



INTERIM REPORT

Three and nine months ended September 30, 2010



ARCAN RESOURCES LTD.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Basis of Presentation

Arcan Resources Ltd. ("**Arcan**" or the "**Corporation**") is engaged in the exploration for, and the development and production of, petroleum and natural gas in Western Canada. Arcan was incorporated on October 9, 2003 and conducted operations as a private corporation until January 1, 2007, maintaining a June 30 year-end. On January 1, 2007 Arcan amalgamated with Desco Energy Ltd. and the amalgamated entity's year-end was established as December 31. The amalgamation resulted in Arcan becoming a public corporation and a reporting issuer, with its common shares commencing trading on the TSX Venture Exchange under the symbol 'ARN' on January 9, 2007.

This Management's Discussion and Analysis ("**MD&A**") is an explanation, through the eyes of management, of how Arcan performed during the periods covered by the unaudited interim financial statements of Arcan filed concurrently with this MD&A, and of Arcan's financial condition and future prospects. This MD&A is for the three and nine month periods ended September 30, 2010 as compared to the three and nine month periods ended September 30, 2009. The MD&A complements and supplements the financial statements of Arcan. For a full understanding of the financial position and results of operations of the Corporation, the MD&A should be read in conjunction with the unaudited interim financial statements for the three and nine month periods ended September 30, 2010 and 2009 together with the notes thereto as well as the audited financial statements for the year ended December 31, 2009 and 2008, together with the notes related thereto and other documents filed on SEDAR, including historical financial statements, the information circular dated April 22, 2010 relating to the Corporation's annual general and special meeting that was held on May 25, 2010 and the Corporation's annual information form dated April 22, 2010 for the year ended December 31, 2009. These documents are available at www.sedar.com under the Corporation's SEDAR profile.

The unaudited financial statements to which this MD&A relates have been prepared in accordance with Canadian Generally Accepted Accounting Principles ("**GAAP**"). In this MD&A, unless otherwise indicated, all monetary amounts disclosed are in Canadian dollars and all references to "\$" are to Canadian dollars.

Arcan's management is responsible for the integrity of the information contained in this report and for the consistency between the MD&A and the unaudited interim financial statements. In the preparation of these statements, estimates are necessary. Management believes these estimates have been based on careful judgments and have been properly presented. The unaudited interim financial statements have been prepared using policies and procedures established by management and management believes that they fairly reflect Arcan's financial position, results of operations and funds from operations.

Arcan's board of directors and audit committee have reviewed and approved the unaudited interim financial statements and MD&A for the three and nine month periods ended September 30, 2010. This MD&A is dated November 18, 2010. Readers are urged to carefully consider the legal advisories at the end of this MD&A.

Non-GAAP Measurements

Readers are cautioned that this 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 GAAP 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 outstanding to determine per share amounts. Operating and corporate netbacks are also presented. "Operating netbacks" represent Arcan's revenue, less royalties and operating expenses, and "corporate netbacks" represent Arcan's operating netback,

less realized economic hedging losses, general and administrative ("**G&A**") and interest expense, 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 GAAP and therefore are unlikely to be comparable to similar measures presented by other companies. Management believes that funds from operations and operating and corporate netbacks are useful supplemental measures as they provide an indication of the ability of Arcan to fund future growth through capital investment and/or 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 that of other companies, and, accordingly, may not be comparable.

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

Funds from Operations				
	Three Months Ended		Nine Months Ended	
(\$000's)	September 30, 2010	September 30, 2009	September 30, 2010	September 30, 2009
Cash flow from operating activities (per GAAP)	5,371	1,235	11,588	4,699
Change in non-cash working capital	2,282	(1,203)	3,392	(21)
Funds from operations	7,652	32	14,980	4,678

Third Quarter 2010 Highlights

- Record production of 2,740 boe per day for the three months ended September 30, 2010, up 115% from the 1,274 boe per day for the three months ended September 30, 2009 and up 41% from the 1,943 boe per day for the three months ended June 30, 2010.
- Operating netbacks rose to \$39.98 per boe (revenue of \$67.87 per boe and operating cost of \$11.95 per boe) for the three months ended September 30, 2010 up 126% from \$17.67 per boe for the three months ended September 30, 2009 and 10% from \$36.31 per boe for the three months ended June 30, 2010.
- Funds from operations increased to \$7.7 million (\$0.10 per diluted share) for the three months ended September 30, 2010 up from \$0.03 million (\$0.00 per diluted share) in the three months ended September 30, 2009 and up 70% from \$4.5 million for the three months ended June 30, 2010.
- The Corporation focused on the Swan Hills Beaverhill Lake light oil reef play ("**Swan Hills**"), drilling three (2.6 net) new horizontal wells in the three months ended September 30, 2010 and has drilled a total of 12 (10.1 net) horizontal wells in Swan Hills as of September 30, 2010.
- Subsequent to the end of the third quarter, Arcan plans on utilizing three drilling rigs to commence the next phase of drilling operations which is estimated to include three wells prior to the end of 2010 and up to nine additional wells in the first quarter of 2011. The first well in this next phase, Arcan's thirteenth horizontal well, has already finished drilling at (02-02) 04-02-68-9W5 and completion operations on this well are anticipated to commence shortly. Well number 14 is drilling within Deer Mountain Unit #2 (the "**DM Unit**") and is Arcan's first dual leg horizontal well. Well number 15 is the first horizontal well in the Morse River Unit #1 (75% interest) (the "**Morse Unit**") where there is existing production infrastructure and an approved water flood already implemented. Well 16 is anticipated to be spudded shortly inside of the Ethel oil pool (100% interest) in the center of Arcan's large undeveloped land base lying to the south of the DM Unit.

- Subsequent to the end of the quarter, Arcan closed an equity financing, raising \$50 million through the issuance of 10.4 million common shares at \$4.80 per share, on November 5, 2010.
- As at November 18, 2010, Arcan has entered into financial oil contracts for a total production of 2,000 barrels per day for fiscal 2011 through collars with a Canadian WTI \$70.00 floor and an approximate \$100.00 ceiling.

Financial and Operating Summary

	Three Months Ended		Nine Months Ended	
	September 30, 2010	September 30, 2009	September 30, 2010	September 30, 2009
Financials (\$000s except per share amounts)				
Oil and NGL sales	16,607	5,894	34,940	17,001
Natural gas sales	500	652	2,214	2,485
Total petroleum and natural gas revenue	17,107	6,546	37,154	19,486
Cash flow from operating activities	5,371	1,235	11,588	4,699
Funds from operations ¹	7,652	32	14,980	4,678
Per share basic ¹	0.10	0.00	0.23	0.12
Per share diluted ¹	0.10	0.00	0.23	0.12
Net loss	(1,355)	(1,408)	(3,151)	(4,013)
Per share basic	(0.02)	(0.04)	(0.05)	(0.11)
Per share diluted	(0.02)	(0.04)	(0.05)	(0.11)
Capital expenditures – cash	28,386	3,111	120,461	6,516
Total assets	269,833	146,130	269,833	146,130
Total liabilities	111,361	61,360	111,361	61,360
Shareholders' equity	158,472	84,770	158,472	84,770
Bank loan	55,141	41,360	55,141	41,360
Net debt and working capital	78,270	42,622	78,270	42,622
Operating				
Production:				
Crude oil (barrels per day)	2,523	913	1,785	1,027
Natural gas (Mcf per day)	1,301	2,166	1,619	2,130
Total (boe per day) (6:1)	2,740	1,274	2,055	1,382
Average realized price:				
Crude oil (\$ per barrel)	71.55	70.18	71.70	60.63
Natural gas (\$ per Mcf)	4.18	3.27	5.01	4.27
Combined average (incl. processing revenue) (\$ per boe)	67.87	55.85	66.23	51.64
Netback (\$ per boe)				
Petroleum and natural gas sales	67.87	55.85	66.23	51.64
Royalties	15.94	17.15	15.80	12.09
Operating and transportation expenses	11.95	21.03	13.44	14.34
Operating netback	39.98	17.67	36.99	25.21
Realized economic hedging losses – cash	-	4.11	-	1.86
G&A expenses – cash	7.50	9.07	7.96	7.65
Interest expense – net	2.07	4.21	2.27	3.07
Corporate netback	30.41	0.28	26.76	12.63
Common Shares (000s)				
Shares outstanding, end of period	75,418	37,869	75,418	37,869
Weighted average shares ² - basic	75,245	37,829	66,297	37,829
- diluted	75,245	37,829	66,297	37,829

