2011 Arcan accelerated its drilling program and spudded a record number of wells. After drilling 11 wells in the first two quarters of the year, Arcan spudded ten wells in the third quarter. Arcan also had a record quarter for fracturing with one well being fractured in June, two wells being fractured in July, four wells being fractured in August and five wells being fractured in September. Despite significant operational challenges caused by extreme flooding and third party pipeline issues in the Swan Hills area, the Corporation was able to ramp up its activities as the third quarter progressed. The flooding cost Arcan seven out of its ten bridges and the third party oil sales pipelines out of the Deer Mountain Unit #2 ("**DM2**") and out of the Morse River Unit #1 ("**Morse River**"). The financial cost to Arcan, in addition to the repairs, accounted for approximately \$10.00 to \$15.00 per barrel in operating costs related to the practical difficulties in trucking emulsion from oil wells to its facilities and then trucking the Corporation's clean oil to sales, additional road maintenance, delayed well testing, and equipping and servicing delays. Despite these operational difficulties, Arcan's significant efforts in the field paid off as production rose, allowing Arcan to achieve record quarterly production of 3,684 BOE per day (94 percent oil). Arcan is now seeing the success of its third quarter 2011 drilling program, as September 2011 production averaged approximately 4,000 BOE per leaving a fourth quarter forecast of 4,600 - 4,800 BOE per day. Based on the results of the first three quarters, Arcan estimates that its 2011 yearly production will average 3,500 BOE per day and is currently on track to meet its 2011 year-end target exit rate to 6,000 BOE per day.

Also in the third quarter, Arcan prepared and subsequently press released the GLJ Update Report. The highlights derived from the GLJ Update Report included a new estimated net asset value of \$7.17 per share, up 29 percent from the \$5.56 per share at December 31, 2010. Arcan's shareholders now own reserves worth \$773 million net present value of future net revenue of working interest total P+P reserves before tax at 10 percent discount rate, up 65 percent from \$468 million posted as at December 31, 2010. The September 30, 2011 numbers are based on 35.2 million BOE ("**MMBOE**") total P+P reserves, representing 67 percent growth in 2011 from the 21.1 MMBOE total P+P reserves as at December 31, 2010. The reserves were only booked for 118 wells on 57 sections of Arcan's 171 sections of land. Arcan will continue to prove up these resources and develop its lands and reserves for its December 2011 year end reserves report. Based upon recorded P+P reserves assigned by GLJ, the Corporation estimates that there are significant additional un-booked resources on its undeveloped land position.

As previously disclosed, Arcan has been strategically procuring the services, equipment, and materials required to execute the development plan in the Swan Hills area. These activities culminated on September 13, 2011 with the acquisition of StimSol Canada Inc. ("**StimSol**") for \$24.0 million (the "**StimSol Acquisition**"). StimSol is a stimulation services company whose business includes an exclusive ten year distribution license for a hydrochloric acid blend called "Stim 28". Arcan has been using Stim 28 in its Swan Hills multi-stage fracture program and acquired StimSol as part of its strategy to secure an acid supply and blend which will assist in the development of its Swan Hills lands. To facilitate safety, product consistency and delivery timing, StimSol is currently constructing a 1,000 cubic meter per day centralized blending facility near the town of Swan Hills that will act as a service supplier for blended acid in the Swan Hills area. Early in 2011, Arcan anticipated acid shortages and attempted to minimize the impact of such shortages on its business. As acid shortages have become very acute in the industry early in the fourth quarter, Arcan's planning and execution has been rewarded as Arcan is now in a position to fracture up to five wells to date in the fourth quarter. Further, Arcan anticipates that it will fracture five additional wells prior to the end of the year. Arcan believes that fracture acid will be in critical demand as it drills through the fourth quarter of 2011 and into the first quarter of 2012 and it continues to focus its efforts to ensure the execution of its development drilling program.

Highlights of the third quarter of 2011:

- Production was up 34 percent to 3,684 BOE per day for the three months ended September 30, 2011 from 2,740 BOE per day for the three months ended September 30, 2010, and up 28 percent from 2,871 BOE per day in the second quarter of 2011;
- Operating netbacks increased to \$41.90 per BOE (on revenue of \$83.70 per BOE with operating costs of \$24.33 per BOE), up five percent from \$39.98 per BOE in the third quarter of 2010 but down 24 percent from \$55.29 per BOE in the second quarter of 2011;
- Funds from operations rose 36 percent to \$10.5 million (\$0.12 per diluted share) in the third quarter of 2011 from \$7.7 million (\$0.10 per diluted share) in the third quarter of 2010 and up four percent from \$10.1 million (\$0.10 per diluted share) in the second quarter of 2011;
- Income of \$0.8 million in the third quarter of 2011 was up from a loss of \$2.0 million in the third quarter of 2010 but down from the income of \$4.3 million in the second quarter of 2011;
- Spud ten horizontal wells and completed 11 horizontal multi-stage fracture oil wells in the third quarter of 2011. Since that time, Arcan has drilled an additional five horizontal wells and completed five horizontal multi-stage fracture treatments;
- Expended \$86.7 million in capital during the third quarter of 2011, including the StimSol Acquisition;

- Hedged an additional 1,000 barrels of oil per day for 2012, bringing the total to 2,000 barrels per day hedged for 2012, and 500 barrels of oil for 2013; and
- Raised \$50.8 million of equity at \$5.45 per share on October 7, 2011, as well as \$85.0 million in 6.50% seven year convertible debentures, leaving Arcan with available funds of \$145.0 million (net of working capital) subsequent to the closing of the financing.

Arcan is well capitalized to execute its business plan into 2012. Since the third quarter, Arcan closed a \$50.8 million equity offering and an \$85.0 million convertible debenture financing. This financing has allowed Arcan to raise its 2011 capital budget to \$225.0 million and has provided Arcan with the financial flexibility required to continue development of its Swan Hills asset base. The Corporation's new budget includes the \$24.0 million StimSol Acquisition, \$13.3 million paid to acquire an additional 13 sections of land and the drilling and completion of 35 new horizontal multi-stage fracture wells in 2011. As at October 7, 2011, Arcan had \$86.3 million of convertible debentures due in 2016, \$85.0 million of convertible debentures due in 2018, a \$26.3 million working capital surplus and \$120.0 million in undrawn bank lines of credit.

Arcan estimates a significant reduction in operating expenses in the first quarter of 2012 due to a number of activities which are currently underway. These activities include completion of a high grade road system that connects the DM2 through Arcan's Ethel property into Morse River, the commencement of pipeline infrastructure along the new road system backbone that will allow production in Ethel to flow to the DM2 oil facility, and the construction of pipeline infrastructure to facilitate water injection in the Ethel area. Arcan is also working on resolving issues with the clean oil pipeline which flows from the DM2.

In the third quarter of 2011, Arcan's funds from operations were \$10.5 million on a 3,684 BOE per day basis with an operating netback of \$41.90 per BOE. Consolidated operating netbacks decreased as a result of oil prices falling to \$83.70 from \$101.10 per barrel in the second quarter. Although royalties decreased to \$16.20 per BOE, operating costs were elevated to \$24.33 per BOE in the third quarter. These results compare to consolidated operating netbacks of \$39.98 per BOE in the third quarter of 2010 and \$55.29 per BOE in the second quarter of 2011.

As of January 1, 2011, Arcan now employs International Financial Reporting Standards ("**IFRS**"). The Corporation encourages you to carefully read its management's discussion and analysis together with its quarterly unaudited interim consolidated financial statements as it has provided information regarding IFRS accounting policies and prepared reconciliations between previous Canadian generally accepted accounting principles ("**GAAP**") and IFRS. Comparative numbers for 2010 have also been updated to reflect IFRS changes. The changes resulting from the Corporation's transition to IFRS have not impacted the operating assets of Arcan, but have significantly modified its consolidated financial statements and related notes. Further information on the impact of the changeover to IFRS is provided in the "Accounting Policies" section of the Arcan's management's discussion and analysis.

Arcan is focusing additional efforts on prudent waterflood management and development nucleating from the DM2 existing infrastructure. Several DM2 injector stimulations and a complete water injection cleanout have been instituted to date in 2011. Source water delineation has been addressed and an ample supply has been identified. Within the DM2 enhanced recovery scheme area two new injectors will be on-stream to assist in voidage replacement prior to year-end. Management anticipates that additional seven injectors will be added within the DM2 scheme via recompletion activities to further facilitate pressure maintenance in the first quarter of 2012. An additional three conversions and six injector drills are also slated for expansion of the Ethel enhanced recovery scheme in the first quarter of 2012. Cumulative voidage replacement since the commencement of the DM2 scheme is 0.6 and to date in 2011 has averaged 0.6 on a monthly basis. A target voidage replacement of one or greater is strategized starting in December 2011. The anticipated impact in DM2 is an enhancement of pool management for the maximization of ultimate pool recoveries and an improvement in the 2012 oil decline projections. Arcan's drilling program continues to be focused around land retention, reserves bookings and production in the Ethel area. To maintain land retention Arcan is drilling wells in its tier one, two and three areas. Overall, Arcan's wells continue to support Arcan's average well type production profile.

The Corporation's success to date has been achieved despite the unpredictable and challenging external events which occurred in the first nine months of 2011. In addition to issues which resulted from extreme flooding in the Swan Hills area, the Rainbow pipeline system in the Hamburg area was also shut down and did not resume shipping until September 2011. Throughout these events, Arcan continued to successfully execute on its business plan and deliver on its strategy of maximizing the value of its Swan Hills assets. Arcan believes that the GLJ Update Report starts to highlight the capital efficiency of the application of a horizontal, multi-stage fracture program in the Swan Hills reservoir. The Corporation now owns 171 net sections of land on the Swan Hills Beaverhill Lake light oil play having drilled or re-entered old well bores covering over 30 kilometres. For 2012, in addition to water injection activities, Arcan plans to utilize three rigs to breakup and add up to 40 wells in the year. Arcan will continue to evaluate capital spending and activity levels to ensure it is able to maintain a strong balance sheet and respond appropriately to any fluctuations or industry downturns caused by world economic events. To provide additional financial stability, Arcan has hedged 2,000 barrels per day for 2012, 500 barrels per day for 2013 and maintains strong banking and finance syndicates. With a large, defined inventory at the forefront of an emerging light oil play, Arcan expects that the Swan Hills area will continue to transform Arcan through the rest of 2011 and beyond.

On behalf of the Board of Directors,

(Signed) "*Ed Gilmet*"

President, Chief Executive Officer and Director

November 24, 2011

MANAGEMENT'S DISCUSSION AND ANALYSIS

Arcan Resources Ltd. ("**Arcan**" or the "**Corporation**") is engaged in exploring for, developing and producing petroleum and natural gas in Western Canada. Arcan was incorporated on October 9, 2003 and conducted operations as a private company until January 1, 2007, maintaining a June 30 year end. On January 1, 2007, Arcan amalgamated with Desco Energy Ltd. with the amalgamated entity's year end established as December 31. The amalgamation resulted in Arcan becoming a public company and a reporting issuer, with its shares trading on the TSX Venture Exchange under the symbol 'ARN' beginning on January 9, 2007. On September 13, 2011 Arcan purchased all of the issued and outstanding shares of StimSol Canada Inc. ("**StimSol**") (the "**StimSol Acquisition**"), which is now a wholly owned subsidiary of Arcan. StimSol provides fracturing and stimulation services to companies operating in the petroleum and natural gas industry in western Canada. Arcan now reports as a consolidated entity, including its wholly owned subsidiary StimSol.

Basis of Presentation

This Management's Discussion and Analysis ("**MD&A**") is reported on a consolidated basis and is an explanation, through the eyes of management, of how Arcan performed during the periods covered by the unaudited financial statements of Arcan filed concurrently with this MD&A, and of Arcan's consolidated financial condition and future prospects. This MD&A is for the three and nine months ended September 30, 2011, as compared to the three and nine months ended September 30, 2010.

The unaudited interim consolidated financial statements to which this MD&A relates have been prepared in accordance with International Financial Reporting Standards ("**IFRS**") and IAS 34 Interim Financial Reporting. The Corporation adopted IFRS on January 1, 2011 with a transition date of January 1, 2010. Previously, Arcan had prepared its consolidated financial statements in accordance with Canadian generally accepted accounting principles ("**GAAP**"). The Corporation has provided IFRS accounting policies and prepared reconciliations between GAAP and IFRS in the notes to its unaudited interim financial statements for the three months ended March 31, 2011, for the three and six months ended June 30, 2011 and for the three and nine months ended September 30, 2011. Further information on the impact of IFRS is provided in the "Accounting Policies" section of this MD&A.

This MD&A complements and supplements the unaudited interim consolidated interim financial statements of Arcan. For a full understanding of the consolidated financial position and results of operations of the Corporation, this MD&A should be read in conjunction with the unaudited interim consolidated interim financial statements for the three and nine months ended September 30, 2011 and 2010, together with the notes thereto, as well as Arcan's audited financial statements for the year ended December 31, 2010, together with the notes thereto, prepared in accordance with GAAP and other documents filed on SEDAR, including Arcan's historical financial statements, the information circular dated April 27, 2011 relating to the Corporation's annual general and special meeting of shareholders held on June 1, 2011 and the Corporation's annual information form for the year ended December 31, 2010 (the

"AIF"). These documents are available under the Corporation's profile on SEDAR at www.sedar.com.

Arcan's management is responsible for the integrity of the information contained in this MD&A and for consistency between the MD&A and the unaudited interim consolidated financial statements. In preparing these statements estimates are necessary and management believes any estimates have been based on careful judgments and are properly presented. The unaudited interim consolidated financial statements have been prepared using policies and procedures established by management and fairly reflect Arcan's consolidated financial position, consolidated results of operations and consolidated funds from operations. In this MD&A, unless otherwise indicated, all monetary amounts are in Canadian dollars as are all references to "\$". Arcan's Board of Directors and Audit Committee have reviewed and approved the unaudited interim consolidated financial statements and MD&A for the three and nine months ended September 30, 2011. This MD&A is dated November 24, 2011.

Readers should carefully read the section "Non-IFRS Measurements" below and the sections "Legal Advisories" and "Forward-Looking Information and Statements" at the end of this MD&A.

Non-IFRS Measurements

Readers are cautioned that this consolidated MD&A contains the term "funds from operations", which should not be considered an alternative to, or more meaningful than, "cash provided by operating activities" or "net earnings" as determined in accordance with IFRS as an indicator of Arcan's performance. Arcan also presents "funds from operations per share", whereby funds from operations are divided by the basic and diluted weighted average number of common shares of Arcan (each, a "**share**") outstanding to determine per share amounts. Operating netbacks are presented on an operating segment and consolidated basis. "Operating netbacks" for the exploration and production segment represent Arcan's petroleum and natural gas revenue, less royalties and production and operating expenses. "Operating netbacks" for the fracturing and stimulation segment represent fracturing and stimulation services revenue, less cost of sales for fracturing and stimulation services. "Consolidated operating netbacks" represent the sum of the operating netbacks for the exploration and production and fracturing and stimulation segments. "Corporate netbacks" represent Arcan's consolidated operating netback, plus other revenue, less realized economic hedging losses, cash general and administrative ("**Cash G&A**") expenses and cash interest expenses in order to determine the amount of funds generated by production. Operating and corporate netbacks have been presented on a per barrel of oil equivalent ("**BOE**") basis, as well.

The measures referenced above do not have any standardized meaning prescribed by IFRS and therefore are unlikely to be comparable to similar measures presented by other companies. Management believes that funds from operations and both operating and corporate netbacks are useful supplemental measures as they indicate Arcan's ability to fund future growth through capital investment and/or to repay debt. These measures have been described and presented in this MD&A in order to provide shareholders and potential investors with additional information regarding Arcan's liquidity and its ability to generate

funds to finance its operations. Arcan's method of calculating funds from operations may differ from other companies, and as such, may not be comparable. Please see the section "Results of Operations – Netbacks" for reconciliations between both operating netbacks and corporate netbacks to revenue.

Arcan determines funds from operations as cash flow from operating activities before changes in non-cash working capital as follows:

Funds from Operations

(\$000's)	Three Months Ended		Nine Months Ended	
	September 30, 2011	September 30, 2010	September 30, 2011	September 30, 2010
Cash flow from operating activities (per IFRS)	10,469	5,372	29,538	11,589
Change in non-cash working capital	21	2,281	(54)	3,392
Funds from operations	10,490	7,653	29,484	14,981

Third Quarter 2011 Highlights:

- Production was up 34 percent to 3,684 BOE per day for the three months ended September 30, 2011 from 2,740 BOE per day for the three months ended September 30, 2010, and up 28 percent from 2,871 BOE per day in the second quarter of 2011;
- Operating netbacks increased to \$41.90 per BOE (on revenue of \$83.70 per BOE with operating costs of \$24.33 per BOE), up five percent from \$39.98 per BOE in the third quarter of 2010 but down 24 percent from \$55.29 per BOE in the second quarter of 2011;
- Funds from operations rose 36 percent to \$10.5 million (\$0.12 per diluted share) in the third quarter of 2011 from \$7.7 million (\$0.10 per diluted share) in the third quarter of 2010 and up four percent from \$10.1 million (\$0.10 per diluted share) in the second quarter of 2011;
- Income of \$0.8 million in the third quarter of 2011 was up from a loss of \$2.0 million in the third quarter of 2010 but down from the income of \$4.3 million in the second quarter of 2011;
- In the third quarter of 2011, ten horizontal wells were spud and 11 horizontal multi-stage fractured oil wells were completed. Since that time, Arcan has drilled an additional five horizontal wells and completed five horizontal multi-stage fracture treatments;
- A capital expenditure program of \$86.7 million was completed, including the StimSol Acquisition; and
- On October 7, 2011, Arcan raised \$50.8 million of equity at \$5.45 per share as well as \$85.0 million in 6.50% seven year convertible debentures, leaving Arcan's available funds of \$145.0 million (net of working capital) subsequent to the closing of the financing.

Consolidated Financial and Operating Summary⁽¹⁾

	Three Months Ended		Nine Months Ended	
	September 30, 2011	September 30, 2010	September 30, 2011	September 30, 2010
Financials (\$000s except per share amounts)				
Oil and NGL sales	27,930	16,607	70,648	34,941
Natural gas sales	440	500	1,242	2,214
Petroleum and natural gas revenue	28,370	17,107	71,890	37,155
Fracturing and stimulation services revenue	351	-	351	-
Cash provided by operating activities	10,469	5,372	29,538	11,589
Funds from operations ⁽²⁾	10,490	7,653	29,484	14,981
Per share basic ⁽²⁾	0.12	0.10	0.33	0.23
Per share diluted ⁽²⁾	0.12	0.10	0.33	0.23
Net income (loss)	776	(1,988)	2,483	(4,742)
Per share basic	0.01	(0.03)	0.03	(0.07)
Per share diluted	0.01	(0.03)	0.03	(0.07)
Capital expenditures, net – cash	86,696	28,386	159,097	120,461
Total assets	440,687	271,255	440,687	271,255
Total liabilities	213,819	115,051	213,819	115,051
Shareholders' equity	226,868	156,204	226,868	156,204
Bank loan	43,990	55,141	43,990	55,141
Net debt and working capital ⁽⁵⁾	163,010	78,554	163,010	78,554
6.25% Debentures maturing in 2016 - face value	86,250	-	86,250	-
Operating				
Production:				
Crude oil and NGLs (bbls per day)	3,477	2,523	2,858	1,785
Natural gas (Mcf per day)	1,242	1,301	1,090	1,619
BOE per day (6:1) ⁽³⁾	3,684	2,740	3,040	2,055
Average realized price:				
Crude oil and NGLs (\$ per bbl)	87.31	71.55	90.55	71.70
Natural gas (\$ per Mcf)	3.85	4.18	4.17	5.01
Combined price per BOE (incl. processing revenue) (\$ per BOE)	83.70	67.87	86.63	66.23
Netback (\$ per BOE)				
Petroleum and natural gas sales	83.70	67.87	86.63	66.23
Fracturing and stimulation services revenue	1.03	-	0.42	-
Royalties	(16.20)	(15.94)	(17.09)	(15.80)
Production and operating expenses	(24.33)	(11.95)	(22.42)	(13.44)
Cost of sales for fracturing and stimulation services	(2.30)	-	(0.94)	-
Consolidated operating netback (\$/BOE)	41.90	39.98	46.60	36.99
Realized economic hedging losses – cash	-	-	(0.42)	-
G&A expenses – cash	(6.06)	(7.50)	(5.98)	(7.96)
Other revenue	0.01	-	0.14	-
Finance expenses - cash	(4.29)	(2.07)	(4.40)	(2.27)
Corporate netback	31.56	30.41	35.94	26.76
Common Shares (000s)				
Shares outstanding	88,426	75,418	88,426	75,418
Weighted average – basic	88,425	75,245	88,242	66,297
Weighted average – diluted ⁽⁴⁾	89,919	75,245	89,397	66,297

Notes:

- (1) The quarters ended September 30, 2010 have been restated for the effect of adopting IFRS. Further information on the impact of IFRS is provided in the unaudited financial statements for those periods and in the "Accounting Policies" section.
- (2) The reader is referred to the section "Non-IFRS Measurements".
- (3) The reader is referred to the section "Legal Advisories".
- (4) Basic and diluted weighted average shares are the same in 2010 as the Corporation incurred a loss in these periods.
- (5) Net debt and working capital is calculated by subtracting the Corporation's current liabilities, bank debt, and convertible debentures for its current assets and excludes net proceeds of the October 7, 2011 financing.

Overview

Swan Hills, Alberta

The Swan Hills reef complex is located in north central Alberta, approximately 200 kilometres northwest of Edmonton. The main portion of Swan Hills was discovered and developed through vertical drilling in the 1950's and 1960's. This reef complex is over 50 miles long, covering more than 24 townships of land and is recognized as having a very large accumulation of 40° API light sweet oil-in-place. The main portion of the reef has undergone extensive waterflood operations, and in many of its pools, has recovered over 40 percent of the oil-in-place.

Arcan first purchased interests in the Swan Hills play in 2005, and has accumulated 176 gross (171 net) sections of land on the play, built new facilities to handle a large production base, and implemented a waterflood in the northern portion of its land base. Oil prices since 2005 have helped solidify the economics in this area; however, significant change has occurred with the Corporation's successful application of horizontal drilling and multi-stage fracture technology. The use of multi-stage fractured wells represents a shift in the exploitation of the Swan Hills reef complex. Arcan completed its first horizontal multi-stage fractured well in February 2010 and is utilizing pre-existing vertical well bores, along with proprietary 3D seismic data to delineate its horizontal drilling activity. For the remainder of the year and the first quarter of 2012, Arcan intends to focus primarily on drilling and implementing a waterflood in the central portion of the Corporation's land block in the Ethel area. By expanding development into these relatively undeveloped areas, Arcan anticipates future reserve additions.

Arcan has two types of well production profiles consisting of: (i) wells on enhanced oil recovery ("**EOR**") which are fully supported by waterflood; and (ii) wells producing on primary recovery which are awaiting future implementation of an EOR scheme. Arcan's operations are focused on drilling followed by EOR to achieve maximum production results. The Corporation believes that once these additional wells are fully supported by waterflood, their production patterns will modify and move to a higher recovery of the original oil-in-place. For 2011, Arcan only replaced fifty-five percent of production with water in the DM2. In the first quarter of 2012 Arcan plans to add 13 injection wells followed by a further three injectors in the second quarter. It is anticipated that these injectors will assist in pressure maintenance and long term production and recoveries.

Arcan estimates that its new wells will reach pay-out at approximately 80,000 barrels ("**bbls**") factoring oil at \$80.00 per barrel ("**bbl**") less a \$5.00 royalty rate and operating costs of \$20.00 per bbl. Given the current economics, Arcan estimates that its 2011 drilling program focused in the Ethel area could pay-out in approximately one year, on primary recovery, and under a fully developed waterflood recovery, could ultimately recover 35 to 40 percent of the oil-in-place. On average, Arcan's wells are drilled to a total depth of approximately 4,000 meters with 1,000 to 1,500 meter horizontal legs which are multi-stage acid fractured utilizing ten to 15 and up to 30 stages with a total of 600 to 1,400 cubic meters of acid. Arcan plans to continue to modify its completion techniques to determine maximum well results. The average cost per well for drilling and multi-stage fracturing, along with all

associated equipment and tie-in is approximately \$4.4 million, with an additional \$1.0 million budgeted per new well to provide for waterflood implementation.

Arcan has worked to secure the four primary components of its development plan, including: drilling rigs, fracture crews and equipment, acid and fracture fluid blending. In recognizing early on that fracture fluids could face shortages Arcan completed the StimSol Acquisition for its rights to "Stim 28", which Arcan uses to fracture its wells in the Swan Hills.

Production and operations in the Swan Hills area were challenging in the first three quarters of 2011. In addition to shut-in production as the Corporation replaced the pumps in all existing multi-stage fracture horizontal wells, Arcan endured record rainfall and encroaching forest fires in the second quarter, which have now abated. Third party non-operated pipeline issues have continued to provide challenges; however, the Corporation anticipates that these issues will be short-term in nature relative to its current development plan. Production in Swan Hills area averaged 3,220 BOE per day on \$47.94 per BOE operating netbacks for the quarter ended September 30, 2011, up from 2,205 BOE per day on \$43.67 per BOE operating netbacks for the quarter ended September 30, 2010 and up from 2,466 BOE per day on \$57.52 per BOE operating netbacks in the second quarter ended June 30, 2011. Arcan's production in the Swan Hills area averaged 2,579 BOE per day on \$50.99 per BOE operating netbacks for the nine months ended September 30, 2011, up from 1,412 BOE per day on \$41.50 per BOE operating netbacks for the nine months ended September 30, 2010. Arcan's wells in the Swan Hills area produced approximately 1,648 BOE per day on average in 2010 and 623 BOE per day on average in 2009. Production increases were primarily attributable to the continued impact of drilling the new horizontal multi-stage fractured oil wells.

The significant growth achieved by Arcan in 2010 and the first nine months of 2011 represents only the beginning of the development of its 176 (171 net) sections of land. The Corporation is currently operating 45 horizontal wells and estimates that it may have access to over 400 additional drilling locations. The Swan Hills reef has long life, light sweet 40° API oil that historically has provided 40 percent recoveries under waterflood. Arcan continues to work towards unlocking the potential of reserves through drilling and waterflood activities, and expects to repeat its success in implementing horizontal drilling and multi-stage fracturing technology to convert the Swan Hills play from a legacy resource play to a robust growth opportunity.

Hamburg, Alberta

Arcan has a 50.25 percent working interest in the Hamburg GG oil pool and is the operator of the oil battery and waterflood. Arcan's wells in the Hamburg GG oil pool produce light sweet 41° API oil and natural gas, the majority of which are located within the waterflood scheme. Arcan owns a 100 percent interest in the three sections of land immediately offsetting the Hamburg GG oil pool on the southern boundary, and drilled one well on these lands in December 2010.

Arcan was forced to truck all of its production from the area for the entire third quarter of 2011 due to the outage of the Rainbow pipeline, which has now been repaired. This negatively impacted netbacks for the third quarter. Production averaged 410 BOE per day on \$11.80 per BOE operating netbacks for the quarter ended September 30, 2011 in Hamburg, down from 456 BOE per day on \$29.01 per BOE operating netbacks for the quarter ended September 30, 2010, but up from 378 BOE per day on \$43.23 per BOE operating netbacks for the second quarter ended June 30, 2011. Production averaged 417 BOE per day on \$27.23 per BOE operating netbacks for the nine months ended September 30, 2011 in Hamburg, down from 549 BOE per day on \$29.79 per BOE operating netbacks for the nine months ended September 30, 2010. The Hamburg area produced approximately 509 BOE per day on average in 2010 and 675 BOE per day on average in 2009. Production declines were primarily attributable to natural declines from a high rate gas well that Arcan drilled in 2009. Arcan is currently producing over 400 BOE per day net from this area. Arcan has not drilled any new wells in this area in 2011.

Arcan is assessing two to four in-fill development drilling opportunities for the Hamburg GG oil pool, and will evaluate this program as economic conditions warrant with longer-term plans calling for additional exploration tests based on 3D seismic. This area also provides potential for up-hole Duvernay, Bluesky and Montney natural gas targets.

McLeod, Alberta

Arcan's McLeod property is characterized by medium-risk, multi-zone liquids rich natural gas targets largely in Mannville Group and Jurassic-aged strata at depths of 1,800 to 2,200 metres. Arcan has drilled seven (5.2 net) Gething natural gas wells to date with 90 percent success at McLeod. These wells produced approximately 54 BOE per day on average in the third quarter of 2011, 27 BOE per day on average for the second quarter of 2011, 86 BOE per day on average in 2010, and 75 BOE per day on average in 2009. Declining production is due to the normal declines of natural gas wells. The Corporation has reduced capital allocations to this area as natural gas prices have remained weak compared to oil prices. Arcan has not drilled any new wells in this area in 2011.

StimSol Canada Inc.

On September 13, 2011, Arcan acquired all of the issued and outstanding shares of StimSol, a private fracturing and stimulation services company based in Calgary, Alberta with services across Western Canada. Total cash consideration for the StimSol Acquisition was \$24.0 million. Incorporated in 1999, StimSol has a full suite of stimulation services including acidizing chemicals and pumping, solvent blends and pumping, and a complete package of specialty programs. StimSol also has an exclusive ten year distribution license for a hydrochloric acid blend called "Stim 28" that Arcan has found to be effective in Arcan's Swan Hills multi-stage fractures. Arcan believes that fracture acid will be in critical demand as it drills through the fourth quarter of 2011 and into 2012. Arcan acquired StimSol as part of its strategy to secure an acid supply and blend which will assist in the development of its Swan Hills properties, as well as potentially marketing "Stim 28" to other operators in the area.

Employees

As at September 30, 2011, Arcan had 23 full-time office employees and five full-time operating employees.

Results of Operations

Exploration and Production Results of Operations

Production Volumes

	Three Months Ended			Nine Months Ended		
	September 30, 2011	September 30, 2010	Change (%)	September 30, 2011	September 30, 2010	Change (%)
Oil and NGLs (bbls per day)	3,477	2,523	38	2,858	1,785	60
Natural gas (Mcf per day)	1,242	1,301	(5)	1,090	1,619	(33)
Total oil equivalent (BOE per day)	3,684	2,740	34	3,040	2,055	48
Oil as a percent of total volumes	94	92	2	94	87	8

Arcan's average production rate for the third quarter of 2011 was 3,684 BOE per day, a 34 percent increase from the third quarter of 2010 average of 2,740 BOE per day and a 28 percent increase over the second quarter 2011 average of 2,871 BOE per day. Oil production increases in the three and nine months ended September 30, 2011 more than offset natural gas declines, as compared to the three and nine months ended September 30, 2010. Arcan's average production rate for the first nine months of 2011 was 3,040 BOE per day, a 48 percent increase from the first nine months of 2010 average of 2,055 BOE per day. Production was higher in the 2011 periods over the 2010 periods primarily due to the additional volumes from the horizontal wells that Arcan drilled in the Swan Hills area during the period. Natural gas production volumes continued to decrease due to normal declines of natural gas wells and as capital was deployed away from natural gas towards oil production.

Production was higher in the third quarter of 2011, compared to the second quarter of 2011 due to additional volumes from new horizontal wells coming on production during the third quarter. Arcan also faced non-operated pipeline failures in the third quarter of 2011 with one failure affecting its Hamburg production and another major pipeline affecting its entire Swan Hills area. These failures, forest fires and wet weather affected many industry producers and prevented the Corporation from realizing the production targets for the third quarter of 2011 that it had anticipated. Fortunately the affected pipelines are oil transportation pipelines which, unlike natural gas pipelines (which can cause production shut-ins due to flaring restrictions), allow Arcan to truck its production rather than requiring it to be shut-in. Based on the production impacts from such challenging external events in the first nine months of 2011, Arcan now estimates it will have an annual average of 3,500 BOE per day versus its original estimate of 4,000 BOE per day. However, in spite of these external factors, the Corporation is already approaching its 2011 elevated exit rate target of 6,000 BOE per day.

Fracturing and Stimulation Results of Operations

Arcan acquired StimSol on September 13, 2011. As a result, only 17 days of StimSol's operations have been accounted for in Arcan's third quarter results. During the 17 days the fracturing and stimulation services revenues totalled \$0.6 million before intercompany eliminating entries, with cost of sales for fracturing and stimulation services totalling \$0.8 million, leaving a negative operating netback for the segment of \$0.2 million. Due to the short time period of operations Arcan believes that the current quarter results are not representative of future operating netbacks for the fracturing and stimulation segment and estimates that the segment will show a positive operating netback in future periods. There are no comparative prior periods as the StimSol Acquisition was completed in the current quarter.

Netbacks

The Corporation considers corporate netbacks to be a good indicator of its ability to produce oil and natural gas and sell fracturing and stimulation products and services profitably and to earn a return on capital invested. Netbacks are one of the Corporation's three possible sources of funding, the others being debt and new equity. Arcan's exploration and production netbacks for the third quarter of 2011 were higher than the third quarter of 2010 due to a 23 percent increase in commodity prices and the 34 percent increase in the Corporation's production rates. Commodity price increases for Arcan of 22 percent on oil were only slightly offset by an eight percent decrease on natural gas. These results are consistent with the Edmonton Par price increase from an average of \$73.51 per bbl for the third quarter of 2010 to an average of \$92.58 per bbl for the third quarter of 2011 and Arcan's low weighting to natural gas.

Netbacks

	Three Months Ended			Nine Months Ended		
	September 30, 2011	September 30, 2010	Change (%)	September 30, 2011	September 30, 2010	Change (%)
\$ thousands						
Petroleum and natural gas revenue	28,370	17,107	66	71,890	37,155	93
Royalties	(5,489)	(4,017)	37	(14,185)	(8,861)	60
Production and operating expenses	(8,245)	(3,012)	174	(18,605)	(7,543)	147
Exploration and production operating netbacks	14,636	10,078	45	39,100	20,751	88
Fracturing and stimulation services revenue	351	-	-	351	-	-
Cost of sales for fracturing and stimulation services	778	-	-	778	-	-
Fracturing and stimulation operating netbacks	(427)	-	-	(427)	-	-
Consolidated operating netbacks	14,209	10,078	41	38,673	20,751	86
Other revenue	4	-	-	116	4	2800
Realized economic hedging loss	-	-	-	(350)	-	-
G&A - cash	(2,054)	(1,890)	9	(4,964)	(4,467)	11
Finance expenses - cash	(1,453)	(522)	178	(3,651)	(1,274)	186
Corporate netbacks	10,706	7,666	40	29,824	15,014	99

Netbacks

	Three Months Ended			Nine Months Ended		
	September 30, 2011	September 30, 2010	Change (%)	September 30, 2011	September 30, 2010	Change (%)
\$ thousands						
Netbacks - \$ per BOE						
Petroleum and natural gas revenue	83.70	67.87	23	86.63	66.23	31
Royalties	(16.20)	(15.94)	2	(17.09)	(15.80)	8
Production and operating expenses	(24.33)	(11.95)	104	(22.42)	(13.44)	67
Exploration and production operating netbacks	43.17	39.98	8	47.12	36.99	27
Fracturing and stimulation services revenue	1.03	-	-	0.42	-	-
Cost of sales for fracturing and stimulation services	(2.30)	-	-	(0.94)	-	-
Fracturing and stimulation operating netbacks	(1.27)	-	-	(0.52)	-	-
Consolidated operating netbacks	41.90	39.98	5	46.60	36.99	26
Other revenue	0.01	-	-	0.14	-	-
Realized economic hedging loss	-	-	-	(0.42)	-	-
G&A - cash	(6.06)	(7.50)	(19)	(5.98)	(7.96)	(25)
Finance expenses - cash	(4.29)	(2.07)	107	(4.40)	(2.27)	94
Corporate netbacks	31.56	30.41	4	35.94	26.76	34

Arcan's exploration and production operating netback, defined as revenue, less royalties and operating expenses, was \$14.6 million in the third quarter of 2011 up from \$10.1 million recorded in the third quarter of 2010 and up from \$14.4 million in the second quarter of 2011. The increase in operating netback for the third quarter of 2011 versus the third quarter of 2010 was based on a 34 percent increase in production volumes and a 23 percent increase in combined prices leading to a 66 percent increase in revenues, partially offset by increases in royalties and operating costs. Arcan's operating netback was up from \$14.4 million in the second quarter of 2011 due to a 28 percent production volume increase offset by a 13 percent decrease in prices leading to a 13 percent increase in revenues, partially offset by increases in royalties and operating costs.

Arcan's operating netback was \$39.1 million for the first nine months of 2011, up from \$20.8 million in the first nine months of 2010. The increase was due to higher revenue which resulted from an increase of 48 percent on production volumes from the Corporation's horizontal well drilling over the period combined with price increases. The increased revenue was offset by higher royalties and operating costs.

Arcan's exploration and production operating netback on a per BOE basis was \$43.17 in the third quarter of 2011, representing an eight percent increase from \$39.98 recorded in the third quarter of 2010. The increase in operating netback was due to higher oil volumes from the new horizontal Swan Hills wells and increased oil prices in the third quarter of 2011, compared to the same period of 2010. Operating netbacks per BOE were down 22 percent from the second quarter of 2011 which was \$55.29 per BOE. This decrease in the operating netback per BOE from the second quarter of 2011 was due to a 13 percent decrease in product prices combined with increased production and operating costs offset slightly by

lower royalties. Arcan's exploration and production operating netback on a per BOE basis increased to \$47.12 for the first nine months of 2011, compared to \$36.99 for the first nine months of 2010. The increase is due to higher pricing offset slightly by increased royalties and operating costs. The move to oil weighting has continued to assist Arcan's exposure to price upside in the last few years which is expected to continue through 2011; however, oil properties present additional operating costs that can be higher on a BOE basis than those for natural gas properties in the early stages of a waterflood. The net effect to Arcan was higher netbacks from oil in 2011 than would have been achieved through natural gas.