Notes:

- (1) The reader is referred to the section – "Non-GAAP Measurements" in this MD&A.
- (2) In computing the net loss per diluted share in the respective periods, nil shares were added to the weighted average number of shares outstanding because they were anti-dilutive.

Overview

Arcan's production increased throughout the third quarter of 2010 as new wells were tested and brought on-stream. For the three months ended September 30, 2010 Arcan experienced record production and oil weighting along with improvements in cash flow and operating and corporate netbacks. In the third quarter of 2010, production averaged 2,740 boe per day with operating netbacks averaging \$39.98 per boe on an Edmonton light sweet oil price of \$73.51 per barrel. Based on a 92% light oil weighting, Arcan posted an increased cash flow of \$7.7 million for the third quarter of 2010. By the end of the third quarter of 2010, 11 of Arcan's 12 new horizontal oil wells in Swan Hills were on-stream and the twelfth well was tied in on October 25, 2010. Over the first nine months of 2010, production has increased 49% to 2,055 boe per day from 1,382 boe per day in the same period in 2009. Production gains combined with a 28% commodity price increase have both contributed to Arcan's 91% increase in revenues to \$37.2 million from \$19.5 million leading to a 215% increase in corporate netbacks to \$15.0 million for the nine months ended September 30, 2010 from \$4.8 million for the nine months ended September 30, 2009.

Arcan's activities in Swan Hills commenced in September 2005 and developed with vertical well technology until December 9, 2009 when Arcan spudded its first multi-stage fracture horizontal well in Swan Hills at 9-29-68-8W5 ('9-29'). Arcan has invested \$120 million in its capital program for the nine months ended September 30, 2010 including, on March 31, 2010, an acquisition of 81 net sections of offsetting and contiguous lands in Swan Hills (the "**Acquisition**") at a cost of \$52.8 million to Arcan. The Acquisition lands combined with Arcan's existing lands provides Arcan with over 150 net sections of land on this play. In addition to the Acquisition, Arcan has drilled and completed 12 (10.1 net) horizontal wells and its extended water injection. Arcan anticipates its capital program could reach up to \$150 million in 2010 as three drilling rigs are deployed on our Swan Hills development program. Arcan continues to be focused on developing Swan Hills and estimates drilling up to 12 additional horizontal wells across its land base by the end of the first quarter of 2011.

Operations Update

Arcan has completed drilling its thirteenth well at (02-02) 04-02-68-9W5 ('4-02') and has moved that rig to the Morse Unit to drill Arcan's the first horizontal well in that unit. Arcan owns a 75% working interest in the Morse Unit which is comprised of seven sections of land, has existing oil battery and water handling facilities as well as an Energy Resources Conservation Board ("**ERCB**") approved waterflood in place. Arcan's first horizontal multi-stage fracture well in the Morse Unit is at (02-31) 13-31-66-9W5 ('13-31') and is offsetting four recent multi-stage horizontal wells drilled by competitors on adjacent lands. A second drilling rig is drilling Arcan's first bilateral multi-stage fracture well at (13-30) 07-30-68-8W5 in the DM Unit where Arcan has an 81% working interest. Arcan is awaiting a third drilling rig with which Arcan expects to spud a new horizontal well in the vicinity of the Ethel oil pool in 67-8-W5. Arcan anticipates that all three of these wells will be drilled and completed by December 31, 2010. Arcan will continue to evaluate and adjust drilling, length, and completion technologies. Adjustments include recognizing that a 1,000 metre leg attracts a 5% royalty for the first 80,000 barrels and a 1,500 metre leg has a 5% royalty for the first 90,000 barrels, translating into approximately \$500,000 in incremental royalty savings for an additional few days of drilling and a few additional fractures.

Arcan anticipates utilizing three drilling rigs until break-up in the spring, with one rig working in the DM Unit and the other two rigs working to develop the Ethel area. Arcan estimates that each drilling rig can drill approximately one horizontal well per month and the three rigs are estimated to drill nine wells in the first quarter of the 2011 drilling program. After drilling an estimated 12 new horizontal wells by the end of first quarter of 2011 Arcan will have 24 wells into Swan Hills. Arcan will review results from its fourth quarter 2010 and first quarter 2011 drilling before commencing the next drilling phase.

Arcan continues to implement water injection in the DM Unit by converting two vertical wells to injectors in the fourth quarter of 2010 to maintain voidage replacement. Arcan anticipates tying-in production in the first quarter of 2011 to the DM Unit facilities and is in the process of applying for waterflood approval in the Ethel pool with implementation expected to begin late in 2011. Waterflood investments must continue to be a high priority for Arcan in order to achieve the desired 40% recovery of the original oil-in-place. To

achieve its ongoing development plans Arcan closed a \$50 million equity financing on November 5, 2010 and increased its Credit Facility (as defined herein) from \$70 to \$100 million on September 30, 2010.

Arcan also continues to build a drill ready inventory and to plan two to three years ahead for drilling and new production facilities in the Ethel area. Arcan has 20 well locations which are drill ready, has surveyed 30 more, and is in the process of surveying a further 40 additional well locations. These existing inventory efforts are expected to set up a significant drilling inventory for 2011 and into 2012. Arcan's development of 12 horizontal wells in the first three quarters of 2010 was a significant operational success and speaks to the repeatability of the play. Each of these wells has a single 800 to 1,500 metre horizontal leg and was or will be completed using seven to 14 multi-stage acid fractures.

As at September 30, 2010, Arcan had 15 full-time office employees and five full-time field employees.

Production Update

Arcan continues to monitor and evaluate the performance of the 12 new horizontal producing wells. Statistically three of the wells have now been on production in excess of six months and the average production rate for the three wells over their first six month period of production is 282 boe per day per well. Eight of Arcan's new horizontal wells have been on production in excess of three months and the average production rate for these eight wells over their first three months of production is 327 boe per day per well. These production rates fall within Arcan's previously announced expected well performance which stated Arcan's internal economic analysis shows a 10 to 12 month payout and an estimated one year cumulative production number of 70,000 to 100,000 boe and potential ultimate recovery of 400,000 to 600,000 boe per well with water flood support resulting in a rate of return of 125% to 200% per well. Results and economic analysis indicate an estimated average production rate for a well over that first year to be approximately 200 to 300 boe per day. This estimated production rate at the end of the first year is anticipated to have an arrested decline in subsequent years due to the reservoir pressure maintenance from the existing or anticipated waterflood activities. These estimates continue to be based upon the current horizontal production data, over 30 years of vertical well production and waterflood history from the DM Unit and as well as adjacent Swan Hills production which historically has shown very low production declines over a 30 to 40 year reserve life index.