Operating netbacks from oil were \$43.85 per BOE and from natural gas were (\$1.28) per BOE in the third quarter of 2011 versus \$41.16 for oil and (\$0.27) for natural gas in the third quarter of 2010 and compared to the \$55.62 per BOE from oil and the \$20.94 per BOE from natural gas in the second quarter of 2011. Operating netbacks from oil were \$47.68 per BOE and from natural gas were \$8.66 per BOE in the first nine months of 2011 versus \$38.22 for oil and \$13.85 for natural gas in the first nine months of 2010. Arcan's oil netbacks have been stronger than its natural gas netbacks for all periods since 2007 due primarily to commodity pricing.

Arcan's corporate netback, defined as consolidated operating netbacks, plus other revenue, less realized economic hedging losses, Cash G&A expense and the cash interest expense portion of finance expenses, was up to \$10.7 million in the third quarter of 2011, as compared to \$7.7 million in the third quarter of 2010 due primarily to higher volumes and prices. The Corporation's corporate netbacks were also up from the \$10.3 million in the second quarter of 2011 due primarily to volume increases. On a per BOE basis, Arcan's corporate netback was \$31.56 in the third quarter of 2011, compared to \$30.41 in the third quarter of 2010 and \$39.24 in the second quarter of 2011. Arcan's corporate netback increased to \$29.8 million or \$35.94 per BOE for the first nine months of 2011 from \$15.0 million or \$26.76 per BOE for the first nine months of 2010. Changes in netbacks and the components thereof are detailed by category in the above table.

Operation details by area for the three months ended September 30, 2011 and 2010 are as follows:

Exploration and Production Operating Netbacks by Area

Area	Three Months ended September 30, 2011			Three Months ended September 30, 2010		
	Swan Hills	Hamburg	McLeod	Swan Hills	Hamburg	McLeod
Daily Production (BOE per day)	3,220	410	54	2,205	456	78
Revenue (\$/BOE)	85.74	76.75	15.37	71.26	57.76	31.15
Royalties (\$/BOE)	16.19	18.10	1.78	15.73	19.07	3.37
Operating Costs (\$/BOE)	21.61	46.85	14.87	11.85	9.68	28.05
Operating Netbacks (\$/BOE)	47.94	11.80	(1.28)	43.67	29.01	(0.27)

Arcan has focused on its oil properties since 2007, as netbacks from its oil properties have provided higher margins than those from its natural gas properties.

Revenues

Exploration and Production Revenue and Realized Prices

(\$000's)	Three Months Ended			Nine Months Ended		
	September 30, 2011	September 30, 2010	Change (%)	September 30, 2011	September 30, 2010	Change (%)
Oil and NGL	27,930	16,607	68	70,648	34,941	102
Natural gas	440	500	(12)	1,242	2,214	(44)
Total petroleum and natural gas revenue	28,370	17,107	66	71,890	37,155	93
\$ per BOE						
Oil and NGL (per bbl)	87.31	71.55	22	90.55	71.70	26
Natural gas (per Mcf)	3.85	4.18	(8)	4.17	5.01	(17)
Total petroleum and natural gas revenue (per BOE)	83.70	67.87	23	86.63	66.23	31
Benchmarks						
WTI (U.S.\$ per bbl)	89.51	76.09	18	95.42	77.58	23
Edmonton Light Sweet (Cdn.\$ per bbl)	92.58	73.51	26	94.43	76.32	24
Alberta Plant Gate (per Mcf)	3.53	3.41	4	3.64	3.97	(8)
Cdn\$ per U.S.\$	1.02	.9624	6	1.02	.9655	6

Arcan posted higher exploration and production revenues for the quarter ended September 30, 2011 than those experienced in the quarter ended September 30, 2010. A 34 percent increase in production volume combined with a 23 percent increase in prices resulted in an increase in revenue for the third quarter ended September 30, 2011, as compared to the third quarter ended September 30, 2010. Exploration and production revenues in the third quarter of 2011 increased, compared to the second quarter of 2011 due to increased production offsetting lower prices. Exploration and production revenues for the nine months ended September 30, 2011 increased to \$71.9 million from \$37.2 million for the same period of 2010 due to increased production volumes and pricing. Based on estimated production volumes and prices and new well completions, Arcan expects to have stronger exploration and production revenues in the fourth quarter of 2011. The Corporation expects ongoing improvements in production volumes for the balance of 2011, and anticipates that overall production in 2012 will be higher than 2011.

Commodity Prices

Arcan's third quarter of 2011 oil production revenue continued to grow as a percentage of its total exploration and production revenues currently weighted 98 percent towards light oil. The average price for West Texas Intermediate ("WTI") increased 18 percent in the third quarter of 2011 versus the same quarter in 2010, increased 23 percent in the first nine months of 2011 versus the same period in 2010 and decreased 12 percent over the second quarter ended June 30, 2011. Meanwhile, the Edmonton Light Sweet price has increased 26 percent in the third quarter of 2011, as compared to the same quarter in 2010, increased 24 percent in the first nine months of 2011 versus the same period in 2010 and decreased nine percent over the second quarter ended June 30, 2011. Stronger increases in the Edmonton Light Sweet prices versus the WTI price increases are due to the impact of the weakening U.S. currency against the Canadian dollar over the past year.

In the third quarter of 2011, Arcan realized average revenue per BOE of \$83.70, compared to \$67.87 recorded in the third quarter of 2010 and \$96.49 in the second quarter of 2011. Arcan realized average revenue per BOE of \$86.63 for the first nine months of 2011, compared to \$66.23 for the same period in 2010. Arcan received an average of \$87.31 per bbl of oil and natural gas liquids in the third quarter of 2011, an increase from \$71.55 per bbl realized in the third quarter of 2010 and down from the \$101.10 per bbl received in the second quarter of 2011. Arcan received an average of \$90.55 per bbl of oil and natural gas liquids in the first nine months of 2011, an increase from \$71.70 per bbl realized in same period of 2010. The increase in Arcan's oil price for the three and nine months ended September 30, 2011, compared to the same periods in 2010 is consistent with the increase in the Edmonton Light Sweet price for the same periods, as is the change from the second quarter of 2011.

The Corporation realized an average natural gas price of \$3.85 per thousand cubic feet ("Mcf") in the third quarter of 2011, a eight percent decrease from the \$4.18 per Mcf averaged in the third quarter of 2010 and a decrease from the \$4.34 per Mcf received in the second quarter of 2011. Arcan realized an average natural gas price of \$4.17 per Mcf in the first nine months of 2011, compared to \$5.01 per Mcf in the first nine months of 2010. This is consistent with the price changes at the Alberta Plant Gate for the same periods. Arcan anticipates that oil prices will remain in the range of U.S.\$75.00 to U.S.\$125.00 WTI for 2012 due to political issues in the Middle East and uncertainty with respect to global economic growth, and that gas prices will remain at 2011 price levels through 2012.

Royalties Expense

	Three Months Ended			Nine Months Ended		
	September 30, 2011	September 30, 2010	Change (%)	September 30, 2011	September 30, 2010	Change (%)
Total (\$000s)	5,489	4,017	37	14,185	8,861	60
Percent of revenue	19	23	(17)	20	24	(17)
Per BOE (\$)	16.20	15.94	2	17.09	15.80	8

The Corporation's royalty expense in the third quarter of 2011 was \$5.5 million, as compared to \$4.0 million in the third quarter of 2010 and to \$4.9 million in the second quarter of 2011. Royalties for the nine months ended September 30, 2011 increased to \$14.2 million from \$8.9 million for the first nine months of 2010. The increase in Arcan's gross royalty amounts, for the three and nine month periods ended September 30, 2011, compared to the same periods in 2010 and for the third quarter of 2011 versus the second quarter of 2011, is primarily the result of increased revenues based on higher commodity prices and production volumes. On a per BOE basis, royalties increased due to higher product pricing. Arcan's royalties are currently decreasing on a percentage of revenue basis due to new wells experiencing a five percent royalty rate for the first 50,000 to 100,000 BOE of production.

Royalty rates fluctuate with the price of oil and gas, as well as when higher rates of production are experienced. There have been a number of changes to royalty rates in the last few years; however, the largest impact is the allowance of a five percent royalty applied up to the first 90,000 bbls of production on wells that Arcan is drilling in the Swan Hills area. Accordingly, Arcan anticipates its royalty rates for 2011 to be 20 percent to 30 percent of revenue depending on drilling activity, production volumes, and prices.

Production and Operating Expenses (including transportation)

	Three Months Ended			Nine Months Ended		
	September 30, 2011	September 30, 2010	Change (%)	September 30, 2011	September 30, 2010	Change (%)
Total (\$000s)	8,245	3,012	174	18,605	7,543	147
Per BOE (\$)	24.33	11.95	104	22.42	13.44	67

In the third quarter of 2011, Arcan incurred operating expenses of \$24.33 per BOE or \$8.2 million, up from the \$11.95 per BOE or \$3.0 million in the third quarter of 2010 and \$22.55 per BOE or \$5.9 million recorded in the second quarter of 2011. For the nine months ended September 30, 2011 operating expenses increased to \$22.42 per BOE or \$18.6 million from \$13.44 per BOE or \$7.5 million for the same period in 2010. A significant portion of the overall increase in operating expenses, on an overall and a per BOE basis, over the three and nine months ended September 30, 2010 related to oil trucking charges, Arcan's well work-overs and pump replacements that were required to remedy production declines, as well as higher snow volumes, higher rainfall and the forest fires in the first nine months of 2011. In addition, with the non-operated pipeline failures experienced this year, Arcan has been trucking a significant portion of its production which has added considerably to its operating costs on an overall and per BOE basis.

Going forward, Arcan's continued transition towards oil-weighted production, including costs to operate EOR, is anticipated to result in \$10.00 to \$15.00 per BOE average operating costs per unit of production, after the short term third party pipeline issues have been resolved.

Realized and Unrealized Losses on Commodity Contracts and Financial Instruments

	Three Months Ended			Nine Months Ended		
	September 30, 2011	September 30, 2010	Change (%)	September 30, 2011	September 30, 2010	Change (%)
Realized loss (\$000's)	-	-	-	(350)	-	-
Per BOE (\$)	-	-	-	0.42	-	-
Unrealized gain (loss) (\$000's)	2,547	(1,018)	(350)	4,341	(1,018)	(526)
Per BOE (\$)	7.52	(4.04)	(286)	5.23	(1.82)	(387)

Periodically, Arcan utilizes economic hedges to protect a portion of its cash flows. The Corporation has hedged 2,000 bbls per day from January 1, 2011 to December 31, 2011 by purchasing Canadian dollar WTI put contracts establishing a \$70.00 floor. As payment Arcan sold four 500 bbls per day Canadian dollar WTI call contracts, two of which are priced at \$100.00, one is priced at \$100.05 and the last is priced at \$100.30. Arcan also has hedged 1,000 bbls per day from January 1, 2012 to December 31, 2012 by purchasing Canadian dollar WTI put contracts establishing a \$75.00 floor. As payment, Arcan sold two 500 bbls per day Canadian dollar WTI call contracts, one of which was priced at \$126.00 and the other was priced at \$127.50. Arcan recognized gain of \$2.5 million during the quarter related to these contracts. Arcan recognized a realized loss of \$0.4 million and an unrealized gain of \$4.3 million during the first nine months of 2011 related to these contracts. The Corporation will mark-to-market these contracts at the end of each quarter with realized and/or unrealized gain or losses, if any, recorded in the statement of income for each reporting period, using the price curve for that instrument on the last day of that month and comparing it to the price curve on the day the hedge was acquired. There were no hedging contracts for 2010 production volumes. All hedges are approved by the Board of Directors of Arcan.

Subsequent to the end of the period, the Corporation entered into additional financial oil contracts. The Corporation has entered into two fixed price swap contracts each for 500 bbls per day, whereby the Corporation will receive a fixed price of \$95.00 per bbl in exchange for payment to the counter-party based on Canadian dollar WTI spot prices. The Corporation has also purchased two call arrangements each for 500 bbls per day, whereby, should the Canadian dollar WTI price exceed \$110.00 and \$115.00 per bbl, respectively, the Corporation would receive the difference from the counter-party. The contracts are for the period from January 1, 2012 to December 31, 2012. The Corporation also entered into a fixed price swap contract for 500 bbls per day, whereby the Corporation will receive a fixed price of \$90.00 per bbl in exchange for payment to the counter-party based on Canadian dollar WTI spot prices. The Corporation has also purchased a call arrangement for 500 bbls per day, whereby should the Canadian dollar WTI price exceed \$110.00 per bbl, the Corporation will receive the difference from the counter-party. This contract is for the period from January 1, 2013 to December 31, 2013.

Contract period	Pricing (Cdn\$ WTI)	Volume per day
January 2011 – December 2011	Collar \$70.00 floor – \$100.00 ceiling	1,000 bbls
January 2011 – December 2011	Collar \$70.00 floor – \$100.05 ceiling	500 bbls
January 2011 – December 2011	Collar \$70.00 floor – \$100.30 ceiling	500 bbls
January 2012 – December 2012	Collar \$75.00 floor – \$126.00 ceiling	500 bbls
January 2012 – December 2012	Collar \$75.00 floor – \$127.50 ceiling	500 bbls
January 2012 – December 2012	Sold Swap price of \$95.00 purchased \$115.00 call	500 bbls
January 2012 – December 2012	Sold Swap price of \$95.00 purchased \$110.00 call	500 bbls
January 2013 – December 2013	Sold Swap price of \$90.00 purchased \$110.00 call	500 bbls

The Corporation has assessed the sensitivity of the fair value of the oil commodity contracts to fluctuations in forward crude oil prices. As at September 30, 2011, if the forward price of crude had been \$1.00 higher, net income for the period would have been approximately \$0.4 million lower, due to a higher unrealized loss on the commodity contracts. An equal and opposite impact would have occurred to net income had the forward price of crude been \$1.00 lower.

Exploration and Evaluation Expenses

	Three Months Ended			Nine Months Ended		
	September 30, 2011	September 30, 2010	Change (%)	September 30, 2011	September 30, 2010	Change (%)
Total (\$000s)	55	407	(86)	58	2,646	(98)
Per BOE (\$)	0.16	1.61	(90)	0.07	4.72	(99)

Exploration and evaluation expenses relate to exploration and evaluation capital projects or undeveloped land that the Corporation has determined is no longer a viable capital project. This capital spending is expensed through the statement of income in the period that management determines the exploration and evaluation expenditures are no longer viable projects. In the third quarter of 2011, Arcan expensed \$0.1 million as exploration and evaluation expenses that related primarily to an undeveloped land expiry in its Hamburg area. In the first nine months of 2010 Arcan drilled an unsuccessful well and expensed \$2.6 million of exploration and evaluation assets. Arcan expects exploration and evaluation expenses to remain low for the remainder of the year as the Corporation anticipates the majority of its capital spending to relate to development property, plant and equipment.

Cash G&A Expenses

	Three Months Ended			Nine Months Ended		
	September 30, 2011	September 30, 2010	Change (%)	September 30, 2011	September 30, 2010	Change (%)
Total (\$000s)	2,054	1,890	9	4,964	4,467	11
Per BOE (\$)	6.06	7.50	(19)	5.98	7.96	(25)

Cash G&A expenses for the third quarter of 2011 decreased on a per BOE basis to \$6.06 per BOE from \$7.50 per BOE in the third quarter of 2010 and decreased from \$9.88 per BOE in the second quarter of 2011. The change year-over-year for the third quarter, on a per BOE basis, resulted from a 38 percent cost increase that was more than offset by an increase in recoveries associated with higher capital expenditure activities. Total Cash G&A expenses for the third quarter of 2011, net of recoveries of \$0.9 million, were \$2.1 million, compared to \$1.9 million in the third quarter of 2010 after recoveries of \$0.4 million. In the second quarter of 2011, Cash G&A expenses were \$2.6 million net of recoveries of \$0.3 million. Cash G&A expenses for the first nine months of 2011 decreased on a per BOE basis to \$5.98 per BOE from \$7.96 per BOE in the first nine months of 2010. Cash G&A expenses totalled \$5.0 million in the first nine months of 2011 versus the \$4.5 million for the first nine months of 2010. Arcan had 23 full-time office employees as at September 30, 2011, as compared to 15 employees as at September 30, 2010. The change year-over-year for the periods, was largely the result of higher salaries and wages due to more office staff, higher office rent, and costs associated with the purchase of StimSol.

Total Cash G&A expenses for three months ended September 30, 2011 of \$3.0 million, before recoveries, was mainly comprised of wages of \$0.7 million, bank fees of \$0.2 million, consulting fees of \$0.5 million, legal fees of \$0.4 million, and rent of \$0.3 million.

Arcan does not capitalize any Cash G&A expenses. In its role as operator of its oil and natural gas properties, the standard industry operating agreements provide for the charging of certain administrative costs to its joint venture capital expenditure programs and well operations. Arcan expects Cash G&A costs to grow marginally as Arcan continues to increase activity levels; however, per BOE numbers should decline as production volumes increase.

Finance Expenses

	Three Months Ended			Nine Months Ended		
	September 30, 2011	September 30, 2010	Change (%)	September 30, 2011	September 30, 2010	Change (%)
Convertible debenture interest	1,369	-	-	3,378	-	-
Bank debt interest	84	522	(84)	273	1,274	(79)
Accretion of convertible debenture liability	671	-	-	1,556	-	-
Accretion of decommissioning obligations	121	133	(9)	403	338	19
Total	2,245	655	243	5,610	1,612	248

Finance Expenses

(\$000s) (\$ per BOE)	Three Months Ended			Nine Months Ended		
	September 30, 2011	September 30, 2010	Change (%)	September 30, 2011	September 30, 2010	Change (%)
Convertible debenture interest	4.04	-	-	4.07	-	-
Bank debt interest	0.24	2.07	(88)	0.33	2.27	(85)
Accretion of convertible debenture liability	1.98	-	-	1.88	-	-
Accretion of decommissioning obligations	0.36	0.53	(32)	0.49	0.60	(18)
Total	6.62	2.60	155	6.77	2.87	136

Historically, Arcan's management has increased debt levels based on operational success and has subsequently reduced those debt levels through equity issuances. As Arcan's asset base has grown, its related borrowing capacity and ability to carry and service higher debt levels has increased. To provide stable and secure longer term financing, Arcan completed two offerings of convertible debentures (the "**Debentures**"). The first offering was in February 2011 for gross proceeds to Arcan of \$86.3 million. The second offering was in October 2011 for gross proceeds to Arcan of \$85.0 million (the "**October 2011 Offering**"). The October 2011 Offering was combined with an equity financing whereby Arcan issued 9.3 million shares at a price of \$5.45 per share for gross proceeds of \$50.8 million. The proceeds realized from Arcan's financing activities are in addition to Arcan's existing credit facility of \$120 million (the "**Credit Facility**"). Arcan expects that its debt to cash flow ratio in 2011 will be higher as it continues to grow its business and that its interest expense will increase as a result of the Debentures and increased debt levels.

Financing expenses in the third quarter of 2011 of \$2.2 million were 243 percent higher than \$0.7 million in the third quarter of 2010. Financing expenses in the first nine months of 2011 of \$5.6 million were 248 percent higher than \$1.6 million in the first nine months of 2010. The increase over both periods in 2011 from 2010 is due primarily to the interest and accretion related to the \$86.3 million aggregate amount of Debentures that Arcan issued in February 2011. Arcan also recorded higher accretion for the first nine months of 2011, compared to the same period in 2010, due to the increased decommissioning obligations related to its wells drilled and acquired in 2010 and the first nine months of 2011. Bank interest was \$0.1 million in the third quarter of 2011, compared to \$0.5 million in the same period of 2010 and was 79 percent lower in the first nine months of 2011, compared to the first nine months of 2010 due to Arcan's maintenance of lower average bank debt levels in 2011 (as a result of the additional funds received upon the issuance of the Debentures). The lower average bank debt levels were complemented by lower interest rates for the third quarter of 2011 versus the same period in 2010. Arcan had an effective interest rate of 4.00 percent on its Credit Facility at September 30, 2011 and 4.75 percent at September 30, 2010.

Financing expenses in the third quarter of 2011 were four percent higher than the \$2.1 million recognized in the second quarter of 2011. Arcan recorded slightly lower accretion of decommissioning obligations in the third quarter of 2011, compared to the second quarter of 2011. Bank interest was \$0.1 million in the third quarter of 2011, compared to nil in the

second quarter of 2011 due to Arcan's maintenance of lower average bank debt levels in the second quarter of 2011 (as a result of the additional funds received upon the issuance of the Debentures). Arcan experienced similar bank interest rates in the third quarter of 2011 as the second quarter of 2011.

The only financial covenant prescribed by the Credit Facility is that Arcan's combined debt and working capital cannot exceed \$120.0 million. There are no financial covenants associated with the Debentures. As at September 30, 2011, the Corporation was in compliance with its financial covenant under the Credit Facility.

Stock-Based Compensation Expense

	Three Months Ended			Nine Months Ended		
	September 30, 2011	September 30, 2010	Change (%)	September 30, 2011	September 30, 2010	Change (%)
Total (\$000's)	2,693	1,560	73	7,773	3,447	126
Per BOE (\$)	7.95	6.19	28	9.37	6.14	53

Stock-based compensation is a non-cash expense, which represents the estimated fair value of performance and other stock options granted to employees as a motivational incentive. Arcan expects that its stock-based compensation will increase as options that have been issued are expensed and new options are issued. This increase may be further magnified as a result of share price volatility.

Arcan recorded a stock-based compensation expense of \$2.7 million in the third quarter of 2011, calculated using the Black-Scholes option-pricing model. During the third quarter of 2011 Arcan granted 170,000 options, 10,000 options were exercised and Arcan cancelled 92,000 options that were forfeited. Arcan's stock-based compensation expense increased significantly for the third quarter and first nine months of 2011, compared to the same periods in 2010 due to the additional options granted in the last three quarters of 2010 and the first three quarters of 2011, and the escalated fair value of the new options due to the increase in Arcan's share trading price on the TSX Venture Exchange over that period. Stock-based compensation also increased in the third quarter of 2011, compared to the second quarter of 2011 due to options that were granted part way through the second quarter of 2011 and options granted in the third quarter of 2011.

Depletion and Depreciation ("D&D")

	Three Months Ended			Nine Months Ended		
	September 30, 2011	September 30, 2010	Change (%)	September 30, 2011	September 30, 2010	Change (%)
(\$000's except per BOE)	7,717	5,488	41	18,374	11,191	64
Depletion and depreciation Per BOE (\$)	22.77	21.77	5	22.14	19.95	11

Depletion is calculated for each component deemed to be an area based upon capital expenditures, production rates and Proved plus Probable reserves. Arcan recorded \$7.7 million or \$22.77 per BOE in D&D expense in the third quarter of 2011 based on production volumes of 338,922 BOE. The increase in D&D expense per BOE for the three and nine months ended September 30, 2011, as compared to the same periods in 2010 is due to acquisitions completed during 2010, including the acquisition of interests in 102 gross (81 net) sections of land with approximately 500 BOE per day of existing production for a cash

purchase price of \$52.8 million in March 2010 (the "**Land Acquisition**"), as well as an increase in capital intensity for reserves found in 2010. Also, capital spending in the last half of 2010 and the first nine months of 2011 on facilities and seismic has caused an increase in the depletion rate. The increase in D&D expense as compared to the second quarter of 2011 is due to increased production in the third quarter, compared to the second quarter. The slight increase in the depletion rate per BOE in the third quarter, compared to the second quarter is due to high capital spending on equipment and facilities in the third quarter of 2011. Under IFRS, Arcan now uses Proved plus Probable reserves in its depletion calculations versus the use of Proved reserves under previous GAAP.

Arcan's D&D rate reflects proportionately higher cumulative capital expenditures, including significant facility and seismic investments and the Land Acquisition, relative to recognized reserves. Arcan's two main properties are in the early stages of enhanced recovery schemes and substantial amounts of capital have been invested in infrastructure and land. The Corporation expects to decrease its depletion per BOE in future years by adding reserves through a development program that has a lower capital intensity as a large portion of infrastructure investments have already been incurred.

The calculation of depletion includes estimated future development costs of \$411.0 million associated with the development of the Corporation's Proved plus Probable reserves and excludes salvage value of \$1.7 million.

Income Taxes - Deferred tax (expense) reduction

	Three Months Ended			Nine Months Ended		
	September 30, 2011	September 30, 2010	Change (%)	September 30, 2011	September 30, 2010	Change (%)
Total (\$000's)	(1,224)	226	(641)	(3,522)	158	(2,329)
Per BOE (\$)	(3.61)	0.90	(501)	(4.24)	0.28	(1,614)

A deferred tax expense of approximately \$1.2 million has been recognized in the third quarter of 2011, which relates to the Corporation experiencing pre-tax income of \$2.0 million for the quarter. The provision for income taxes differs from the amount obtained by applying the combined federal and provincial income tax rate for 2011, which was 26.5 percent and is calculated on income before income taxes. The difference is primarily due to non-deductible stock-based compensation and future tax rate differences.

The deferred income tax liability on Arcan's statement of financial position increased by \$8.2 million in the first nine months of 2011 due to a \$2.7 million liability being booked on the equity component of the Debentures, \$2.0 million being booked on the StimSol Acquisition, and \$3.5 million being booked as a deferred tax expense based on Arcan's nine months ended September 30, 2011 pre-tax income of \$6.0 million.

Arcan has not paid any cash taxes since inception and has accumulated sufficient tax deductions such that it does not anticipate paying any taxes for 2011. However, Arcan is not able to forecast future possible changes in federal and provincial tax regimes. Arcan estimates its tax pools as follows:

Estimated Tax Pools

(\$ millions)

Type	September 30, 2011	Rate of Claim (%)
Canadian exploration expense	20.4	100
Non-capital losses	94.7	100
Canadian development expense	116.2	30
Undepreciated capital costs	63.5	20 - 100
Share issue	6.7	20
Canadian oil and natural gas property expense	53.5	10
Total	355.0	

With estimated capital spending in 2011 and 2012, Arcan does not believe it will be in a taxable position until late 2013 at the earliest. Arcan does not have a tax partnership in place.

Net Income (Loss), Funds From Operations and Cash Flow From Operating Activities

(\$000's except per share)	Three Months Ended			Nine Months Ended		
	September 30, 2011	September 30, 2010	Change (%)	September 30, 2011	September 30, 2010	Change (%)
Net income (loss)	776	(1,988)	(139)	2,483	(4,742)	(152)
Per share – basic and diluted	0.01	(0.03)	(133)	0.03	(0.07)	143
Funds from operations	10,490	7,653	37	29,484	14,981	97
Per share – basic and diluted	0.12	0.10	20	0.33	0.23	43
Cash flow from operating activities	10,469	5,372	95	29,538	11,589	155
Per share – basic and diluted	0.12	0.07	71	0.33	0.17	94

Arcan is generating funds from the operations of its three properties. Net income has been realized in the third quarter of 2011 as higher commodity prices and volumes combined with an unrealized gain on commodity contracts and decreased exploration and evaluation impairments were somewhat offset by higher royalties and operating costs as well as non-cash items such as stock-based compensation and depletion and depreciation and accretion charges. As Arcan continues to develop its properties, it anticipates that additional revenues will be generated resulting in additional funds from operations as well as additional net earnings.

Summary of Quarterly Operating and Financial Results for the Eight Most Recent Quarters

Fiscal quarter ended (\$000's, except per share amounts)	2011			2010			2009 ⁽¹⁾	
	Sept.	June	March	Dec.	Sept.	June	March	Dec.
Total revenue ⁽²⁾	28,721	25,214	18,306	18,420	17,107	11,056	8,992	7,804
Net income (loss)	776	4,267	(2,560)	(2,377)	(1,988)	(627)	(2,127)	(1,730)
Net income (loss) per share – basic	0.01	0.05	(0.03)	(0.03)	(0.03)	(0.01)	(0.04)	(0.04)
Net income (loss) per share – diluted	0.01	0.05	(0.03)	(0.03)	(0.03)	(0.01)	(0.04)	(0.04)

Notes:

- (1) Arcan's IFRS transition date was January 1, 2010, therefore 2009 comparative information has not been restated.
- (2) Total revenue includes petroleum and natural gas revenue and fracturing and stimulation services revenue.

Total revenue has moved in an upward direction over the most recent eight quarters due primarily to ongoing light oil volume increases as a result of ongoing horizontal multi-stage fracture drilling operations in the Corporation's Swan Hills core area.

Liquidity and Capital Resources

Arcan spent \$86.7 million of capital on its properties during the three months ended September 30, 2011, up from \$28.4 million for the three months ended September 30, 2010. For the nine months ended September 30, 2011 Arcan spent \$159.1 million of capital, up from \$120.5 million spent in the first nine months of 2010. The increase in capital expenditures for the nine months ended September 30, 2011 versus the same period in 2010 is primarily due to significantly increased drilling levels and the StimSol Acquisition in 2011 versus the closing of the Land Acquisition in the second quarter of 2010. Arcan generated \$29.5 million in funds from operations in the first nine months of 2011, raised \$86.3 million through the issuance of the Debentures and as at September 30, 2011, \$44.0 million was drawn on its Credit Facility and Arcan had a working capital deficit of \$163.0 million, including bank debt and convertible debt. Subsequent to the end of the quarter Arcan issued \$85.0 million in Debentures and raised \$50.8 million of additional equity. With its solid asset base Arcan estimates that it has the ability to generate short-term and long-term cash flow to meet obligations as they become due. Arcan's management increased debt levels from the second quarter of 2011 through increased capital expenditures in the third quarter of 2011. Arcan's September 30, 2011 funds from operations (based on annualized third quarter 2011 funds from operations) to net debt ratio was 3.9 to one. The Corporation expects the ratio will remain elevated, including the Debentures, but will be under one to one in bank debt alone.

On February 14, 2011, Arcan issued \$75,000,000 aggregate amount of 6.25% Debentures and on February 22, 2011 issued an additional \$11,250,000 aggregate amount of 6.25% Debentures pursuant to the exercise of an over-allotment option by the underwriters. The 6.25% Debentures are convertible into shares at a price of \$8.75 per share and mature on February 28, 2016. On October 7, 2011, Arcan issued \$85,000,000 aggregate amount of 6.50% Debentures as well as \$50.8 million of equity at a price of \$5.45 per share. The 6.50% Debentures are convertible into shares at a price of \$8.75 per share and mature on October 31, 2018.

As at the date hereof, the Corporation has \$120.0 million available under its Credit Facility. The Credit Facility is comprised of a \$110.0 million syndicated revolving credit facility and a \$10.0 million revolving operating facility which is based on Arcan's reserves report for the period ended December 31, 2010. The Credit Facility has a revolving period of 364 days from the closing date and is extendible annually. If not extended, the Credit Facility will automatically convert to a one year non-revolving term loan. Arcan is currently in compliance with its financial covenant to keep debt and working capital under the \$120 million loan maximum and the renewal date for the Credit Facility is May 29, 2012. The Credit Facility is secured by a charge on all of Arcan's assets. As at the date hereof, the Credit Facility is undrawn with \$39.5 million of cash on hand. As well, Arcan has \$291.3 million in total credit capacity comprised of the \$120.0 million Credit Facility, the \$86.3 million in Debentures and the \$85.0 million in Debentures outstanding. Arcan estimates that

as at the date hereof, due to capital expenditures in the Swan Hills, the total net debt of its Debentures, debt and working capital deficiency is approximately \$175.0 million. Arcan estimates that it will have capital expended in excess of cash flow in the fourth quarter of 2011 and expects to have debt and working capital less than the bank loan limits throughout 2012. With the addition of the Debentures from the October 2011 Offering, Arcan expects that it will maintain a net debt and working capital deficiency position while its Debentures are outstanding.

Arcan was previously engaged in a substantial capital expenditure program to develop its Swan Hills core oil property. Arcan anticipates that current and future capital requirements will be funded through a combination of internal cash flow, debt and/or equity financing.

Arcan expects its capital expenditure program to total \$225.0 million for 2011 and that the total net debt of its Debentures, debt and working capital deficiency will be approximately \$185.0 million, providing Arcan with approximately \$105.0 million in available funds at the end of 2011. Capital expenditures in 2011 will be higher than in 2010 due to the substantial capital program in Arcan's Swan Hills area. Arcan expects expenditures for the remainder of 2011 and 2012 to be financed through its Credit Facility and available funds from operations. Additional equity may be available later if the condition of the equity markets permit; however, the Corporation does not currently forecast requiring such a cash in-flow to complete its capital program. Arcan has no fixed capital commitments and the capital program can be curtailed to ensure management of net debt levels. A number of factors and circumstances may impact Arcan's funds from operations and capital program. See the "Business Risks" section of this MD&A.

The components of Arcan's working capital deficiency are as follows:

(\$000's)	Quarter Ended September 30, 2011	Year Ended December 31, 2010
Current assets	22,404	17,138
Less:		
Accounts payable and accrued liabilities	68,106	45,500
Bank loan	43,990	20,823
Working capital (deficiency)	(89,692)	(49,185)
Debentures	73,318	-
Working capital (deficiency) including Debentures	(163,010)	(49,185)

Proforma, after taking effect of the October 7, 2011 financing, the working capital deficiency decreased from \$89.7 million to a working capital surplus of \$39.7 million and the working capital deficiency, including the Debentures decreased from \$163.0 million to \$118.6 million.

Capital Expenditure Summary				
(\$ millions)	Q3 2011	Q2 2011	Q1 2011	YTD September 30, 2011
Land and seismic	0.4	(1.2)	6.2	5.4
Drilling and intangibles	47.9	22.9	33.9	104.7
Corporate acquisition	21.1	-	-	21.1
Facilities and equipment	17.3	6.5	4.1	27.9
Total Capital – cash expended	86.7	28.2	44.2	159.1

Arcan's capital expenditures for the third quarter of 2011 were \$86.7 million focused primarily on drilling and completing horizontal wells in the Swan Hills area and the StimSol Acquisition. Arcan's capital spending in the third quarter was up from the \$28.4 million spent in the same period of 2010 due to an increased drilling and completions program in 2011 and the StimSol Acquisition. Capital spending for the first nine months of 2011 was up to \$159.1 million from \$120.5 million in the first nine months of 2010. The increase over the two nine month periods was due to the drilling and completing of horizontal wells in the Swan Hills area. Capital spending in the third quarter of 2011 increased from the \$28.2 million spent in the second quarter of 2011. This was due to increased drilling and completions occurring in the third quarter, compared to the second quarter of 2011 and the StimSol Acquisition which occurred in the third quarter.

During the three months ended September 30, 2011 Arcan spudded ten (9.6 net) successful horizontal multi-stage fracture wells on its Swan Hills play. Arcan has, as it did in 2010, budgeted capital expenditures to remain within cash flow and Credit Facility limitations for 2011. As at September 30, 2011 Arcan has entered into contracts to secure both trucking and fracturing services for a period of one year. The total commitment related to these contracts is \$5.9 million.

Liquidity risk related to financial instruments is the risk that the Corporation will not be able to meet its financial obligations as they come due. The Corporation's approach to managing liquidity is to ensure, as far as possible, that it will have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions without incurring unacceptable losses or risking harm to the Corporation's reputation.

2011 Drilling Activity (wells spudded)

2011	Exploration		Development		Total		Success Rate %	Working interest %
	Gross	Net	Gross	Net	Gross	Net		
Q1	0.0	0.0	4.0	3.6	4.0	3.6	100	90
Q2	0.0	0.0	7.0	7.0	7.0	7.0	100	100
Q3	0.0	0.0	10.0	9.6	10.0	9.6	100	96

Related Party Transactions

In conjunction with the Debenture issuance in February 2011, certain officers and directors acquired \$1,335,000 aggregate amount of Debentures.

In conjunction with the Debenture and equity issuance in October 2011, certain officers and directors acquired \$225,000 aggregate amount of Debentures as well as 129,100 shares at a price of \$5.45 per share.

Contractual Obligations

The Corporation has previously entered into, or is involved in, farm-in and/or farm-out agreements in the normal course of business in 2011. As of the date of this MD&A, Arcan has no farm-in and/or farm-out commitments.

Arcan has the following commitments:

Contractual Obligations (\$000's)	Total	Payments Due by Period			
		Less than 1 year	1 – 3 years	4 – 5 years	After 5 years
Debt	43,990	-	43,990	-	-
Finance Lease Obligations	-	-	-	-	-
Operating Leases	4,068	871	1,743	1,454	-
Purchase Obligations	5,842	5,842	-	-	-
Debenture Obligations	234,520	8,490	21,831	105,386	98,813
Total Contractual Obligations	244,430	15,203	23,574	106,840	98,813

Off-Balance Sheet Arrangements

There were no off-balance sheet obligations as at September 30, 2011.

Outstanding Share and Debenture Data

	As of November 24, 2011	Quarter Ended September 30, 2011	Quarter Ended September 30, 2010	Quarter Ended Dec. 31, 2010
Common shares	97,749	88,426	75,418	87,670
Warrants	-	-	124	-
Stock options	8,696	8,696	7,285	8,390
Debentures (face value)				
6.25% Maturing 2016	\$86,250	\$86,250	-	-
6.50% Maturing 2018	\$85,000	-	-	-

In the third quarter of 2011, Arcan's number of issued and outstanding shares increased by 10,000 shares as a result of employee and officer option exercises. The Corporation also issued 170,000 options to employees and officers, and cancelled 92,000 options during the quarter due to forfeitures.

In 2010, Arcan's number of issued and outstanding shares increased by 39.7 million shares. The number of issued and outstanding shares increased as a result of offerings of 26.0 million shares in March 2010 and 10.4 million shares in November 2010 and various warrant, option and performance share exercises throughout 2010 for an aggregate of 3.3 million shares. All warrants and performance shares outstanding at the end of 2009 were exercised or cancelled during 2010. The number of outstanding options changed primarily as a result of the issuance of 2.9 million options in the third quarter and the issuance of 2.9 million options in the fourth quarter of 2010 to officers, directors and employees of the Corporation.