In an ongoing effort to maximize production from the new horizontal wells, Arcan is drilling out the existing fracture seats and fracture balls on the majority of the currently producing horizontal wells. These re-entries commenced subsequent to the end of the quarter, in October 2010, utilizing a coil tubing drilling rig and taking production off-line for up to two weeks per well. The operation involves the removal of surface production equipment with a service rig to prepare for the operation, the drilling of the fracture balls with a coil tubing unit, swabbing to recover drilling fluids and reinstallation of the surface equipment. Early results from these operations show positive production gains and the procedure is expected to be completed on all 12 wells by mid-December. The short term production outages caused by these operations will affect Arcan's fourth quarter and annual average production averages; however, Arcan anticipates the operation will have a positive impact on well economics as well as 2010 exit production. During these operations, production is expected to be maintained at approximately 3,000 boe per day and all 12 wells should be back on-stream by mid December 2010. On new wells Arcan anticipates that it will drill out the fracture seats and fracture balls immediately after completing fracturing operations and prior to initial production.

Overview of the Arcan's Swan Hills Core Area

Swan Hills - The Complex

Located in north-central Alberta, approximately 200 kilometres northwest of Edmonton, the main portion of the Swan Hills complex was developed in the 1950's and 1960's. The reef complex is over 80 kilometres long covering over 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 was developed through vertical drilling and has undergone extensive waterflood operations and recovered over 40% of the oil-in-place. As

announced by the Alberta provincial government, the reef is now to be developed under CO₂ flood as part of its \$2 billion carbon capture and storage fund, through the Swan Hills Synfuels project. Because the Swan Hills pools hold such large volumes of original-oil-in-place, each percentage point increase in the overall recovery factor represents significant incremental production and reserves with low geological risk.

Swan Hills - The Land

Arcan's land base extends over 24 kilometres north/south along the Swan Hills reef trend with over 50 sections of Arcan's land base already proven productive through vertical well control. Arcan's working interest in the DM Unit is currently 81%. The DM Unit commenced production in 1964 with unitization occurring in 1984. The DM Unit has only just started primary recovery. The DM Unit is comprised of just over nine sections of land and is situated at the northernmost tip of Arcan's 150 net section land base which is immediately adjacent and to the south of its existing infrastructure in the DM Unit – making Arcan the largest undeveloped land holder on the Swan Hills oil play. Through an understanding of the old well bores drilled into the Beaverhill Lake formation, Arcan mapped a continuous reef structure extending from the DM Unit through its 100% working interest lands to other producing wells to the south. Historically, the DM Unit wells were drilled vertically and supported by an injection wells to establish long life production patterns. The application of the horizontal multi-stage fracture has significantly enhanced the production profile and pool economics. Recognizing the potential long-term viability of this asset, Arcan built a new 4,000 barrel per day battery recently upgraded to handle 8,000 barrels per day total fluid as well as a 5,000 pounds per square inch centralized water injection system covering the DM Unit.

Swan Hills - The Reserves

As Arcan has drilled its horizontal multi-stage fracture wells after December 31, 2009, the related impact is not reflected in the proved producing year-end reserve report. To date, the DM Unit which covers 9.5 sections of land, has recovered approximately 3.9 million boe ("**MMboe**"). This amount represents approximately 10% of the original oil-in-place estimate of GLJ Petroleum Consultants Ltd. of approximately 39 MMboe or approximately four MMboe per section. Offsetting units with over 40 years of production history have proven over six MMboe of oil-in-place per section and have recovered more than 35% of their estimated original oil-in-place, and are believed capable of 45% ultimate recovery under vertical well development and waterflood. Arcan estimates oil-in-place of four to ten MMboe per section and up to a 40% recovery under waterflood realizing a potential recovery of 400,000 to 600,000 barrels oil per well based on a four horizontal wells per section development program.

Arcan anticipates that a large portion of its land base to the south of the DM Unit will also have similar reserves and economic profiles. Arcan's technical team has completed an in depth analysis of existing vertical wells drilled into the Beaverhill Lake formation across Arcan's land base. This work included detailed petrophysical and core analysis plus the analysis of existing production and reservoir pressure data plus the recently acquired well data from Arcan's 100% multi-stage fracture horizontal wells at 6-09-67-8W5 and 10-27-67-8W5. This data has been integrated into a three dimensional geological and reservoir model for a large portion of Arcan's land base giving Arcan's management confidence in the potential productivity of the reservoir and the effectiveness of a waterflood on the lands offsetting DM Unit.

Hamburg and McLeod, Alberta

Arcan discovered the Hamburg GG oil pool in February 2006, and is the operator and owns a 50.25% working interest in this 41° API sweet oil pool. There is an approved waterflood scheme in place and Arcan is currently injecting over 3,000 barrels of water per day water to restore pool voidage. Arcan has infill development opportunities to drill in this pool as well as exploration opportunities in the surrounding area and expects these operations to commence this program as economic conditions warrant.

McLeod is a multi-zone liquids rich gas prone area and Arcan has interests in five (3.9 net) natural gas wells in this area and is producing approximately 400 thousand cubic feet ("**Mcf**") (70 boe net) per day.

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

Fiscal quarter ended ⁽¹⁾	2010			2009			2008	
	Sept.	June	March	Dec.	Sept.	June	March	Dec.
Operating								
Oil and NGLs (barrels per day)	2,523	1,674	1,142	1,001	913	1,061	1,110	1,102
Price (\$/barrel)	71.55	68.13	77.35	73.80	70.18	63.98	49.36	63.55
Natural gas (Mcf per day)	1,301	1,613	1,951	2,105	2,166	2,772	1,444	2,199
Price (\$/Mcf)	4.18	4.60	5.91	5.20	3.27	4.09	6.17	8.19
Barrels of oil equivalent (boe per day)	2,740	1,943	1,468	1,352	1,274	1,523	1,350	1,468
Financial (\$000's, except per share amounts)								
Revenues								
Petroleum and natural gas	17,107	11,056	8,992	7,804	6,546	7,209	5,731	8,099
Royalties	(4,017)	(2,491)	(2,352)	(2,554)	(2,010)	(1,275)	(1,277)	(1,881)
Interest and other income	-	-	3	1	-	2	1	(220)
Realized loss on commodity contracts	-	-	-	(737)	(481)	(222)	-	-
Unrealized gain (loss) on commodity contracts	(1,019)	-	-	531	1,228	(1,115)	(644)	-
Net revenues	12,071	8,565	6,643	5,045	5,283	4,599	3,810	5,998
Expenses								
Operating	3,012	2,143	2,388	2,672	2,465	1,593	1,352	2,416
General and administrative	1,891	1,542	1,034	788	1,063	959	863	1,086
Stock-based compensation	1,122	1,124	438	391	166	193	193	337
Interest	522	370	382	380	494	398	272	291
Accretion	202	194	108	103	104	105	101	99
Depletion and depreciation	6,853	4,139	3,219	2,795	2,680	3,098	2,720	3,036
Total expenses	13,602	9,512	7,569	7,130	6,972	6,346	5,501	7,265
Income (loss) before income taxes	(1,531)	(947)	(926)	(2,085)	(1,689)	(1,747)	(1,690)	(1,269)
Future income tax expense (reduction)	(176)	44	(122)	(354)	(281)	(433)	(400)	(495)
Net income (loss)	(1,355)	(991)	(804)	(1,730)	(1,408)	(1,314)	(1,290)	(772)
Net income (loss) per share- basic	(0.02)	(0.01)	(0.02)	(0.04)	(0.04)	(0.03)	(0.03)	(0.02)
Net income (loss) per share- diluted	(0.02)	(0.01)	(0.02)	(0.04)	(0.04)	(0.03)	(0.03)	(0.02)
Funds from operations	7,652	4,501	2,826	667	32	2,680	1,966	1,987
Per share – basic and diluted	0.10	0.06	0.06	0.02	0.00	0.07	0.05	0.05
Cash flow from (used in) operating activities (per GAAP)	5,371	3,669	2,548	(371)	1,235	2,102	1,361	4,590
Operating Netbacks (\$/boe)								
Petroleum and natural gas revenues	67.87	62.52	68.07	62.74	55.85	52.01	47.16	59.95
Royalties	15.94	14.09	17.81	20.53	17.15	9.20	10.51	13.93
Operating and transportation expenses	11.95	12.12	18.08	21.48	21.03	11.50	11.12	17.88
Operating Netbacks	39.98	36.31	32.18	20.73	17.67	31.31	25.53	28.15
Total assets (\$000's)	269,833	244,234	227,067	151,251	146,130	145,729	150,398	149,724
Capital expended (\$000's)	28,386	21,240	70,835	4,979	3,111	229	3,177	9,980
Debt and working capital (\$000's)	(78,270)	(57,263)	(40,908)	(34,779)	(42,622)	(40,414)	(42,073)	(40,406)
Shares (000's)	75,418	75,173	74,928	47,940	37,869	37,869	37,869	37,869