Officers or directors of Arcan exercised 1.3 million options and sold the shares issued pursuant to such exercises during the year ended December 31, 2010. An officer of Arcan exercised 0.4 million options and sold the shares issued pursuant thereto in January 2011. Two officers and one employee of the Corporation exercised 0.8 million performance warrants prior to their expiry on March 1, 2010. During 2011 one officer exercised 0.4 million options, one director sold 2,000 shares, various officers and directors sold \$0.7 million in convertible Debentures, and various officers and directors purchased 0.2 million shares. Officers of the Corporation purchased \$1.3 million aggregate amount of Debentures in the February 2011 financing. Officers of the Corporation purchased \$0.2 million aggregate

amount of Debentures in the October 2011 Offering and \$0.1 million in the concurrent equity financing at \$5.45 per share.

Arcan has used the funds received from the November 2010 equity offering and the February 2011 Debenture offering to fund its drilling and waterflood activities in the Swan Hills light oil play as originally disclosed.

Outlook

The application of the horizontal multi-stage fractured wells to the Swan Hills reef property is changing Arcan's asset base. Drilling combined with water injection is expected to generate significantly increased production and recoveries, creating enhanced reserves and net asset value ("NAV"). With significant investments in infrastructure in place, Arcan now looks to continue to rapidly take advantage of its deep development inventory to continue to increase NAV per share through horizontal multi-stage acid fracture wells in the Swan Hills reef play. Arcan's plans for 2011 and beyond include:

- implementing a rigorous development schedule.
- significant expansion of drilling horizontal multi-stage fracture wells in the Swan Hills reef light oil play on its 171 net sections of land. Arcan also intends to increase and expand the existing water injection scheme;
- continued development and water injection in the Hamburg GG pool;
- ongoing review of opportunities at in the McLeod area; and
- evaluation of potential new core areas.

Arcan's 2011 capital program is expected to remain within cash flow, the proceeds from the Debenture issuances and expanded debt capacities and will continue to focus mainly on rapid growth in the Swan Hills area. Arcan is currently developing a strategy to best exploit its land base over the long term. The Corporation's strengths include over \$300.0 million of tax pools, a strong slate of directors, experienced staff, excess productive capacity for tie-in, recently initiated and growing waterfloods, new drilling plans and significant growth potential.

Industry Trends

There are a number of trends that have been developing in the oil and gas industry during the past several years that appear to be shaping the near future of the business.

The first trend currently affecting the oil and gas industry, as well as many other industries, is the impact on capital markets caused by investor uncertainty in the credit markets and the global economy through 2010 and into 2011. Global economics ultimately dictate commodity demand and therefore prices. Arcan realizes that it is dependent on price fluctuations as a price taker and therefore must maintain the financial flexibility to deal with uncertain commodity prices. The current optimistic nature of the oil and gas industry has

resulted in numerous opportunities for equity financings. Arcan has participated in these financings as it is unable to estimate the timing or magnitude of stock market corrections in the context of the evolving current global economic situation.

A second trend is the volatility of commodity prices. Crude oil is influenced by the world economy and the ability of the Organization of Petroleum Exporting Countries (OPEC) to adjust supply to world demand. Global concerns over currency, debt levels and political will-power in both the European Union and the United States dominate the demand side of the equation versus concerns over supplies from the Middle East and demands from growing economies such as China and India.

Natural gas is a commodity that has been strongly influenced by intensive shale gas drilling within North America, significant long term investments and commitments in energy from foreign state petroleum companies and producers drilling for liquids rich gas that remain economic in this pricing environment. In addition, North American fluctuations in supply, influenced by drilling activity, natural gas storage levels, imports continue to outweigh demand (which is impacted both by weather and by economic factors) and has resulted in dampened price of natural gas in Canada and the United States.

The impact on the oil and gas industry from commodity price volatility is significant. Historically, during periods of high prices, producers generated higher cash flows and conducted active exploration programs without external capital. Higher commodity prices frequently translate into very busy periods for service suppliers triggering premium costs for their services. Purchasing land and properties similarly increased in price during these periods. More recently rising oil prices has dramatically increased activity as producers have increased access to capital. With increased activity, the prices charged by the various service suppliers have and will continue to rise.

A third trend has been the rapid adoption of the use of horizontal drilling, employing multi-stage fracturing techniques for completions. Significant but less productive previously discovered oil and natural gas reservoirs in tight formations such as the Bakken, Montney, Doig, Cardium and the Beaverhill Lake are being revitalized based on the tremendous increases in productive rates. Arcan has been positively impacted by this trend in the drilling of its horizontal wells. Arcan plans to continue to develop and expand its current acreage and drilling inventory position

Arcan's need for capital will be 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, exploration and development of oil and natural gas properties requires substantial amounts of long-term capital. In addition to equity financing, Arcan uses several sources of financing, including internally generated cash flow, Debentures and bank debt. Current economic conditions including the variable global credit and equity markets have elevated the risks associated with this aspect of Arcan's business.

A fourth trend specifically impacting the Swan Hills is shortages of raw acid used in fracturing. Arcan identified early on that the significant increases in raw acid consumption could be a limiting factor in Swan Hills development. Arcan has been working on securing

alliances and supplies for most of 2011 and purchased StimSol to facilitate the vertical integration through the ultimate consumption of that acid. Arcan will continue to be a dominant user of raw acid through its development plans and will continue to work closely with its partners to secure acid as well as other required services.

A fifth trend, and one that will continue to garner heightened attention and consequently increased governmental intervention, is an increasing call for carbon capture due to greenhouse gas emissions. Capital requirements to meet emission standards are potentially enormous and are directly impacted by events such as the Kyoto Protocol. Arcan realizes that it will be required to meet governmental standards as they are introduced and must maintain the financial flexibility to do so. A longer term advantage may be derived from the waterflood activities and related increased recoveries in the Swan Hills property, as Arcan is likely a leading candidate for CO₂ flooding.

Business Risks

Arcan is engaged in the business of exploration, development, production and acquisition of crude oil and natural gas. This business has many risks that even a combination of knowledge, experience and careful evaluation may not be able to overcome. These risks may cause Arcan's actual performance and financial results in future periods to differ materially from any estimates or projections of future performance or results expressed or implied by forward-looking information in this MD&A. For a comprehensive discussion of the risk factors affecting Arcan and its business and operations, readers are encouraged to review the risks covered in Arcan's AIF under the heading "Risk Factors", which risk factors are incorporated by reference herein.

Arcan's principal business risks are related to finding and developing economic hydrocarbon reserves efficiently and its ability to fund the capital expenditure program. Without the ongoing addition of new oil and natural gas reserves, any existing reserves Arcan has, and the production therefrom, will decline over time as the existing reserves are produced. A future increase in Arcan's reserves will depend not only on Arcan's ability to explore and develop any properties it has, but also on its ability to 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 Arcan.

In addition to the risks outlined above with respect to commodity prices, financial risks associated with the petroleum industry include fluctuations in interest rates, and currency exchange rates. Arcan may use hedging instruments to manage these risks at the direction and under the supervision of the Board of Directors.

Operational risks faced by Arcan include competition, environmental factors, reservoir performance uncertainties, a complex regulatory and taxation environment and safety concerns.

StimSol's operations are subject to hazards inherent in the oil and gas service industry, such as equipment defects, damage, loss, malfunctions and failures, and natural disasters which may result in fires, vehicle accidents, explosions and uncontrollable flows of natural gas or

well fluids that can cause personal injury, loss of life, suspension of operations, damage to formations, damage to facilities, business interruptions, and damage to or destruction of property and equipment. These hazards could expose StimSol, and consequently Arcan, to liability for personal injury, wrongful death, property damage and other environmental damages. Arcan will be continuously monitoring StimSol's activities for quality control and safety and will maintain insurance coverage it believes to be adequate and customary in the industry. However, such insurance may not be adequate to cover StimSol's liabilities and may not be available in the future at rates Arcan considers reasonable and commercially justifiable. If StimSol were to incur substantial liability and such damages were not covered by insurance or were in excess of policy limits, or if StimSol were to incur such liability at a time when it is not able to obtain liability insurance, Arcan's business, financial condition, results of operations and cash flow could be materially adversely affected.

Compliance with various environmental laws, rules legislation and guidelines could impose greater costs on StimSol's business than are currently anticipated. The various environmental laws and regulations applicable to StimSol primarily govern the manufacture, processing, importation, transportation, handling and disposal of certain materials used in StimSol's operations and may require extensive remediation or impose civil or criminal liability for violations. StimSol is subject to increasingly stringent environmental laws and regulations, some of which may provide for strict liability for damages to natural resources or threats to public health or safety. While Arcan maintains liability insurance for StimSol, the insurance is subject to coverage limits and may exclude coverage for damage resulting from environmental contamination. There can be no assurance that insurance will continue to be available to Arcan on commercially reasonable terms, that the possible types of environmental liability will be covered by insurance or that the dollar amount of such liabilities will not exceed Arcan's policy limits. Even a partially insured claim, if successful and of sufficient magnitude, could have a material adverse effect on Arcan's business, results of operations and prospects. Further to this, stringent regulation of fracturing services could have a material adverse impact on StimSol and consequently, the financial position and operating results of Arcan.

The supply of service and production equipment at competitive prices is critical to the ability to add reserves at a competitive cost and produce the reserves in an economic and timely fashion. In periods of increased activity, these services and supplies can become difficult to obtain. Arcan attempts to mitigate this risk by developing strong long-term relationships with suppliers and contractors, and by maintaining an appropriate inventory of production equipment.

Arcan's longest producing Swan Hills horizontal well has been on-stream since February 23, 2010. This limited time frame for data creates risks for unexpected production profiles.

Arcan attempts to manage its business risks. Firstly, Arcan has an experienced, talented, and highly motivated staff of oil and natural gas professionals. Arcan also operates almost all of its properties. This enables Arcan to control the timing, direction and costs related to exploration and development opportunities. Arcan's geological focus is on areas in which the prospects are well understood by management. Technological tools are regularly used to reduce risk and increase the probability of success. Arcan closely follows all government

regulations and has an up-to-date emergency response plan that has been communicated to field operations by management. Arcan also carries insurance coverage to attempt to minimize potential losses.

Application of Critical Accounting Estimates

The significant accounting policies used by Arcan are disclosed in Note 3 to the unaudited interim consolidated financial statements for the periods ended September 30, 2011 and 2010. Certain accounting policies require that management make appropriate decisions with respect to the formulation of estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Management reviews its estimates on a regular basis. The emergence of new information and changed circumstances may result in actual results or changes to estimate amounts that differ materially from current estimates. The following discussion identifies the accounting policies and practices of the Corporation and is intended to assist readers in determining the likelihood of materially different results being reported by Arcan.

Accounting Policies

International Financial Reporting Standards

On January 1, 2011, IFRS became the generally accepted accounting principles in Canada for profit-oriented publicly accountable enterprises and Arcan adopted IFRS for financial reporting purposes, using a transition date of January 1, 2010. The adoption of IFRS required the restatement of comparative amounts reported by Arcan for the nine months ended September 30, 2010, the year ended December 31, 2010, as well as the presentation of an opening balance sheet as at January 1, 2010. As a result, the Corporation's financial results for the quarter and nine months ended September 30, 2011 and comparative periods are reported under IFRS while selected historical data prior to January 1, 2010 continues to be reported under former GAAP.

While the adoption of IFRS did not have a material impact on reported net cash flows, it did have a material impact on certain accounting policies, and Arcan's reported financial position and results of operations. None of the changes have led to any technical violations of the Credit Facility. The most significant areas of impact for Arcan include property, plant and equipment, decommissioning obligations (formerly "asset retirement obligations"), accounting for share-based payments, and deferred taxes (formerly "future taxes").

Petroleum and Natural Gas Assets

IFRS standards require that a Corporation choose to report their petroleum and natural gas ("P&NG") assets either at the amount which would have been recorded had the Corporation always followed current IFRS standards or at fair value on the date of adoption of IFRS. Alternatively, IFRS standards allow for a conversion exemption whereby companies can choose to record opening petroleum and natural gas properties at a deemed cost equal to historic cost as calculated under GAAP. Arcan recorded P&NG assets at historic cost as calculated under GAAP on January 1, 2010. The Corporation, under the exemption,

allocated historic costs to cash generating units and components subject to depletion based on reserve values.

Under previous GAAP, all P&NG assets were accounted for under the full cost accounting guideline. Under IFRS, P&NG assets are divided into exploration and evaluation properties ("**E&E assets**") and petroleum and natural gas properties and equipment ("**development assets**"). E&E assets are initially capitalized and accumulated pending determination of technical feasibility and economic viability. E&E assets are not depreciated and are carried at cost less any accumulated impairment losses. Development assets are measured at cost less accumulated depletion and depreciation and any accumulated impairment losses. The Corporation has determined that it has \$9.8 million of E&E assets with the balance of \$130.5 million considered to be development assets on transition to IFRS as of January 1, 2010. For the quarter ended September 30, 2010, the Corporation has determined that it has \$24.6 million of E&E assets with the balance of \$228.1 million considered to be development assets. For the year ended December 31, 2010 the Corporation has determined that it has \$23.9 million of E&E assets with the balance of \$250.2 million considered to be development assets.

Both E&E assets and development assets were assessed to determine whether impairment losses exist under IFRS as at January 1, 2010. These impairment tests differed from the GAAP full cost ceiling test in several significant ways. Assets were allocated to cash generating units ("**CGUs**") and a separate impairment test was completed for each CGU identified. Under GAAP, the ceiling test was a two step test. The carrying value of assets was first compared to the undiscounted future cash flows. If the carrying value of the assets exceeded the undiscounted future cash flows, then the second step of the test was required whereby the assets were written down to the value of the discounted future cash flows. Under IFRS, the impairment test compares the carrying value of the assets to the greater of the fair value, less the cost to sell, the assets and the value-in-use of the assets, which is a discounted cash flow measure. As a result, impairments are recorded more frequently under IFRS. Future impairment tests may be required when management determines that indicators of impairment exist. Should impairment losses be recorded in accordance with IFRS, certain of those losses can reverse in the future if facts and circumstances change. On transition, the Corporation did not recognize any impairment in its E&E assets or development assets. For the quarter ended September 30, 2010, the Corporation recognized a \$0.4 million impairment in its E&E assets with a \$1.3 million impairment in the development assets. For the year ended December 31, 2010 the Corporation recognized an impairment of \$4.0 million in its E&E assets with a \$1.3 million impairment in its development assets.

Depreciation under GAAP was calculated using a unit-of-production method based on total Proved reserves for all accumulated costs (excluding unproved properties). Under IFRS, the net carrying value of development assets are still depleted using a unit of production method; however, significant components with different useful lives are accounted for as separate items and depreciated separately. In addition, IFRS allows depreciation to be calculated using either Proved reserves or Proved plus Probable reserves. Arcan has determined that depreciation will be calculated using Proved plus Probable reserves which resulted in a reduction to D&D expense. Due to the change in accounting policy, for the three months

ended September 30, 2010, D&D decreased to \$5.5 million from \$6.9 million. For the year ended December 31, 2010 D&D decreased to \$16.8 million from \$21.5 million.

Under the full cost accounting guideline, gains or losses were not recognized upon the disposition of P&NG assets unless the disposition results in a significant change in the depletion rate. Under IFRS, gains and losses are recognized in net income on the disposal of an item of P&NG assets. The amount of the gain or loss is determined by comparing the proceeds from disposal with the carrying amount of the item. This will include transactions such as sales of assets, farm-outs, asset swaps and other non-monetary transactions which typically did not result in gains or losses being recorded under GAAP. There was no impact to Arcan during the transition period for these types of transactions.

Decommissioning Liabilities

Under IFRS, decommissioning liabilities (referred to as "asset retirement obligations" under GAAP) have increased as a result to the change from a credit-adjusted risk-free rate of eight to ten percent to a risk-free rate of approximately four percent in the discounting of the liabilities to their present value. In addition, any change to the discount rate affected the entire liability and not just current period additions. Upon transition to IFRS this resulted in a \$2.3 million increase in the decommissioning obligations with a corresponding decrease in retained earnings. As a result of the change in the risk free rate the decommissioning obligations increased by \$2.4 million for the three months ended September 30, 2010 with a corresponding increase in property, plant and equipment. At December 31, 2010 this resulted in a \$2.4 million increase in the decommissioning obligations with a corresponding increase in property, plant and equipment. For the three months ended September 30, 2010 and for the year ended December 31, 2010 accretion expense has decreased.

Stock-Based Compensation

IFRS standards require stock-based awards that vest in instalments, such as on anniversaries of the grant date, to be accounted for as though each instalment or vesting date were a separate award. This resulted in stock-based compensation expense increasing in the earlier vesting periods immediately following new grants. Under IFRS, estimates of the number of stock-based awards expected to vest or expected to be forfeited prior to their expiry also have a quantitative impact on the amount of stock-based compensation expense recorded over the vesting period. GAAP allowed for forfeitures to be recorded as they occurred and for the expense to be recognized on a straight line basis for the entire award. The Corporation recognized an increase of \$0.2 million to contributed surplus with the offset to the deficit on transition. For the quarter ended September 30, 2010, stock-based compensation expense increased by \$0.4 million and for the year ended December 31, 2010, stock-based compensation increased by \$1.5 million.

Business Combinations

Accounting for business combinations also differs under IFRS. Arcan elected not to restate business combinations recorded prior to January 1, 2010 in accordance with IFRS standards. Any goodwill recognized in business combinations after January 1, 2010 recorded under IFRS will represent the excess of the cost of the acquisition over the net fair value of the identifiable assets, liabilities and contingent liabilities of the acquired entity. When the excess is negative, it will be recognized immediately in profit and loss. In addition, transaction costs which are included in the cost of the acquisition will be expensed under IFRS.

Deferred Taxes

GAAP and IFRS follow the liability method of accounting for income taxes whereby tax liabilities and assets are recognized on temporary differences. The Corporation's deferred tax liability was affected by the tax effects resulting from the IFRS changes discussed in this section. In addition, while GAAP separated future income taxes between current and non-current, IFRS allows only for the presentation of non-current deferred tax assets and liabilities.

IFRS also differs in the measurement of flow-through shares by the Corporation, with the premium initially set-up as a liability when the flow-through shares are issued and then released through earnings subsequently when the tax impact is recorded. This change resulted in a deferred flow-through share premium of \$0.1 million being recognized on transition, an increase to share capital of \$2.3 million with the offsetting \$2.2 million recognized against the deficit. For the nine months ended September 30, 2010 this change resulted in a decrease to the deferred flow-through share premium of \$0.1 million being recognized on transition, resulting in a balance of nil at September 30, 2010.

Future Accounting Changes

The following pronouncements from the International Accounting Standards Board will become effective for financial reporting periods beginning on or after January 1, 2013 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 9 – *Financial Instruments* addresses the classification and measurement of financial assets.

IFRS 10 – *Consolidated Financial Statements* builds on existing principles and standards and identifies the concept of control as the determining factor in whether an entity should be included within the consolidated financial statements of the parent company.

IFRS 11 – *Joint Arrangements* establishes the principles for financial reporting by entities when they have an interest in arrangements that are jointly controlled.