Note:

(1) The reader is referred to the section – "Non-GAAP Measurements" in this MD&A.

Results of Operations

Arcan invested \$28.4 million of capital in the third quarter of 2010, primarily in the Swan Hills horizontal drilling program.

Drilling

	Drilling		Success rate (%) (gross)	Working interest (%)
	Gross	Net		
Q1 / 2010	4	2.8	75	70
Q2 / 2010	7	5.7	100	81
Q3 / 2010	3	2.6	100	87
Year to Date 2010	14	11.1	93	79

In the third quarter of 2010, Arcan drilled three gross (2.6 net) wells. All of these three wells were horizontal oil wells drilled in Swan Hills, with one of these being a 100% interest well.

	Production					
	Three Months Ended			Nine Months Ended		
	September 30, 2010	September 30, 2009	Change (%)	September 30, 2010	September 30, 2009	Change (%)
Oil and NGL (barrels per day)	2,523	913	176	1,785	1,027	74
Natural gas (Mcf per day)	1,301	2,166	(40)	1,619	2,130	(24)
Total (boe per day)	2,740	1,274	115	2,055	1,382	49
Oil as a % of total volumes	92	72	-	87	74	-

Arcan's average production rate for the third quarter of 2010 was 2,740 boe per day, a 115% increase from the third quarter of 2009 average of 1,274 boe per day and a 41% increase over the second quarter 2009 average of 1,943 boe per day. Oil production increases in the three and nine month periods ended September 30, 2010 more than offset natural gas declines, as compared to the three and nine month periods ended September 30, 2009. Arcan's average production rate for the first nine months of 2010 was 2,055 boe per day, a 49% increase from the first nine months of 2009 average of 1,382 boe per day. Production was higher in the 2010 periods over the 2009 periods due to volumes acquired in the Acquisition and production from the new horizontal wells more than offsetting vertical well shut-ins in the Swan Hills area. Volumes of approximately 400 boe per day acquired in the Acquisition were included commencing April 1, 2010.

Arcan's capital expenditures continue to be focused towards Swan Hills as oil prices have remained stable and elevated compared to natural gas prices. Year-to-date capital expenditures continue to be focused towards Arcan's oil properties as oil prices have continued to remain stable and elevated as compared to natural gas prices. Arcan expects the majority of its efforts for the remainder of 2010 and into 2011 will be directed to expanding the Swan Hills light oil production base and water injection. Arcan's oil and natural gas liquids ("NGLs") weighting was 92% for the third quarter of 2010, and it is estimated to be above 90% light oil in the fourth quarter of 2010 as the new horizontal oil wells and the Acquisition expanded Arcan's oil production rates. After taking into account down-time relating to drilling out fracture balls, Arcan estimates the average production rate for the final quarter of 2010 to be 2,800 to 3,200 boe per day.

Netbacks

The Corporation considers corporate netbacks to be an indication of ability to produce oil and natural gas profitably to earn a return on capital invested and is one of Arcan's three sources of funding (the others

being raising debt and equity). Commodity price increases of 22% and volume increases of 115% were the main factors causing the significant gain in corporate netbacks for the third quarter of 2010 over the third quarter of 2009. While Arcan expects commodity price fluctuations over the upcoming year, overall oil price levels are expected to remain relatively stable at \$70 to \$90 per barrel and royalty rates are expected to decrease as royalty rate reductions by the Alberta provincial government become effective January 1, 2011 and the new well incentive program provides for a 5% royalty cap on up to 100,000 barrels of production per well. Operating costs are also expected in the \$8 to \$12 per boe range based on higher volumes covering fixed costs and economies of scale. Arcan estimates that at a \$70 oil price less the 5% royalty of \$4 and a \$12 operating cost, the new horizontal wells are contributing \$54 per barrel to netbacks. These factors, as well as Arcan's growing oil production, are expected to increase the netbacks received by Arcan for the balance of 2010.

Netbacks						
	Three Months Ended			Nine Months Ended		
\$ thousands	September 30, 2010	September 30, 2009	Change (%)	September 30, 2010	September 30, 2009	Change (%)
Revenue	17,107	6,546	161	37,154	19,486	91
Royalties	4,017	2,010	100	8,861	4,563	94
Operating expenses	3,012	2,465	22	7,543	5,410	39
Operating netbacks	10,078	2,071	387	20,750	9,513	118
Realized economic hedging loss	-	481	-	-	703	-
G&A - cash	1,891	1,063	78	4,468	2,886	55
Interest expenses - net	522	494	6	1,274	1,161	10
Corporate netbacks	7,665	33	-	15,008	4,763	215
Netbacks - \$ per boe						
Revenue	67.87	55.85	22	66.23	51.64	28
Royalties	15.94	17.15	(7)	15.80	12.09	31
Operating expenses	11.95	21.03	(43)	13.44	14.34	(6)
Operating netbacks	39.98	17.67	126	36.99	25.21	47
Realized economic hedging loss	-	4.11	-	-	1.86	-
G&A - cash	7.50	9.07	(17)	7.96	7.65	4
Interest expenses	2.07	4.21	(51)	2.27	3.07	(26)
Corporate netbacks	30.41	0.28	-	26.76	12.63	112

Arcan's operating netback, defined as sales revenue, less royalties and operating expenses, was \$10.1 million in the third quarter of 2010, a 387% percent increase from \$2.1 million recorded in the third quarter of 2009 and a 57% increase over the \$6.4 million in the second quarter ended June 30, 2010 mainly due to increases in volumes. Arcan's operating netback on a per boe basis was \$39.98 in the third quarter of 2010, a 126% percent increase from \$17.67 per boe recorded in the third quarter of 2009. The increase in operating netback was due to a 22% increase in price combined with decreases in royalties and operating costs on a per boe basis in the third quarter of 2010 as compared to the same period in 2009. Arcan's operating netback on a per boe basis was 10% percent higher than the \$36.31 per boe recorded in the second quarter of 2010. The increase in operating netback over the second quarter of 2010 was due a 1% reduction in operating costs combined with a nine percent increase in prices partially offset by a 13% increase in royalties per boe.

Arcan's operating netback for the first nine months of 2010 was \$20.8 million, a 118% percent increase from \$9.5 million recorded in the first nine months of 2009 mainly due to increases in prices and volumes. Arcan's operating netback on a per boe basis was \$36.99 in the first nine months of 2010, a 47% percent increase from \$25.21 per boe recorded in the first nine months of 2009. The increase in operating netback was due to a 28% increase in price combined with a 49% increase in volumes in the first nine months of 2010 as compared to the same period in 2009. The impact of price increases has been moderated by the rising Canadian dollar versus the decreasing U.S. dollar in 2010. The move to oil weighting has significantly increased Arcan's exposure to price upside in oil both in 2010 and in 2009.

The net effect to Arcan was higher netbacks from oil than would have been achieved through natural gas as natural gas prices continue to wane below \$30 per boe.

Operating netbacks from oil were \$41.16 per boe and natural gas were (\$0.27) per boe in the third quarter of 2010 versus \$17.91 per boe for oil and were negative per boe for natural gas in the third quarter of 2009. Operating netbacks from oil were \$38.22 per boe and from natural gas were \$13.85 per boe in the first nine months of 2010 versus \$26.90 per boe for oil and almost zero per boe for natural gas in the first nine months of 2009. Operating netbacks from oil were \$37.59 per boe and from natural gas were \$14.82 per boe during the second quarter ended June 30, 2010. Arcan's oil netbacks were stronger than natural gas netbacks for all periods mainly due to commodity pricing.

Arcan's corporate netback, defined as operating netback, less realized economic hedging gains and losses, G&A and interest (income less expense), was \$7.7 million in the third quarter of 2010 compared to \$0.03 million in the third quarter of 2009. The large increase from 2009 related mainly to commodity prices and volume increases. On a per boe basis, the corporate netback was \$30.41 per boe in the third quarter of 2010 compared to \$0.28 per boe in the third quarter of 2009 and \$25.50 per boe in the second quarter 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, 2010 and 2009 are as follows:

Operating Netbacks by Area						
Area	Three Months Ended September 30, 2010			Three Months Ended September 30, 2009		
	Hamburg	Swan Hills	McLeod	Hamburg	Swan Hills	McLeod
Daily Production (boe)	456	2,205	78	625	634	11
Revenue (\$ per boe)	57.76	71.26	31.15	42.71	69.93	NM
Royalties (\$ per boe)	19.07	15.73	3.37	10.94	24.69	NM
Operating Costs (\$ per boe)	9.68	11.85	28.05	23.77	17.56	NM
Operating Netbacks (\$ per boe)	29.01	43.67	(0.27)	8.00	27.68	NM

Arcan has mainly focused on its oil properties from early in 2008 through into 2010 as netbacks from its oil properties continue to outpace natural gas netbacks. On a year-to-date basis, production from Hamburg is 549 boe per day, McLeod is 95 boe per day and Swan Hills is 1,412 boe per day, reducing (23%) and increasing 36% and 122%, respectively, over the same period in 2009.

Revenues

Arcan posted higher production revenues for the quarter ended September 30, 2010 versus the same quarter in 2009. The 115% increase in production volumes and 22% increase in price resulted in an increase in revenue of 161% to \$17.1 million in the third quarter of 2010 from the \$6.5 million recorded in the third quarter of 2009 and was up from the \$11.1 million in the second quarter of 2010. Year-to-date 2010 production revenues were higher versus the same period in 2009. The 49% increase in production volumes and 28% increase in price resulted in increased revenue of 91% to \$37.2 million in the first nine months of 2010 from the \$19.5 million recorded in the first nine months of 2009.

Revenue and Realized Prices						
	Three Months Ended			Nine Months Ended		
(\$000's)	September 30, 2010	September 30, 2009	Change (%)	September 30, 2010	September 30, 2009	Change (%)
Oil and NGL	16,607	5,894	182	34,940	17,001	106
Natural gas	500	652	(23)	2,214	2,485	(11)
Total petroleum and natural gas revenue	17,107	6,546	161	37,154	19,486	91
\$ per boe						
Oil and NGL (per boe)	71.55	70.18	2	71.70	60.63	18
Natural gas (per Mcf)	4.18	3.27	28	5.01	4.27	17
Total petroleum and natural gas revenue (per boe)	67.87	55.85	22	66.23	51.64	28
Benchmarks						
WTI (U.S.\$ per barrel)	76.09	68.14	12	77.58	57.21	36
Edmonton Light Sweet (\$Cdn. per barrel)	73.51	71.74	2	76.32	62.82	21
Alberta Plant Gate (per Mcf)	3.41	2.83	20	3.97	3.64	9
Cdn\$ per U.S.\$.9624	.9100	6	.9655	.8580	13

Commodity Prices

In the third quarter of 2010, Arcan realized average revenue per boe of \$67.87 as compared to \$55.85 per boe recorded in the third quarter of 2009 and \$62.52 per boe in the second quarter of 2010. Arcan realized an average of \$71.55 per barrel of oil and NGL in the third quarter of 2010, an increase of 2% from the \$70.18 per barrel realized in the third quarter of 2009 and up from the \$68.13 per barrel received in the second quarter of 2010. Arcan does truck the oil emulsion from each new well to a third party facility while the well is cleaning up, receiving a lower price through this clean-up period as the oil is mixed with drilling contaminants. After drilling contaminants have been produced and trucked away, Arcan ties in the well and processes the clean oil through its own facility, receiving higher pricing. This lower pricing period from the new wells is blended into the quarterly pricing Arcan received compared to an average Edmonton Light Sweet price of \$73.51 per barrel in the third quarter of 2010. Oil and NGL prices received by the Corporation moved consistent with benchmark prices for the relative periods. The Corporation realized an average natural gas price of \$4.18 per Mcf in the third quarter of 2010, a 28% increase from the \$3.27 per Mcf averaged in the third quarter of 2009 and a decrease from the \$4.60 per Mcf received in the second quarter of 2010. This is consistent with the price changes at the Alberta Plant gate for the same periods.

In the first nine months of 2010, Arcan realized average revenue per boe of \$66.23 compared to \$51.64 per boe recorded in the first nine months of 2009. Arcan realized an average of \$71.70 per barrel of oil and NGL in the first nine months of 2010, an increase of 18% from the \$60.63 per barrel realized in the first nine months of 2009. This compares to an average Edmonton Light Sweet price of \$76.32 per barrel in the first nine months of 2010. Oil and NGL prices received by the Corporation were consistent with benchmark prices for the relative periods. The Corporation realized an average natural gas price of \$5.01 per Mcf in the first nine months of 2010, a 17% increase from the \$4.27 per Mcf averaged in the first nine months of 2009. This is consistent with the price changes at the Alberta plant gate for the same periods.

Arcan continues to receive a premium for its heat content on natural gas. Arcan anticipates oil prices will remain above U.S.\$70.00 WTI and that gas prices may remain soft through the fall of 2010 at current levels, and recover to the \$5.00 to \$7.00 per Mcf over the winter period. The strength in commodity prices has been mitigated somewhat by the strength in the Canadian dollar in 2010 as U.S. WTI moved up 12% from the third quarter of 2009 to the third quarter of 2010, whereas Edmonton oil only gained 2% with the balance due to the dollar gaining 6% over that same period. Based on anticipated production volumes Arcan expects to post higher revenues for the balance of 2010 over the third quarter if WTI pricing exceeds \$80.00 per barrel based on anticipated production volumes for the balance of 2010.