IFRS 12 – *Disclosure of Interests in Other Entities* provides the disclosure requirements for interests held in other entities including joint arrangements, associates, special purpose entities and other off balance sheet entities.

IFRS 13 – *Fair Value Measurement* defines fair value, requires disclosure about fair value measurements and provides a framework for measuring fair value when it is required or permitted within the IFRS standards.

IAS 27 – *Separate Financial Statements* revised the existing standard which addresses the presentation of parent company financial statements that are not consolidated financial statements.

IAS 28 – *Investments in Associate and Joint Ventures* revised the existing standard and prescribes the accounting for investments and sets out the requirements for the application of the equity method when accounting for investments in associates and joint ventures.

The Corporation is working on but has not yet completed its evaluation of the effect of adopting these standards on its financial statements.

Legal Advisories

BOEs may be misleading, particularly if used in isolation. The calculation of BOEs is based on a conversion ratio of six Mcf of natural gas to one bbl of oil based on an energy equivalency conversion primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.

Please refer to the "Abbreviations" in the Corporation's AIF for meanings of certain abbreviations used in this MD&A.

Additional information about the Corporation, including the Corporation's AIF for the year ended December 31, 2010, is available under Arcan's profile on SEDAR at www.sedar.com.

Forward-Looking Information and Statements

This MD&A contains certain forward-looking information and statements within the meaning of applicable securities laws. The use of any of the words "expect", "anticipate", "continue", "estimate", "guidance", "objective", "ongoing", "may", "will", "project", "should", "believe", "plans", "intends", "possible" and similar expressions are intended to identify forward-looking information or statements. In particular, but without limiting the foregoing, this MD&A contains forward-looking information and statements pertaining to, among other things, the following: Arcan's focus for the remainder of 2011; anticipated reserves increases; the timing, method and results of drilling and waterflood operations; expectations respecting original oil-in-place recoveries; the timing of pay-out for Arcan's 2011 drilling program; anticipated production volumes, including anticipated year end exit volumes; estimated additional drilling locations; changes and improvements to Arcan's drilling and completion techniques; impact of and estimated waterflood recoveries; the estimated impact and resolution of third party non-operated pipeline issues; expectations respecting future acid demand and the impact of the StimSol Acquisition on the business and operations of Arcan; the application and modification of horizontal, multi-stage fracture technologies; future revenues; future liquidity and financial capacity and resources; results from operations and financial ratios; the volume and product mix of Arcan's oil and gas production; cost and expense estimates and expectations; Arcan's income taxes, tax liabilities and tax pools; oil and natural gas prices and Arcan's risk management programs; the amount of asset retirement obligations; cash flow ratios and sensitivities; royalty rates and their impact on Arcan's operations and

results; the Credit Facility; Arcan's 2011 capital expenditure program; expectations respecting the financing and completion of Arcan's capital program; industry trends; future accounting changes; future growth including development, exploration, acquisition, construction and operational activities and related expenditures.

The forward-looking information and statements contained in this MD&A reflect several material factors and expectations and assumptions of Arcan including, without limitation: that Arcan will continue to conduct its operations in a manner consistent with past operations; the accuracy of current horizontal production data, historical well production and waterflood results; the general continuance of current or, where applicable, assumed industry conditions; continuity of reservoir conditions across Arcan's land base; availability of debt and/or equity sources to fund Arcan's capital and operating requirements as needed; the continuance of existing and, in certain circumstances, proposed tax and royalty regimes; the continuance of laws and regulations relating to environmental matters; ability to retain key employees and executives; the accuracy of the estimates of Arcan's reserve volumes; and certain commodity price and other cost assumptions.

Arcan believes the material factors, expectations and assumptions reflected in the forward-looking information and statements are reasonable at this time but no assurance can be given that these factors, expectations and assumptions will prove to be correct. The forward-looking information and statements included in this MD&A are not guarantees of future performance and should not be unduly relied upon. Such information and 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 information or statements including, without limitation: changes in commodity prices; unanticipated operating results or production declines; for reasons currently unforeseen, the current drilling locations identified by Arcan may prove to be unsuitable or unavailable and drilling on the locations identified may not occur; third party pipeline issues may adversely impact Arcan in a manner or magnitude which is currently unanticipated; changes in tax or environmental laws or royalty rates; increased debt levels or debt service requirements; inaccurate estimation of Arcan's oil and gas reserves volumes; limited, unfavourable or no access to debt or equity capital markets; increased costs and expenses; the impact of competitors; reliance on industry partners; circumstances may arise, including changes in accounting policies, regulations or economic conditions, which could change the assumptions, estimates or expectations or the information provided; shareholder value may not be maximized in the manner suggested by Arcan or at all; there may be circumstances where, for unforeseen reasons, a reallocation of funds may be necessary as may be determined at the discretion of Arcan and there can be no assurance as at the date of this MD&A as to how those funds may be reallocated; should any one of a number of issues arise, Arcan may find it necessary to alter its current business strategy and/or capital expenditure program; currently unforeseen issues may arise in the integration of the business and operations of Arcan and StimSol; the StimSol Acquisition may not positively impact Arcan's business and operations in the manner currently anticipated or at all; and certain other risks detailed from time to time in Arcan's public disclosure documents including, without limitation, those risks identified in this MD&A, and in the AIF, copies of which are available on Arcan's SEDAR profile at www.sedar.com.

The forward-looking information and statements contained in this MD&A speak only as of the date of this MD&A, and Arcan does not assume any obligation to publicly update or revise them to reflect new events or circumstances, except as may be required pursuant to applicable laws.

ARCAN RESOURCES LTD.

Condensed Interim Consolidated Statements of Financial Position

(000's of Canadian dollars)

(unaudited)

	Note	September 30, 2011	December 31, 2010
Assets			
Trade and other receivables		\$ 18,891	\$ 15,610
Prepays and deposits		1,896	1,528
Fair value of commodity contracts	5	1,617	–
Total current assets		22,404	17,138
Fair value of commodity contracts	5	491	–
Intangible assets	6	16,085	–
Property, plant and equipment	7	378,234	250,155
Exploration and evaluation assets	8	23,473	23,935
Total non-current assets		418,283	274,090
Total assets		\$ 440,687	\$ 291,228
Liabilities			
Trade and other payables		\$ 68,106	\$ 43,267
Fair value of commodity contracts	5	–	2,233
Total current liabilities		68,106	45,500
Bank loan	13	43,990	20,823
Convertible debentures	14	73,318	–
Decommissioning obligations	16	18,029	15,476
Deferred tax liabilities		10,376	2,204
Total non-current liabilities		145,713	38,503
Total liabilities		213,819	84,003
Equity			
Share capital	11	214,824	212,721
Contributed surplus		14,906	7,820
Equity component of convertible debentures	14	7,971	–
Deficit		(10,833)	(13,316)
Total equity		226,868	207,225
Commitments	17		
Subsequent events	19		
Total equity and liabilities		\$ 440,687	\$ 291,228

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

ARCAN RESOURCES LTD.

Condensed Interim Consolidated Statements of Income (Loss) and Comprehensive Income (Loss)

(000's of Canadian dollars, except per share amounts)
(unaudited)

	Note	Three months ended September 30,		Nine months ended September 30,	
		2011	2010	2011	2010
Revenue:					
Petroleum and natural gas		\$ 28,370	\$ 17,107	\$ 71,890	\$ 37,155
Royalties		(5,489)	(4,017)	(14,185)	(8,861)
Unrealized gain (loss) on commodity contracts	5	2,547	(1,018)	4,341	(1,018)
Realized loss on commodity contracts	5	–	–	(350)	–
Fracturing and stimulation services		351	–	351	–
Other revenue		4	–	116	4
		<u>25,783</u>	<u>12,072</u>	<u>62,163</u>	<u>27,280</u>
Expenses:					
Production and operating expenses		8,245	3,012	18,605	7,543
Cost of sales for fracturing and stimulation services		778	–	778	–
Exploration and evaluation impairments		55	407	58	2,646
Impairment		–	1,274	–	1,274
Depletion and depreciation		7,717	5,488	18,374	11,191
General and administrative expenses		4,747	3,450	12,737	7,914
Finance expenses	9	2,245	655	5,610	1,612
Gain on sale of property, plant, and equipment		(4)	–	(4)	–
		<u>23,783</u>	<u>14,286</u>	<u>56,158</u>	<u>32,180</u>
Income (loss) before income tax		2,000	(2,214)	6,005	(4,900)
Deferred tax (expense) reduction		(1,224)	226	(3,522)	158
Income (loss) and comprehensive income (loss) the period		<u>\$ 776</u>	<u>\$ (1,988)</u>	<u>\$ 2,483</u>	<u>\$ (4,742)</u>
Income (loss) per share:					
Basic	12	\$ 0.01	\$ (0.03)	\$ 0.03	\$ (0.07)
Diluted	12	\$ 0.01	\$ (0.03)	\$ 0.03	\$ (0.07)

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

ARCAN RESOURCES LTD.

Condensed Interim Consolidated Statements of Changes in Equity

(000's of Canadian dollars, except share amounts)

(unaudited)

	Number of common shares	Share capital	Contributed surplus	Share purchase loan	Equity component of convertible debentures	Deficit	Total equity
Balance at January 1, 2010	47,940,060	\$ 95,677	\$ 4,274	\$ (100)	\$ –	\$ (6,198)	\$ 93,653
Issue of common shares	26,000,000	65,000	–	–	–	–	65,000
Share issue costs, net of tax of \$1,123	–	(3,212)	–	–	–	–	(3,212)
Warrants exercised	452,011	866	–	–	–	–	866
Options exercised	275,833	442	–	–	–	–	442
Performance options exercised	750,000	750	–	–	–	–	750
Stock-based compensation	–	–	3,447	–	–	–	3,447
Transfer of stock-based compensation on exercises	–	481	(481)	–	–	–	–
Net loss	–	–	–	–	–	(4,742)	(4,742)
Balance at September 30, 2010	75,417,904	\$ 160,004	\$ 7,240	\$ (100)	\$ –	\$ (10,940)	\$ 156,204
Balance at January 1, 2010	47,940,060	\$ 95,677	\$ 4,274	\$ (100)	\$ –	\$ (6,198)	\$ 93,653
Issue of common shares	36,421,875	115,025	–	–	–	–	115,025
Share issue costs, net of tax of \$1,869	–	(5,347)	–	–	–	–	(5,347)
Warrants exercised	515,511	993	–	–	–	–	993
Options exercised	2,043,000	3,773	–	–	–	–	3,773
Performance options exercised	750,000	750	–	–	–	–	750
Stock-based compensation	–	–	5,396	–	–	–	5,396
Transfer of stock-based compensation on exercises	–	1,850	(1,850)	–	–	–	–
Share purchase loan repaid	–	–	–	100	–	–	100
Net loss	–	–	–	–	–	(7,118)	(7,118)
Balance at December 31, 2010	87,670,446	212,721	7,820	–	–	(13,316)	207,225
Share issue costs, net of tax of \$18	–	(52)	–	–	–	–	(52)
Options exercised	755,500	1,468	–	–	–	–	1,468
Stock-based compensation	–	–	7,773	–	–	–	7,773
Transfer of stock-based– compensation on exercises	–	687	(687)	–	–	–	–
Equity component on issuance of convertible debentures, net of tax	–	–	–	–	7,971	–	7,971
Net income	–	–	–	–	–	2,483	2,483
Balance at September 30, 2011	88,425,946	\$ 214,824	\$ 14,906	\$ –	\$ 7,971	\$ (10,833)	\$ 226,868

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

ARCAN RESOURCES LTD.

Condensed Interim Consolidated Statements of Cash Flows

(000's of Canadian dollars)
(unaudited)

	Note	Three months ended September 30,		Nine months ended September 30,	
		2011	2010	2011	2010
Cash flows from operating activities:					
Net income (loss) for the period		\$ 776	\$ (1,988)	\$ 2,483	\$ (4,742)
Adjustments for:					
Depletion and depreciation		7,717	5,488	18,374	11,191
Unrealized (gain) loss on commodity contracts		(2,547)	1,018	(4,341)	1,018
Net finance expenses (including accretion)		3,841	977	5,148	1,947
Stock-based compensation		2,693	1,560	7,773	3,447
Exploration and evaluation impairments		55	407	58	2,646
Impairment		-	1,274	-	1,274
Deferred tax expense (reduction)		1,224	(226)	3,522	(158)
Gain on sale of Property, plant and equipment		(4)	-	(4)	-
Reclamation costs		(216)	(13)	(340)	(33)
Change in non-cash working capital	10	(21)	(2,281)	54	(3,392)
Interest paid		(3,049)	(844)	(3,189)	(1,609)
Net cash from operating activities		10,469	5,372	29,538	11,589
Cash flows from investing activities:					
Property, plant and equipment expenditures		(8,371)	(26,240)	(67,327)	(60,214)
Property acquisition		(21,100)	-	(21,100)	(52,803)
Corporate acquisition					
Additions to exploration and evaluation assets		(57,353)	(2,146)	(70,798)	(7,444)
Proceeds on sale of equipment		128	-	128	-
Change in non-cash working capital	10	23,520	1,316	22,604	19,594
Net cash used in investing activities		(63,176)	(27,070)	(136,493)	(100,867)
Cash flows from financing activities:					
Proceeds from issue of convertible debentures		-	-	86,250	-
Proceeds from issue of share capital		-	-	-	65,000
Bank loan proceeds		43,990	21,238	23,167	26,555
Proceeds from exercise of share options and warrants		28	457	1,468	2,058
Convertible debenture issuance costs		-	-	(3,860)	-
Share issuance costs		(58)	3	(70)	(4,335)
Net cash from financing activities		43,960	21,698	106,955	89,278
Change in cash and cash equivalents		(8,747)	-	-	-
Cash and cash equivalents beginning of period		8,747	-	-	-
Cash and cash equivalents end of period		\$ -	\$ -	\$ -	\$ -

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

ARCAN RESOURCES LTD.

Notes to Condensed Interim Consolidated Financial Statement

For the three and nine months ended September 30, 2011 and 2010
(000's of Canadian dollars, except share amounts)
(unaudited)

1. Reporting entity:

Arcan Resources Ltd. ("Arcan" or the "Company") is a publicly listed company with a registered head office in Calgary, Alberta. The Company is engaged in the exploration for and development and production of oil and natural gas in the province of Alberta. The Company acquired Stimsol Canada Inc. ("Stimsol") effective September 13, 2011 and now provides fracturing and stimulation services to companies operating in the oil and natural gas industry in Western Canada. The condensed interim consolidated financial statements (hereinafter referred to as the "interim financial statements") are comprised of the Company and its wholly owned subsidiary, Stimsol Canada Inc. All inter-company balances and transactions have been eliminated. The Company conducts many of its activities jointly with others; these interim financial statements reflect only the Company's proportionate interest in such activities.

2. Basis of preparation:

(a) Statement of compliance:

The interim financial statements have been prepared in accordance with IAS 34 – Interim Financial Reporting of the International Financial Reporting Standards ("IFRS"). These interim financial statements are the Company's third IFRS interim financial statements after its transition to reporting in accordance with IFRS and before the issuance of its first publicly issued annual IFRS financial statements. IFRS 1 – First-time adoption of International Financial Reporting Standards ("IFRS 1") has been applied to these interim financial statements. These interim financial statements use the accounting policies which the Company expects to adopt in its annual financial statements for the year ended December 31, 2011, with the exception of certain disclosures that are normally required to be included in annual financial statements which have been condensed or omitted.

An explanation of how the transition to IFRS has affected the reported financial position, financial performance and cash flows of the Company is provided in note 20. The note includes reconciliations of equity and net loss for comparative periods from former Canadian GAAP to IFRS.

These interim financial statements were authorized for issue by the Board of Directors on November 24, 2011.

(b) Basis of measurement, functional and presentation currency and use of estimates and judgments:

For discussion of the basis of measurement, functional and presentation currency and the use of estimates and judgments refer to note 2 of the Company's interim financial statements for the three months ended March 31, 2011 and 2010.

ARCAN RESOURCES LTD.

Notes to Condensed Interim Consolidated Financial Statements, page 2

For the three and nine months ended September 30, 2011 and 2010
(000's of Canadian dollars, except share amounts)
(unaudited)

3. Significant accounting policies:

For discussion of the Company's significant accounting policies refer to note 3 of the Company's interim financial statements for the three months ended March 31, 2011 and 2010.

All accounting policies have been applied consistently to all periods presented in these financial statements. Certain comparative amounts have been reclassified to conform with the current period's presentation.

The acquisition of Stimsol effective September 13, 2011 necessitated the addition of the following accounting policies for the three and nine months ended September 30, 2011.

(a) Basis of consolidation:

The purchase method of accounting is used to account for acquisitions of subsidiaries and assets that meet the definition of a business under IFRS. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The excess of the cost of acquisition over the fair value of the identifiable assets, liabilities and contingent liabilities acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognized immediately in the statement of income. Transaction costs that the Company incurs in connection with a business combination are expensed as incurred.

A subsidiary is an entity controlled by the Company. Control exists when the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that currently are exercisable are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

Intercompany balances and transactions are eliminated in preparing the interim financial statements.

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3. Significant accounting policies (continued):

(b) Property, plant and equipment:

(i) Recognition and measurement:

Items of property, plant and equipment are measured at cost less accumulated depreciation and accumulated impairment losses.

Cost includes expenditures that are directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the assets to a working condition for their intended use, the costs of dismantling and removing the items and restoring the site on which they are located, and borrowing costs on qualifying assets for which the commencement date for capitalization is on or after January 1, 2010.

When parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items (major components) of property, plant and equipment.

Gains and losses on disposal of an item of property, plant and equipment are determined by comparing the proceeds from disposal with the carrying amount of property, plant and equipment, and are recognized net in profit or loss.

(ii) Subsequent costs:

The cost of replacing a part of an item of property, plant and equipment is recognized in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Company, and its cost can be measured reliably. The carrying amount of the replaced part is derecognized. The costs of the day-to-day servicing of property, plant and equipment (repair and maintenance) are recognized in profit or loss as incurred.

(iii) Depreciation:

Depreciation is recognized in profit or loss on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment from the date they are ready for use. Leased assets are depreciated over the shorter of the lease term and their useful lives unless it is reasonably certain that the Company will obtain ownership by the end of the lease term. Land is not depreciated.

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3. Significant accounting policies (continued):

(b) Property, plant and equipment (continued):

(iii) Depreciation (continued):

The estimated useful lives are as follows:

Buildings	25 years
Field equipment and vehicles	3 – 10 years
Office equipment	5 – 12 years
Computer software/hardware	2 – 5 years
Fixtures and fittings	5 – 10 years

Depreciation methods, useful lives and residual values are reviewed at each reporting date.

(c) Intangible assets:

Intangible assets that are acquired by the Company which have finite useful lives, such as licenses, patents, trademark and customer lists, are measured at cost less accumulated amortization and accumulated impairment losses. Subsequent expenditures are capitalized only when they increase the future economic benefits embodied in the specific asset to which it relates.

Amortization is recognized in profit or loss on a straight-line basis over the estimated useful lives of the related intangible assets from the date they are available for use.