All of Arcan's production for 2010 has been sold on the spot market. Arcan had no hedged volumes effective during the quarter ended September 30, 2010. In the third quarter of 2010, the Corporation entered into costless collar financial oil contracts. The contracts are all Canadian dollar WTI for a total volume of 2,000 barrels per day of oil with a floor price of \$70.00 per barrel and a ceiling price of approximately \$100.00 per barrel. These contracts are for the period from January 1, 2011 to December 31, 2011. For the period from April 1, 2009 to December 31, 2009 Arcan had an economic hedge of 500 barrels per day of oil at a fixed price of \$64.40 per barrel.

Royalties

Royalty expense in the third quarter of 2010 was \$4.0 million or 23% of revenue, compared to \$2.0 million or 31% of revenue in the third quarter of 2009, and was \$2.5 million or 23% of revenue in the second quarter of 2010. Royalty expense in the first nine months of 2010 was \$8.9 million or 24% of revenue, compared to \$4.6 million or 23% of revenue in the first nine months of 2009. Royalty rates fluctuate both based on the price of oil and gas and based on well production levels. On January 1, 2009 the Province of Alberta implemented the New Royalty Framework ("**NRF**") which increased Arcan's royalties to a maximum of 50% of revenue. On May 27, 2010 the Province of Alberta reduced the maximum royalty for oil to 40% of revenue effective January 1, 2011. As part of these modifications a new well incentive program was implemented allowing for 5% royalties on up to 100,000 barrels of production per well, or over \$2 million in royalty reductions per well.

Royalties have increased on a gross dollar basis over the third quarter of 2009 based on higher volumes but have decreased on a percentage of revenue and on a per boe basis over the third quarter of 2009 and due mainly to the 5% royalty rates applicable to new wells. Royalties have increased on a percentage of revenue, per boe and on a gross dollar basis over the first nine months of 2009 based on higher volumes and higher prices over the first nine months of 2009 due mainly to the higher royalty rates applicable under the NRF for higher production volumes and prices. Royalties are higher on a percentage of revenue, per boe and on a gross dollar basis over the second quarter of 2010 due to higher volumes, higher prices and the continued move to oil weighting. Arcan anticipates royalties will be blended lower on a percentage of revenue basis as more new horizontal wells are on production and after January 1, 2011 when rates on older wells are reduced.

The impact of royalties enacted by December 31, 2009 has been factored into Arcan's reserves estimates and Credit Facility and such calculations do not include the significant royalty reductions enacted on May 27, 2010. Based on fluctuating commodity prices, production rates, drilling profiles and fluctuating modifications to the NRF it is challenging to predict future royalty rates. Accordingly, Arcan anticipates its royalty rates for 2010 to be 20% to 30% depending on production volumes, prices and possible future royalty changes.

As part of the change in royalties in the past few years the Province of Alberta implemented a drilling credit whereby drilling new wells can create royalty credits that are recorded as a reduction to capital costs and are capped at 50% of royalties paid. Depending on production volumes and commodity prices, Arcan anticipates that it will be in a position to drill 12 to 18 horizontal wells so as to maximize its drilling credits of approximately \$10 million by the end of the first quarter of 2011.

Royalties						
	Three Months Ended			Nine Months Ended		
	September 30, 2010	September 30, 2009	Change (%)	September 30, 2010	September 30, 2009	Change (%)
Total (\$000s)	4,017	2,010	100	8,861	4,563	94
% of revenue	23	31	(26)	24	23	4
Per boe (\$)	15.94	17.15	(7)	15.80	12.09	31

Operating Expenses (including transportation)

Operating expenses in the third quarter of 2010 decreased to \$11.95 per boe from the second quarter of 2010 of \$12.12 per boe and were down from the \$21.03 per boe recorded in the third quarter of 2009. Operating costs have decreased from the second quarter on a per boe basis as volumes have increased in Arcan's Swan Hills facilities. Total operating expenses in the third quarter of 2010 were \$3.0 million, up 22% from \$2.5 million in the third quarter of 2009 and up from the \$2.1 million in the second quarter of 2010. Higher costs were more than offset with higher production volumes in the first nine months of 2010 resulting in an decrease in per boe operating costs of 6% to \$13.44 per boe of production from the \$14.34 per boe recorded in the first nine months of 2009. Total operating expenses in the first nine months of 2010 were \$7.5 million, up 39% from \$5.4 million in the first nine months of 2009 due to increased production volumes.

Arcan's operating expenses have increased since 2006 due to the Corporation's move toward oil-weighted production. Arcan's continued transition towards oil-weighted production from horizontal wells, including costs to operate the enhanced recovery, is anticipated to result in \$8 to \$12 per boe average operating costs per unit of production. Cost reductions are also anticipated as a result of the new free water knock out in Hamburg and in the prolific nature of the Swan Hills horizontal wells.

Operating Expenses (including transportation)						
	Three Months Ended			Nine Months Ended		
	September 30, 2010	September 30, 2009	Change (%)	September 30, 2010	September 30, 2009	Change (%)
Total (\$000s)	3,012	2,465	22	7,543	5,410	39
Per boe (\$)	11.95	21.03	(43)	13.44	14.34	(6)

Realized and Unrealized Loss on Commodity Contracts and Financial Instruments

Periodically Arcan utilizes economic hedges to protect a portion of its cash flows. In July of 2010, the Corporation entered into two costless collar financial oil contracts. The contracts are each for 500 barrels per day of oil with a floor price of \$70.00 per barrel and a ceiling price of \$100.05 and \$100.30 per barrel, respectively. In August of 2010, the Corporation entered into two costless collar financial oil contracts. The contracts are each for 500 barrels per day of oil with a floor price of \$70.00 per barrel and a ceiling price of \$100.00 per barrel each. All four contracts are Canadian dollar WTI for the period from January 1, 2011 to December 31, 2011. These contracts were entered into in the third quarter of 2010 and as the volumes relate to 2011, no realized loss was recorded but an unrealized loss of \$1.0 million was recorded for the quarter ended September 30, 2010. Arcan anticipates that these contracts will be marked-to-market at the end of each quarter with realized or unrealized gain or losses, if any, recorded in the statement of operations for each reporting period. Arcan had no production volumes hedged during the nine months ended September 30, 2010.

In March 2009, Arcan entered into a fixed price oil swap contract to receive \$64.40 per barrel in exchange for Canadian dollar WTI on oil production of 500 barrels per day for the period from April 1, 2009 to December 31, 2009. The realized loss was \$0.5 million and the unrealized gain on commodity contracts was \$1.2 million for the three months ended September 30, 2009. In 2009 Arcan had marked-to-market the fixed price swap and recorded gains and losses to the statement of operations for each reporting period. Arcan had a total realized loss of \$1.4 million in 2009 related to this hedge. No amounts have been realized in 2010.