The estimated useful lives are as follows:

Licenses	10 years
Customer lists	7 years

Amortization methods, useful lives and residual values are reviewed at each reporting date.

(d) Impairment of property, plant and equipment and intangible assets:

The carrying amounts of property, plant and equipment and intangible assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated.

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3. Significant accounting policies (continued):

(d) Impairment of property, plant and equipment and intangible assets (continued):

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the "cash-generating unit, or CGU"). The Company considers the Stimsol non-financial assets to be its own CGU.

An impairment loss is recognized if the carrying amount of an asset or its CGU exceeds its estimated recoverable amount. Impairment losses are recognized in profit or loss. Impairment losses recognized in respect of CGU's are allocated to the carrying amounts of the assets in the unit (group of units) on a pro rata basis.

Impairment losses recognized in prior years are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depletion and depreciation or amortization, if no impairment loss had been recognized.

(e) Revenue recognition:

Fracturing and stimulation service revenues are generally derived from the provision of services which are based on contracts that include fixed or determinable prices based upon daily and hourly rates. Revenue is recognized when services are provided and only when collectability is reasonably assured.

(f) Segment reporting:

An operating segment is a component of the Company that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Company's other components. All operating segments' operating results are reviewed regularly by the Company's senior management team to make decisions about resources to be allocated to the segment and assess its performance, and for which discrete financial information is available.

Segment results that are reported to the senior management team include items directly attributable to a segment as well as those that can be allocated on a reasonable basis.

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4. Corporate acquisition:

On September 13, 2011, Arcan acquired all of the issued and outstanding shares of Stimsol, a private fracturing and stimulation services company based in Calgary, Alberta with services across Western Canada. Total cash consideration for the purchase of Stimsol was \$24.0 million. Acquisition costs of \$0.3 million have been expensed as period costs and are included in general and administrative expenses in the interim consolidated statement of income and comprehensive income for the periods ending September 30, 2011. The purchase of Stimsol was undertaken to secure services related to the Company's capital program, specifically fracturing and well stimulation.

The acquisition has been accounted for using the purchase method with the results of Stimsol's operations included in the Company's financial and operating results commencing September 13, 2011. The allocation of net assets acquired is based on the best available information at this time and could be subject to further change within the measurement period. The transaction was accounted for by the acquisition method described in IFRS 3, with the preliminary allocation of the purchase price based on estimated fair values as follows:

Consideration:	
Cash (including \$2,917 accrued for final purchase adjustments)	\$ 24,017
<hr/>	
Fair value of net assets acquired:	
Trade and other receivables	5,966
Prepays and deposits	722
Property, plant and equipment	5,558
Intangible assets	16,085
Deferred tax liability	(2,011)
Trade and other payables	(2,303)
	<hr/>
	\$ 24,017

Accounts receivables are recognized at the contractual amounts, representing fair values, and are expected to be collected. Estimates regarding deferred taxes may change as tax returns are finalized at the date of the change of control and could result in changes to the allocation.

Included in the consolidated statements of income and comprehensive income are the following amounts:

Stimsol amounts since acquisition:	
Fracturing and stimulation services revenue	\$ 351
Loss and comprehensive loss	(424)

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4. Corporate acquisition (continued):

If Stimsol had been acquired on January 1, 2011, the incremental consolidated entities revenue and loss recognized for the period ending September 30, 2011 and the pro forma results would have been as follows:

Nine months ended September 30, 2011	As stated	Stimsol prior to acquisition	Pro forma
Net revenue ¹	\$ 62,163	\$ 8,057	\$ 70,220
Income (loss) and comprehensive income (loss) ²	2,483	(3,969)	(1,486)

¹ Revenues are presented net of royalties and include the unrealized gain and realized loss on commodity contracts and other revenue. Revenue earned by Stimsol from Arcan has been eliminated and is not included in this reconciliation.

² Income earned by Stimsol from Arcan has been eliminated and is not included in this reconciliation.

5. Financial risk and capital management:

(a) Commodity price risk:

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

During the year ended December 31, 2010 the Company entered into four costless collar financial oil contracts. The contracts are each for 500 barrels per day of oil with floor prices of \$70.00 per barrel Canadian dollar WTI. Two of the contracts have ceiling prices of \$100.00 per barrel Canadian dollar WTI and the other two contracts have ceiling prices of \$100.05 and \$100.30 per barrel Canadian dollar WTI, respectively. All contracts are for the period from January 1, 2011 to December 31, 2011. During the nine months ended September 30, 2011 the Company entered into two costless collar financial oil contracts. The contracts are each for 500 barrels per day of oil with floor prices of \$75.00 per barrel Canadian dollar WTI.

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Notes to Condensed Interim Consolidated Financial Statements, page 8

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5. Financial risk and capital management (continued):

(a) Commodity price risk (continued):

One of the contracts has a ceiling price of \$126.00 per barrel Canadian dollar WTI and the other contract has a ceiling price of \$127.50 per barrel Canadian dollar WTI. Both contracts are for the period from January 1, 2012 to December 31, 2012. The Company recognized an unrealized gain of \$4.3 million on the contracts for the nine months ended September 30, 2011 (2010 – \$1.0 million loss). The Company recognized a realized loss of \$350 on the contracts for the nine months ended September 30, 2011 (2010 – \$nil).

The Company has assessed the sensitivity of the fair value of the oil commodity contracts to fluctuations in forward crude oil prices. As at September 30, 2011, if the forward price of crude had been \$1.00 lower, net income for the period would have been approximately \$412 higher, due to a higher unrealized gain on the commodity contracts. An equal and opposite impact would have occurred to net income had the forward price of crude been \$1.00 higher.

(b) Capital management:

The Company's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain the future development of the business.

The Company manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of the underlying petroleum and natural gas assets. The Company considers its capital structure to include shareholder's equity of \$226.9 million (December 31, 2010 - \$207.2 million), bank debt and convertible debentures of \$117.3 million (December 31, 2010 - \$20.8 million) and a working capital deficiency of \$45.7 million (December 31, 2010 - \$28.4 million). In order to maintain or adjust the capital structure, the Company may from time to time issue shares and adjust its capital spending to manage current and projected debt levels.

The Company monitors capital based on the ratio of net debt to quarterly annualized funds from operations. In this ratio, net debt is defined as outstanding bank debt plus convertible debentures plus or minus working capital, divided by funds from operations for the most recent calendar quarter, annualized (multiplied by four). Funds from operations are defined as cash flow from operating activities before changes in non-cash working capital. The Company's strategy is to maintain a ratio of less than 2 to 1 although it is anticipated to be higher than that ratio over the next few years due to the long-term nature of the convertible debenture. This ratio may increase at certain times as a result of acquisitions. In order to facilitate the management of this ratio, the Company prepares annual capital expenditure budgets, which are updated as necessary depending on varying factors including current and forecast prices, successful capital deployment and general industry conditions. The annual and updated budgets are approved by the Board of Directors.

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5. Financial risk and capital management (continued):

(b) Capital management (continued):

As at September 30, 2011 and December 31, 2010, the Company's ratio of net debt to quarterly annualized funds from operations was 3.9 to 1 and 1.6 to 1, respectively. The Company's ratio of net debt to quarterly annualized funds from operations at September 30, 2011 was above the 2 to 1 ratio that management targets to maintain. The Company issued 9,323,400 common shares at a price of \$5.45 for gross proceeds of \$50.8 million subsequent to the end of the period to reduce this ratio (note 19). The Company issued \$86.3 million principal amount of convertible debentures during the period (note 14) which was used to reduce bank debt levels through this debt instrument with a five year term.

Also, subsequent to the end of the period the Company issued \$85.0 million principal amount of convertible debentures with a seven year term (note 19).

The Company's bank completed its semi-annual borrowing base review on May 25, 2011 and the bank credit facility has been established at \$120 million. The next scheduled renewal is on or before May 29, 2012. The Company continually monitors its financing alternatives, and expects to finance its 2011 cash capital expenditures program from internally generated funds from operations, debt, and equity.

The net debt to quarterly annualized funds from operations has been calculated as follows:

Three months ended	September 30, 2011	December 31, 2010
Working capital deficiency (including bank debt and convertible debentures)	\$ 163,010	\$ 49,185
Cash flow from operating activities	10,469	8,044
Change in non-cash operating working capital	21	(285)
Funds from operations	10,490	7,759
Annualizing factor	x4	x4
Annualized funds from operations	\$ 41,960	\$ 31,036
Ratio	3.9 to 1	1.6 to 1

The Company's share capital is not subject to external restrictions, however the bank debt facility is based on petroleum and natural gas reserves and a financial covenant (see note 13). The Company has not paid or declared any dividends since the date of incorporation, nor are any contemplated in the foreseeable future.

There were no changes in the Company's approach to capital management during the period.

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6. Intangible assets:

	Licenses	Customer Lists	Total
Cost:			
Acquisition (note 4)	\$ 12,385	\$ 3,700	\$ 16,085
Balance at September 30, 2011	\$ 12,385	\$ 3,700	\$ 16,085

7. Property, plant and equipment:

	Oil and Gas Properties	Stimsol Assets	Corporate Assets	Total
Cost or deemed cost:				
Balance at January 1, 2010	\$ 129,627	\$ -	\$ 845	\$ 130,472
Additions	87,280	-	120	87,400
Acquisitions	42,821	-	-	42,821
Decommissioning obligations	7,500	-	-	7,500
Balance at December 31, 2010	267,228	-	965	268,193
Additions	62,820	-	4,507	67,327
Transfers from exploration and evaluation assets	71,202	-	-	71,202
Acquisition (note 4)	-	5,558	-	5,558
Disposals	-	(124)	-	(124)
Decommissioning obligations	2,490	-	-	2,490
Balance at September 30, 2011	\$ 403,740	\$ 5,434	\$ 5,472	\$ 414,646
Depletion, depreciation and impairment losses:				
Balance at January 1, 2010	\$ -	\$ -	\$ -	\$ -
Depletion and depreciation	16,582	-	182	16,764
Impairment loss	1,274	-	-	1,274
Balance at December 31, 2010	17,856	-	182	18,038
Depletion and depreciation	18,032	30	312	18,374
Balance at September 30, 2011	\$ 35,888	\$ 30	\$ 494	\$ 36,412
Carrying amounts:				
At January 1, 2010	\$ 129,627	\$ -	\$ 845	\$ 130,472
At December 31, 2010	\$ 249,372	\$ -	\$ 783	\$ 250,155
At September 30, 2011	\$ 367,852	\$ 5,404	\$ 4,978	\$ 378,234

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7. Property, plant and equipment (continued):

The calculation of depletion includes estimated future development costs of \$411,003 (2010 - \$54,536) associated with the development of the Company's proved plus probable reserves and excludes salvage value of \$1,707 (2010 - \$1,707).

(a) Security:

At September 30, 2011 and December 31, 2010 all of the Company's properties and equipment are pledged as security for the bank loans.

(b) Contingencies:

Although the Company believes that it has title to its oil and natural gas properties, it cannot control or completely protect itself against the risk of title disputes or challenges.

8. Exploration and evaluation assets:

Balance at January 1, 2010	\$	9,832
Acquisitions		9,981
Additions		8,134
Exploration and evaluation impairments		(4,012)
Balance at December 31, 2010		23,935
Additions		70,798
Transfers to property, plant and equipment		(71,202)
Exploration and evaluation impairments		(58)
Balance at September 30, 2011	\$	23,473

Exploration and evaluation (E&E) assets consist of the Company's exploration projects which are pending the determination of proven and/or probable reserves. Additions represent the Company's share of costs incurred on E&E assets during the period.

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9. Finance expenses:

	Three months ended		Nine months ended	
	September 30,		September 30,	
	2011	2010	2011	2010
Financial expenses:				
Interest on bank loans	\$ 84	\$ 522	\$ 273	\$ 1,274
Interest on convertible debentures	1,369	–	3,378	–
Accretion on convertible debentures	671	–	1,556	–
Accretion of decommissioning obligations	121	133	403	338
	\$ 2,245	\$ 655	\$ 5,610	\$ 1,612

10. Supplemental cash flow information:

Changes in non-cash working capital is comprised of:

	Three months ended		Nine months ended	
	September 30,		September 30,	
	2011	2010	2011	2010
Source/(use) of cash:				
Trade and other receivables	\$ (4,522)	\$ (3,884)	\$ (3,281)	\$ (7,558)
Prepays and deposits	(248)	147	(368)	(15)
Trade and other payables	26,801	2,772	24,839	23,775
Non-cash working capital acquired (note 4)	1,468	–	1,468	–
	\$ 23,499	\$ (965)	\$ 22,658	\$ 16,202
Related to operating activities	\$ (21)	\$ (2,281)	\$ 54	\$ (3,392)
Related to investing activities	\$ 23,520	\$ 1,316	\$ 22,604	\$ 19,594

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Notes to Condensed Interim Consolidated Financial Statements, page 13

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11. Share capital:

The Company is authorized to issue an unlimited number of common shares.

The holders of common shares are entitled to receive dividends as declared by the Company and are entitled to one vote per share.

The Company is also authorized to issue an unlimited number of preferred shares issuable in series.

12. Earnings per share:

The following table summarizes the basis for the determination of basic and diluted per share amounts:

	Three months ended		Nine months ended	
	September 30,		September 30,	
	2011	2010	2011	2010
Weighted average number of shares – basic	88,425,294	75,245,426	88,242,434	66,296,618
Weighted average number of shares – diluted	89,918,910	75,245,426	89,397,331	66,296,618

In computing diluted per share amounts at September 30, 2011, 4,230,500 options (September 30, 2010 – 7,285,167 options), nil warrants (September 30, 2010 – 123,500 warrants) were excluded for the calculation as their effect was anti-dilutive. The Company has also excluded the convertible debentures which would convert into an additional 9,857,143 common shares (September 30, 2010 – nil common shares), as they were also anti-dilutive.

13. Bank loans:

The Company has total available credit facilities of \$120 million (the "Facilities") comprised of a \$110 million syndicated extendible, revolving term credit facility and a \$10 million non-syndicated extendible revolving operating term credit facility. The Facilities are available on a revolving basis until May 29, 2012. On May 29, 2012, at the Company's discretion, the Facilities are available on a non-revolving basis for a period of one year, at which time the Facilities would be due and payable. Alternatively, the Facilities may be extended for a further 364 day period at the request of the Company, subject to approval by the lenders. Interest on the Facilities is calculated at the bank prime rate of interest, plus an applicable facility margin depending upon certain ratios. The \$120 million borrowing base is subject to a semi-annual and annual review by the bank.

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13. Bank loans (continued):

As the available lending limits of the Facilities are based on the bank's interpretation of the Company's reserves and future commodity prices, there can be no assurance as to the amount of the facilities that will be determined at each scheduled review. The Facilities are secured by a \$500 million first floating charge debenture and a general security agreement over all Company assets. Pursuant to the terms of the credit facilities, the Company has provided the covenant that at all times its working capital ratio shall be not less than 1 to 1. The working capital ratio is defined under the terms of the Facilities as current assets, including the undrawn portion of the Facilities, to current liabilities, excluding any current bank indebtedness under the Facilities. The Company is compliant with this covenant at September 30, 2011 and December 31, 2010. This facility had an effective interest rate of 4.00% at September 30, 2011 (September 30, 2010 – 4.75%).

14. Convertible debentures:

On February 14, 2011, Arcan issued \$86.3 million principal amount of 6.25% Convertible Unsecured Subordinated Debentures for net proceeds of \$82.4 million. The Debentures pay interest semi-annually on February 28 and August 31, commencing with the initial interest payment on August 31, 2011 and have a maturity date of February 28, 2016. The Debentures are convertible at the option of the holder to common shares at a conversion price of \$8.75 per common share. The Company has the option to redeem the Debentures on and after February 28, 2014 and at any time prior to February 28, 2016 at a redemption price equal to 100% of their principal amount plus accrued and unpaid interest provided that the current market price is at least 125% of the conversion price of \$8.75. On redemption or maturity the Company may elect to repay the principal and satisfy its interest obligations by issuing Arcan common shares.

Upon issuance of the debentures, the liability component of the convertible debentures was recognized initially at the fair value of a similar liability that does not have an equity conversion option. The difference between these two amounts of \$10.6 million has been recorded as equity with the remaining \$71.8 million allocated to long-term debt, net of \$3.9 million of transaction costs. The discount on the debentures is being accreted such that the liability at maturity will equal the face value of \$86.3 million.

Certain officers and directors of the Company acquired \$1.3 million of the debenture issue.

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14. Convertible debentures (continued):

The directly attributable transaction costs of \$3.9 million were proportionally allocated to the liability and equity components.

	February 14, 2011
Long-term liability, net of transaction costs	\$ 71,762
Equity component, net of transaction costs and deferred tax	7,971
Deferred tax on equity component of convertible debentures	2,657
Transaction costs	3,860
Face value	\$ 86,250

The following table indicates the changes in the convertible debentures during the period:

	Face Value	Debt Component	Equity Component
Balance at February 14, 2011	\$ 86,250	\$ 71,762	\$ 7,971
Accretion on convertible debentures	-	1,556	-
	\$ 86,250	\$ 73,318	\$ 7,971

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15. Share based payments:

The Company's stock option plan provides for granting of options to directors and employees to a maximum of ten percent of the total issued and outstanding common shares of the Company. These options have a term of five years to expiry. Some of the options vest immediately, others vest one-third as of the date of grant, and one-third on each of the first two anniversary dates, and others vest one-third on each of the first three anniversary dates. The Company has reserved common shares for issuance under the stock option plan in the amount of the stock options outstanding from time to time.

The number and weighted average exercise prices of share options are as follows:

	Nine months ended		Year ended	
	September 30, 2011		December 31, 2010	
(in thousands of options)	Number of options	Weighted average exercise price	Number of options	Weighted average exercise price
Outstanding at beginning of period	8,390	\$ 3.82	4,671	\$ 2.01
Granted	1,306	5.05	5,834	4.57
Exercised	(756)	1.94	(2,043)	1.85
Forfeited	(244)	3.81	(72)	2.87
Outstanding at end of period	8,696	\$ 4.17	8,390	\$ 3.82
Exercisable at end of period	2,682	\$ 2.92	2,342	\$ 2.12

The fair value of the options was estimated using the Black Scholes model with the following weighted average inputs:

	Nine months ended, September 30, 2011	Year ended, December 31, 2010
Fair value at grant date	\$ 3.45	\$ 3.25
Share price	5.05	4.57
Exercise price	5.05	4.57
Volatility	85.8%	91.2%
Option life	5 years	5 years
Dividends	0%	0%
Risk-free interest rate	2.4%	2.6%

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15. Share based payments (continued):

A forfeiture rate of 8 % (2010 - 8 %) is used when recording stock-based compensation. This estimate is adjusted to the actual forfeiture rate. Stock-based compensation cost of \$7.8 million (September 30, 2010 - \$3.4 million) was expensed during the nine months ended September 30, 2011.