Realized and Unrealized Losses on Commodity Contracts						
	Three Months Ended			Nine Months Ended		
	September 30, 2010	September 30, 2009	Change (%)	September 30, 2010	September 30, 2009	Change (%)
Realized loss (\$000's)	-	481	-	-	703	-
Per boe (\$)	-	4.11	-	-	1.86	-
Unrealized loss (gain) (\$000's)	1,019	(1,228)	(183)	1,018	531	92
Per boe (\$)	4.04	(10.48)	(139)	1.82	1.41	29

Cash General and Administrative ("Cash G&A")

Cash G&A expenses for the third quarter of 2010 decreased on a per boe basis to \$7.50 per boe from \$9.07 per boe in the third quarter of 2009 and decreased from \$8.72 per boe in the second quarter of 2010. The change year over year for the third quarter periods, on a per boe basis, resulted from a 78% total cost increase offset somewhat by a large increase in recoveries associated with higher capital expenditure activities. Total Cash G&A expenses for the third quarter of 2010, net of recoveries of \$0.4 million, were \$1.9 million, compared to \$1.1 million in the third quarter of 2009 after recoveries of \$0.1 million. In the second quarter of 2010, Cash G&A was \$1.5 million net of recoveries of \$0.2 million. Arcan had 20 full-time employees as at September 30, 2010 and September 30, 2009. Cash G&A expenses for the first nine months of 2010 increased on a per boe basis to \$7.96 per boe from \$7.65 per boe in the first nine months of 2009. Cash G&A totalled \$4.5 million in the first nine months of 2010 versus the \$2.9 million for the first nine months of 2009. The change year-over-year for the periods, was largely the result of \$0.8 million in bonuses paid in the third quarter of 2010, \$0.5 million in fees relating to the increased syndicated credit facility and a \$0.3 million charge from a third party firm Arcan had hired to determine potential avenues of debt financing for the Acquisition should the equity issuance prove unsuccessful. Cash G&A expense on a per boe and gross dollar basis is forecast to be lower in the fourth quarter of 2010 compared to the third quarter as higher volumes and no significant items are anticipated.

Total Cash G&A for three months ended September 30, 2010 of \$1.9 million was mainly comprised of wages of \$0.5 million, bonuses of \$0.8 million, bank fees of \$0.2 million, legal fees of \$0.1 million and rent of \$0.1 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.

G&A Expenses						
	Three Months Ended			Nine months Ended		
	September 30, 2010	September 30, 2009	Change (%)	September 30, 2010	September 30, 2009	Change (%)
Total (\$000s boe)	1,891	1,063	78	4,468	2,886	55
Per boe (\$)	7.50	9.07	(17)	7.96	7.65	4

Interest Expense

Interest expense in the third quarter of 2010 was \$0.5 million or \$2.07 per boe as compared to \$0.5 million or \$4.21 per boe in the third quarter of 2009 and \$2.09 per boe in the second quarter of 2010. Interest expense in the first nine months of 2010 was \$1.3 million or \$2.27 per boe as compared to \$1.2 million or \$3.08 per boe in the first nine months of 2009. The increase on interest expense was due to the increase in bank debt levels from \$41.4 million at September 30, 2009 to \$55.1 million at September 30, 2010. Arcan's management had increased debt and working capital deficit levels based on

operational success, but has closed an equity financing for gross proceeds of \$50 million on November 5, 2010 to reduce those debt levels. Arcan forecasts that the debt to annualized third quarter 2010 cash flow ratio of 2.6 to one will be lowered in the fourth quarter due to the equity financing offsetting additional drilling capital. Arcan estimates that interest expense will increase as higher debt levels are maintained and interest rates increase. Arcan had an effective interest rate of 4.75% on its debt facility at September 30, 2010 and 2009.

Based on Arcan's assets, the Corporation's Credit Facility was increased from \$50 million to \$70 million in May 2010 and increased again to \$100 million in September 2010. Arcan expects to carry bank debt as required as part of routine operations on an ongoing basis.

Interest Expense, Net						
	Three Months Ended			Nine months Ended		
	September 30, 2010	September 30, 2009	Change (%)	September 30, 2010	September 30, 2009	Change (%)
Total (\$000s)	522	494	6	1,274	1,164	9
Per boe (\$)	2.07	4.21	(51)	2.27	3.08	(26)

Funds from Operations

Funds from operations increased dramatically in the third quarter of 2010 to \$7.7 million from \$0.03 million in the third quarter of 2009, mainly due to volume and commodity price increases, and were up from \$4.5 million in the second quarter of 2010, mainly on volume increases. On a diluted per share basis, funds from operations increased to \$0.10 in the third quarter of 2010 from \$0.00 in the same period of 2009. Funds from operations increased by 220% in the first nine months of 2010 to \$15.0 million from \$4.7 million in the first nine months of 2009, mainly due to volume and commodity price increases. On a diluted per share basis, funds from operations were up significantly to \$0.23 in the first nine months of 2010 versus the \$0.12 in the first nine months of 2009, mainly due to volume and commodity price increases.

Arcan's method of calculating funds from operations may differ from that of other companies, and, accordingly, may not be comparable. Arcan determines funds from operations as cash flow from operating activities before changes in non-cash working capital as follows:

Funds from Operations						
	Three Months Ended			Nine months Ended		
(\$000's except per share and per boe)	September 30, 2010	September 30, 2009	Change (%)	September 30, 2010	September 30, 2009	Change (%)
Cash flow from operating activities (per GAAP)	5,371	1,235	335	11,588	4,699	147
Change in non-cash working capital	2,282	(1,203)	(290)	3,392	(21)	-
Funds from operations	7,652	32	-	14,980	4,678	220
Per share (\$)	0.10	0.00	-	0.23	0.12	92
Per share – diluted (\$)	0.10	0.00	-	0.23	0.12	92
Per boe (\$ Corporate netbacks less reclamation costs)	30.41	0.27	-	26.76	12.40	116

Funds from operations per share is calculated using the weighted average basic and diluted shares used in calculating earnings per share.

Stock-Based Compensation

Arcan recorded stock-based compensation expense of \$1.1 million in the third quarter of 2010 or \$4.45 per boe, calculated using the Black-Scholes option-pricing model. There was a significant increase in

expense over the third quarter of 2009 but relatively unchanged from the second quarter of 2010 as Arcan granted 2.9 million options on April 1, 2010 at an exercise price of \$4.20 per share and had not granted any options in the third quarter of 2009 or first quarter of 2010. These newly granted options have vesting terms with one-third of the options vesting on each of the first three anniversary dates and expire after five years. These options had a calculated value of \$3.06 per share based on the Black-Scholes option-pricing model. Changes to the various periods are as a result of inputs for calculations, varied amounts of option grants as well as relative numbers of options vesting during the periods. The elevated stock-based compensation expense related to these new options will be recorded quarterly over the next three years. Arcan granted a further 1.2 million options with a \$4.61 exercise price on November 5, 2010. These options also have vesting terms with one-third of the options vesting on each of the first three anniversary dates and expire after five years.

Stock-based compensation expense 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 stock-based compensation expense to increase as new options are issued, but decrease on a per unit basis as volumes increase. No stock-based compensation is capitalized.

Stock-Based Compensation Expense						
	Three Months Ended			Nine months Ended		
	September 30, 2010	September 30, 2009	Change (%)	September 30, 2010	September 30, 2009	Change (%)
Total (\$000's)	1,122	166	577	2,684	552	387
Per boe (\$)	4.45	1.41	215	4.78	1.46	227

Depletion, Depreciation and Accretion ("DD&A")

Depletion and depreciation are calculated based upon capital expenditures, production rates and reserves. Arcan recorded \$6.9 million or \$27.19 per boe in depletion and depreciation expense in the third quarter of 2010 based on production volumes of 252,062 boe. The 19% increase in depletion expense per boe as compared to the third quarter of 2009 is primarily the result of the Acquisition, production volumes and estimated reserves recognized in 2010. Depletion per boe was up over the second quarter of 2010, where Arcan recorded \$23.41 per boe. Arcan recorded \$14.2 million or \$25.33 per boe in depletion and depreciation expense in the first nine months of 2010 based on production volumes of 560,986 boe. The 12% increase in depletion expense per boe in the first nine months of 2010 as compared to the first nine months of 2009 is primarily the result of the Acquisition and changes in reserves estimated in 2010. The Corporation plans to decrease the depletion per boe amount in future years by adding reserves through an effective exploration and development program.