16. Decommissioning obligations:

	September 30, 2011	December 31, 2010
Balance, beginning of period (January 1)	\$ 15,476	\$ 7,647
Liabilities incurred	1,399	1,130
Liabilities incurred on acquisition	–	5,692
Accretion expense	403	468
Changes in estimates	1,091	679
Reclamation costs	(340)	(140)
Balance, end of period	\$ 18,029	\$ 15,476

The Company's decommissioning obligations result from its ownership interest in oil and natural gas assets including well sites and gathering systems. The total decommissioning obligation is estimated based on the Company's net ownership interest in all wells and facilities, estimated costs to reclaim and abandon these wells and facilities and the estimated timing of the costs to be incurred in future years. The Company has estimated the net present value of the decommissioning obligations to be \$18.0 million as at September 30, 2011 (December 31, 2010 - \$15.5 million) based on an undiscounted total future liability of \$22.8 million (December 31, 2010 - \$21.0 million). These payments are expected to be made over the next 10 years with the majority of costs to be incurred between 2018 and 2019. An inflation rate of 2% (2010 – 2%) was used to inflate the costs, and a long-term risk-free rate of 2.8% (2010 – 3.5%) was used to calculate the carrying value of the decommissioning obligations.

17. Commitments:

The Company has entered into contracts to secure oilfield services over the course of one year. The total approximate commitment remaining related to these contracts is \$2.2 million in 2011 and \$3.7 million in 2012.

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18. Segmented disclosure:

The Company operates in two main industry segments. These segments are Exploration and Production Operations ("E&P"), which includes the exploration, development and production of oil and natural gas in Alberta, and Fracturing and Stimulation services ("Fracturing and Stimulation"), which includes services for well fracturing as well as the sale of acid blends for use in fracturing to oil and natural gas companies. The Company's senior management team assesses the performance of its segments based on operating and corporate netbacks and net income or loss. The segmented amounts are as follows:

	Exploration and Production	Fracturing and Stimulation	Eliminations	Total
As at and for the three months ended September 30, 2011:				
Petroleum and natural gas revenue	\$ 28,370	\$ –	\$ –	\$ 28,370
Royalties	(5,489)	–	–	(5,489)
Production and operating expenses	(8,245)	–	–	(8,245)
Fracturing and stimulation services revenue	–	609	(258)	351
Cost of sales for fracturing and stimulation services	–	(778)	–	(778)
Operating netbacks	14,636	(169)	(258)	14,209
Other revenue	4	–	–	4
Cash general and administrative expenses	(1,943)	(111)	–	(2,054)
Cash finance expenses	(1,452)	(1)	–	(1,453)
Corporate netbacks	11,245	(281)	(258)	10,706
Non-cash finance expenses	(792)	–	–	(792)
Exploration and evaluation impairments	(55)	–	–	(55)
Stock-based compensation	(2,693)	–	–	(2,693)
Depletion and depreciation	(7,687)	(30)	–	(7,717)
Unrealized gain on commodity contracts	2,547	–	–	2,547
Gain on sale of property, plant and equipment	–	4	–	4
Deferred tax (expenses) reduction	(1,365)	141	–	(1,224)
Net income (loss)	\$ 1,200	\$ (166)	\$ (258)	\$ 776
Total assets	\$ 439,781	4,244	(3,338)	440,687
Total liabilities	\$ 212,232	4,667	(3,080)	213,819
Cash capital expenditures (proceeds) ¹	\$ 65,982	\$ (128)	\$ (258)	\$ 65,596

¹ Excludes the corporate acquisition of stimulation and fracturing services company.

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18. Segmented disclosure (continued):

	Exploration and Production	Fracturing and Stimulation	Eliminations	Total
As at and for the nine months ended September 30, 2011:				
Petroleum and natural gas revenue	\$ 71,890	\$ –	\$ –	\$ 71,890
Royalties	(14,185)	–	–	(14,185)
Production and operating expenses	(18,605)	–	–	(18,605)
Fracturing and stimulation services revenue	–	609	(258)	351
Cost of sales for fracturing and stimulation services	–	(778)	–	(778)
Operating netbacks	39,100	(169)	(258)	38,673
Other revenue	116	–	–	116
Realized loss on commodity contracts	(350)	–	–	(350)
Cash general and administrative expenses	(4,853)	(111)	–	(4,964)
Cash finance expenses	(3,650)	(1)	–	(3,651)
Corporate netbacks	30,363	(281)	(258)	29,824
Non-cash finance expenses	(1,959)	–	–	(1,959)
Exploration and evaluation impairments	(58)	–	–	(58)
Stock-based compensation	(7,773)	–	–	(7,773)
Depletion and depreciation	(18,344)	(30)	–	(18,374)
Unrealized gain on commodity contracts	4,341	–	–	4,341
Gain on sale of property, plant and equipment	–	4	–	4
Deferred tax (expenses) reduction	(3,663)	141	–	(3,522)
Net income (loss)	2,907	(166)	(258)	2,483
Total assets	439,781	4,244	(3,338)	440,687
Total liabilities	212,232	4,667	(3,080)	213,819
Cash capital expenditures (proceeds) ¹ \$	\$ 138,383	\$ (128)	\$ (258)	\$ 137,997

¹ Excludes the corporate acquisition of stimulation and fracturing services company.

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19. Subsequent events:

On October 3, 2011, the Company purchased undeveloped petroleum and natural gas properties for \$13.3 million.

On October 7, 2011, the Company issued \$85.0 million principal amount of 6.50% Convertible Unsecured Subordinated Debentures for net proceeds of \$81.6 million. The Debentures pay interest semi-annually on April 30 and October 31, commencing with the initial interest payment on April 30, 2012 and have a maturity date of October 31, 2018. The Debentures are convertible at the option of the holder to common shares at a conversion price of \$8.75 per common share. The Company has the option to redeem the Debentures on and after October 31, 2015 and at any time prior to October 31, 2017 at a redemption price equal to 100% of their principal amount plus accrued and unpaid interest provided that the current market price is at least 125% of the conversion price of \$8.75. On or after October 31, 2017 and prior to October 31, 2018, the debentures may be redeemed in whole or in part at the option of Arcan on not more than 60 days and not less than 40 days prior to notice at a price equal to their principal amount plus accrued and unpaid interest. On redemption or maturity the Company may elect to repay the principal and satisfy its interest obligations by issuing Arcan common shares.

Also on October 7, 2011, the Company issued 9,200,000 common shares at \$5.45 per common share for gross proceeds of \$50.1 million. On November 8, 2011 the underwriters exercised a portion of the over-allotment option on the financing resulting in an additional 123,400 common shares being issued for gross proceeds of \$0.7 million.

Subsequent to the end of the period, the Company entered into additional financial oil contracts. The Company has entered into two fixed price swap contracts each for 500 barrels per day, whereby the Company will receive a fixed price of \$95.00 per barrel in exchange for payment to the counter-party based on Canadian dollar WTI spot prices. The Company has also purchased two call arrangements each for 500 barrels per day, whereby should the Canadian dollar WTI price exceed \$110 and \$115 per barrel, respectively for each contract, the Company would receive the difference from the counter-party. The contracts are for the period from January 1, 2012 to December 31, 2012. The Company also entered into a fixed price swap contract for 500 barrels per day, whereby the Company will receive a fixed price of \$90.00 per barrel in exchange for payment to the counter-party based on Canadian dollar WTI spot prices. The Company has also purchased a call arrangement for 500 barrels per day, whereby should the Canadian dollar WTI price exceed \$110 per barrel the Company would receive the difference from the counter-party. The contract is for the period from January 1, 2013 to December 31, 2013.

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20. Transition to IFRS:

These interim financial statements are the Company's third prepared under IFRS.

The adoption of IFRS requires the application of IFRS 1. IFRS 1 generally requires that an entity retrospectively apply all IFRS effective at the end of its first IFRS reporting period; however IFRS 1 provides certain mandatory exceptions and permits limited optional exemptions. The IFRS 1 optional exemptions that have been applied include:

- Deemed cost exemption for full cost oil and gas entities as further described in note 20 (a).
- Decommissioning obligation exemption that allows any changes in decommissioning obligations on transition to IFRS to be adjusted through opening retained earnings.
- Stock-based compensation exemption that allows a company to only have to evaluate share based compensation awards that were unvested as of the date of transition and that were issued subsequent to November 7, 2002.
- Business combinations exemption that allows a company to not have to restate any business combinations that occurred prior to the date of transition.

The accounting policies in note 3 have been applied in preparing the interim financial statements for the three and nine months ended September 30, 2011, the comparative information for the three and nine months ended September 30, 2010, the financial statements for the year ended December 31, 2010 and the preparation of the opening IFRS balance sheet at January 1, 2010, the Company's date of transition to IFRS.

In preparing its opening IFRS balance sheet, comparative information for the three and nine months ended September 30, 2010 and financial statements for the year ended December 31, 2010, the Company adjusted amounts previously reported in financial statements prepared in accordance with former Canadian GAAP. An explanation of how the transition from former Canadian GAAP to IFRS has affected the Company's financial position, financial performance and cash flows is set out in the following tables and the notes accompanying the tables.

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For the three and nine months ended September 30, 2011 and 2010

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20. Reconciliation of equity and loss from Canadian GAAP to IFRS (continued):

Reconciliation of the consolidated statement of financial position as at September 30, 2010:

	Canadian GAAP	Effect of transition to IFRS	IFRS
Assets			
Trade and other receivables	\$ 17,570	\$ –	\$ 17,570
Prepays and deposits	950	–	950
Total current assets	18,520		18,520
Property, plant and equipment	251,027	(22,903)	228,124
Exploration and evaluation assets		24,611	24,611
Total non-current assets	251,027	1,708	252,735
Total assets	\$ 269,547	\$ 1,708	\$ 271,255
Liabilities			
Trade and other payables	\$ 40,915	\$ –	\$ 40,915
Fair value of commodity contracts	1,018	–	1,018
Total current liabilities	41,933	–	41,933
Bank loan	55,141	–	55,141
Decommissioning obligations	10,315	4,717	15,032
Deferred tax liabilities	3,686	(741)	2,945
Total non-current liabilities	69,142	3,976	73,118
Total liabilities	111,075	3,976	115,051
Equity			
Share capital	157,665	2,339	160,004
Share purchase loan	(100)		(100)
Contributed surplus	6,284	956	7,240
Deficit	(5,377)	(5,563)	(10,940)
Total equity	158,472	(2,268)	156,204
Total equity and liabilities	\$ 269,547	\$ 1,708	\$ 271,255

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20. Reconciliation of equity and loss from Canadian GAAP to IFRS (continued):

Reconciliation of the consolidated statement of loss and comprehensive loss for the three months ended September 30, 2010:

	Canadian GAAP	Effect of transition to IFRS	IFRS
Revenue:			
Petroleum and natural gas	\$ 17,107	\$ –	\$ 17,107
Royalties	(4,017)	–	(4,017)
Unrealized loss on commodity contracts	(1,018)	–	(1,018)
	12,072		12,072
Expenses:			
Production and operating expenses	3,012	–	3,012
Exploration and evaluation expenses	–	407	407
Impairment	–	1,274	1,274
Depletion and depreciation	6,854	(1,366)	5,488
General and administrative	3,013	437	3,450
Accretion	202	(202)	–
Interest	522	(522)	–
Finance expenses	–	655	655
	13,603	683	14,286
Loss before income tax	(1,531)	(683)	(2,214)
Deferred tax expense	176	50	226
Loss and comprehensive loss for the period	\$ (1,355)	\$ (633)	\$ (1,988)
Loss per share:			
Basic and diluted	\$ (0.02)	\$ (0.01)	\$ (0.03)

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Notes to Condensed Interim Consolidated Financial Statements, page 24

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20. Reconciliation of equity and loss from Canadian GAAP to IFRS (continued):

Reconciliation of the consolidated statement of loss and comprehensive loss for the nine months ended September 30, 2010:

	Canadian GAAP	Effect of transition to IFRS	IFRS
Revenue:			
Petroleum and natural gas	\$ 37,155	\$ –	\$ 37,155
Royalties	(8,861)	–	(8,861)
Other revenue	4	–	4
Unrealized loss on commodity contracts	(1,018)	–	(1,018)
	27,280		27,280
Expenses:			
Production and operating expenses	7,543	–	7,543
Exploration and evaluation expenses	–	2,646	2,646
Impairment	–	1,274	1,274
Depletion and depreciation	14,211	(3,020)	11,191
General and administrative expenses	7,152	762	7,914
Accretion	504	(504)	–
Interest	1,274	(1,274)	–
Finance expenses	–	1,612	1,612
	30,684	1,496	32,180
Loss before income tax	(3,404)	(1,496)	(4,900)
Deferred tax reduction (expense)	254	(96)	158
Loss and comprehensive loss for the period	\$ (3,150)	\$ (1,592)	\$ (4,742)
Loss per share:			
Basic and diluted	\$ (0.05)	\$ (0.02)	\$ (0.07)

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20. Reconciliation of equity and loss from Canadian GAAP to IFRS (continued):

Notes to reconciliations

(a) IFRS 1 election for full cost oil and gas entities

The Company elected an IFRS 1 exemption whereby the Canadian GAAP full cost pool was measured upon transition to IFRS as follows:

- (i) exploration and evaluation assets were reclassified from the full cost pool to exploration and evaluation assets at the amount that was recorded under Canadian GAAP; and
- (ii) the remaining full cost pool was allocated to the respective CGU's and components in property, plant and equipment pro rata using reserve values.

For January 1, 2010, this resulted in a \$9.8 million increase in exploration and evaluation assets with a corresponding decrease in property, plant and equipment. For September 30, 2010, there was a \$24.6 million increase in exploration and evaluation assets with a corresponding decrease in property, plant and equipment. For December 31, 2010, there was a \$23.9 million increase in exploration and evaluation assets with a corresponding decrease in property, plant and equipment.

(b) Decommissioning obligations:

Under previous Canadian GAAP asset retirement obligations were discounted at a credit adjusted risk free rate of 8 percent. Under IFRS the estimated cash flow to abandon and remediate the wells and facilities has been risk adjusted therefore the provision is discounted at a risk free rate of 4 percent. Upon transition to IFRS this resulted in a \$2.3 million increase in the decommissioning obligations with a corresponding increase in deficit. As a result of the change in the risk free rate the decommissioning obligations increased by \$2.4 million for the nine months ended September 30, 2010 with a corresponding increase in property, plant and equipment. At December 31, 2010 this resulted in a \$2.4 million increase in the decommissioning obligations with a corresponding increase in property, plant and equipment.

As a result of the change in the decommissioning obligation accretion expense decreased by \$69 and \$166 during the three and nine months ended September 30, 2010, respectively, under IFRS compared to Canadian GAAP. For the year ended December 31, 2010, decommissioning obligation accretion expense decreased by \$242 under IFRS compared to Canadian GAAP. In addition, under Canadian GAAP accretion of the discount was included in depletion and depreciation. Under IFRS it is included in finance expenses.

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20. Reconciliation of equity and loss from Canadian GAAP to IFRS (continued):

(c) Share-based payments:

Under previous Canadian GAAP, the Company recognized an expense related to their share-based payments on a straight-line basis through the date of full vesting and did not incorporate a forfeiture rate. Under IFRS, the Company is required to recognize the expense over the individual vesting periods for the graded vesting awards and estimate a forfeiture rate. For January 1, 2010, this resulted in a \$194 increase to contributed surplus with a corresponding increase to deficit. For three and nine months ended September 30, 2010, this resulted in a \$437 and \$762 respective increase to stock-based compensation expense with a corresponding increase to contributed surplus. For December 31, 2010, this resulted in a \$1.5 million increase to stock-based compensation expense with a corresponding increase to contributed surplus.

(d) Depletion policy:

Upon transition to IFRS, the Company adopted a policy of depleting oil and natural gas interests on a unit of production basis over proved plus probable reserves. The depletion policy under Canadian GAAP was based on units of production over proved reserves. In addition depletion was done on the Canadian cost centre under previous Canadian GAAP. IFRS requires depletion and depreciation to be calculated based on individual components (ie. fields or combinations thereof).

There was no impact of this difference on adoption of IFRS at January 1, 2010 as a result of the IFRS 1 election as discussed above.

For the year ended December 31, 2010 component accounting over proved and probable reserves resulted in a decrease to depletion expense of \$4.7 million with a corresponding change to property, plant and equipment. For the three and nine months ended September 30, 2010 component accounting resulted in a decrease to depletion expense of \$1.4 million and \$3.0 million, respectively, with a corresponding change to property, plant and equipment.

(e) Impairments:

Under previous Canadian GAAP, an impairment of oil and gas assets was recognized and measured at a country cost centre level and was not reversed. Under IFRS, impairments of oil and gas assets are recognized and measured at a cash-generating unit level and impairments are reversed. The Company recognized impairment for the year ended December 31, 2010 of \$1.3 million. The impairment relates to the Company's natural gas CGU and arose primarily due to declining forward natural gas prices. The impairment was based on the difference between the property, plant and equipment net book values and their recoverable amounts. The recoverable amounts were determined using fair value less costs

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(unaudited)

20. Reconciliation of equity and loss from Canadian GAAP to IFRS (continued):

(e) Impairments (continued):

to sell based on discounted future cash flows of proved and probable reserves using forecast prices and costs discounted at 15%.

The Company also expensed \$0.4 million, \$2.6 million and \$4.0 million of exploration and evaluation costs for the three and nine months ended September 30, 2010 and the year ended December 31, 2010, respectively, related to unsuccessful exploration projects and expiring land leases.

(f) Flow-through shares:

Under previous Canadian GAAP, proceeds received from flow-through shares were included in their entirety in share capital and the estimated tax cost of issuing flow-through shares was reflected in share capital and deferred taxes when the expenditures were renounced. Under IFRS, the premium received on the flow-through shares, being the difference in price over a common share with not tax attributes, is not included in share capital, but rather is included on the balance sheet as a deferred liability. In addition, as the flow-through expenditures are incurred the deferred tax liability associated with the renounced tax deductions are recognized through profit and loss along with a pro-rata portion of the deferred premium.

On transition the Company increased share capital by \$2.0 million reflecting the net impact of eliminating the premiums on previous flow-through share issuances and the associated deferred tax amounts. A deferred premium liability of \$0.1 million was also recognized on transition. During the 2010 year, the deferred premium of \$0.1 million and associated tax effect of the flow-through shares of \$0.4 million was recognized in the deferred tax reduction on the statement of income.

(g) Cash flows:

Upon transition to IFRS, there were no significant changes to operating, investing or financing cash flows for the three and nine months ended September 30, 2010 or the year ended December 31, 2010.

Directors

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Independent Director

Andy Fisher
Executive Vice President, Arcan Resources Ltd.

Ed Gilmet
President and CEO, Arcan Resources Ltd.

Michael J. Laffin
Independent Director

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Ed Gilmet
President and CEO

Douglas Penner
Executive Vice President and CFO

Andy Fisher
Executive Vice President

Graeme Ryder
Vice President, Finance and Controller

Kyle Baumgardner
Vice President, Operations

Thanos Natras
Vice President, Exploration

Kevin Gunning
Vice President, Engineering

Michael J. Laffin
Corporate Secretary

Registrar and Transfer Agent

Valiant Trust Company

Stock Exchange Listing: TSX-V

Common Shares - "ARN"

6.25% 2016 Debentures - "ARN.DB"

6.50% 2018 Debentures - "ARN.DB.B"

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