The Corporation excluded from its depletion and depreciation calculation costs associated with undeveloped land and seismic of \$26.7 million and included future development costs of \$42.8 million.

Arcan uses the asset retirement obligation method to record the present value of estimated clean-up and restoration costs for all of its facilities, including well sites and pipelines. The liability amount is decreased each reporting period due to the passage of time and the amount of accretion is charged to earnings in the period. Arcan recorded \$0.80 per boe of accretion expense in the third quarter of 2010, a decrease from \$0.89 per boe in the third quarter of 2009 as a result of higher volumes in 2010 compared to 2009. Arcan recorded \$0.90 per boe of accretion expense in the first nine months of 2010, an increase from \$0.82 per boe in the first nine months of 2009 as a result of higher accumulating obligations in 2010 compared to 2009. The estimated clean-up costs related to the properties in the Acquisition accounted for the majority of the change to the asset retirement obligation of \$10.3 million at September 30, 2010 from \$5.4 million at December 31, 2009.

Depletion, Depreciation and Accretion Expense						
Three Months Ended				Nine months Ended		
(\$000's except per boe)	September 30, 2010	September 30, 2009	Change (%)	September 30, 2010	September 30, 2009	Change (%)
Depletion and depreciation	6,853	2,680	156	14,211	8,498	67
Per boe (\$)	27.19	22.87	19	25.33	22.52	12
Accretion	202	104	93	504	310	62
Per boe (\$)	0.80	0.89	(10)	0.90	0.82	9

Income and Other Taxes

A future tax reduction of approximately \$0.2 million has been recognized in the financial statements for the third quarter of 2010, which relates to the Corporation experiencing a pre-tax loss of \$1.5 million for the quarter which included non-deductible stock based compensation of \$1.1 million. This is similar to the third quarter of 2009 comparative period when a pre-tax loss of \$1.7 million was recorded. A future tax reduction of approximately \$0.3 million has been recognized in the financial statements for the first nine months of 2010, which relates to the Corporation experiencing a pre-tax loss of \$3.4 million for the first nine months of 2010. In the first nine months of 2009 comparative period a pre-tax loss of approximately \$5.1 million was recognized and a future tax reduction of \$1.1 million was recorded. The Corporation also recorded a future tax asset of \$1.1 million on the tax effect of the share issue costs and a future tax liability of \$0.4 million on the tax effect of the flow-through shares issued in 2009. The provision for income taxes differs from the amount obtained by applying the combined federal and provincial income tax rate for 2010, which was 28.0% to pre-tax income due to non-deductible stock-based compensation and future tax rate differences.

As at September 30, 2010 the Corporation has approximately \$0.8 million in flow-through obligations outstanding.

Arcan has not paid any cash taxes since inception and estimates it has approximately \$220 million in tax pools. With capital spending in 2010 and reduced commodity prices, Arcan does not expect to be in a taxable position until 2012 at the earliest. However, Arcan is not able to forecast future possible changes in federal and provincial tax regimes.

Tax Expense (Reduction)						
Three Months Ended				Nine months Ended		
	September 30, 2010	September 30, 2009	Change (%)	September 30, 2010	September 30, 2009	Change (%)
Total (\$000's)	(176)	(281)	(37)	(254)	(1,115)	(77)
Per boe (\$)	(0.70)	(2.40)	(71)	(0.45)	(2.95)	(85)

Net Income (Loss)

The net loss for the third quarter of 2010 was \$1.4 million or \$0.02 per basic and diluted share, down slightly from the \$1.4 million net loss in the third quarter of 2009. The net loss for the first nine months of 2010 was \$3.2 million or \$0.05 per basic and diluted share, down from the \$4.0 million net loss in the first nine months of 2009. The improvement in operating netbacks was the primary contributor to these changes.

Net Income (Loss)						
Three Months Ended				Nine months Ended		
(\$000's except per boe)	September 30, 2010	September 30, 2009	Change (%)	September 30, 2010	September 30, 2009	Change (%)
Total	(1,355)	(1,408)	(4)	(3,151)	(4,013)	(21)
Per share - basic	(0.02)	(0.04)	(50)	(0.05)	(0.11)	(55)
- diluted	(0.02)	(0.04)	(50)	(0.05)	(0.11)	(55)
Per boe (\$)	(6.06)	(12.02)	(50)	(5.92)	(10.64)	(44)

Capital Expenditures

The third quarter of 2010 was focused mainly in Swan Hills. Capital expenditures for the third quarter of 2010 were \$28.4 million. This was up materially from the \$3.1 million spent in the third quarter of 2009. The capital program consisted of drilling twelve (10.1 net) horizontal wells in Swan Hills. Year to date in 2010 capital expenditures were \$120.5 million which included the \$52.8 million spent in respect of the Acquisition.

Capital Expenditure Summary

(\$ millions)	Q3 2010	Q2 2010	Q1 2010	YTD September 30, 2010
Land and seismic	1.8	0.5	4.3	6.6
Acquisitions	-	1.0	52.8	53.8
Drilling and intangibles	18.0	16.2	9.0	43.2
Facilities and equipment	8.6	3.6	4.7	16.9
Total Capital – cash expended	28.4	21.3	70.8	120.5

Property, plant and equipment on the balance sheet in the financial statements increased to \$250.9 million at September 30, 2010 from \$140.3 million at the end of 2009. This change reflects the increased capital expended of \$124.9 million (including \$4.4 million of asset retirement obligations) reduced by DD&A expense of \$14.3 million.

Liquidity and Capital Resources

Arcan incurred \$28.4 million on capital expenditures during the third quarter ended September 30, 2010 and generated \$7.7 million in funds from operations, up significantly from \$3.1 million in capital expenditures and the \$0.03 million in funds from operations generated during the third quarter ended September 30, 2009. Arcan expended \$120.5 million on the Acquisition and capital during the first nine months ended September 30, 2010 and generated \$15.0 million in funds from operations in the first nine months of 2010, up significantly from \$6.5 million in capital expenditures and the \$4.7 million in funds from operations generated during the first nine months ended September 30, 2009.

At September 30, 2010 Arcan had borrowed \$55.1 million from its \$100 million credit facility and had a working capital deficit including bank debt of \$78.3 million as at September 30, 2010. With its current 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 increased bank debt and working capital deficit levels from the \$34.8 million at December 31, 2009 through increased capital expenditures while the Acquisition was partially offset by the issuance of equity. Arcan's third quarter 2010 annualized funds from operations to net debt was 2.6 to one. Subsequent to the end of the third quarter, Arcan has closed an equity financing for gross proceeds of \$50.0 million on November 5, 2010 to reduce debt levels and expand its capital program. The ratio is expected to stay under 3:1 at the end of 2010.

In May 2010 Arcan entered into an agreement for a \$70 million syndicated credit facility (the "**Credit Facility**"). On September 30, 2010 the Credit Facility was increased further to \$100 million. The Credit Facility consists of a \$90 million syndicated revolving credit facility and a \$10 million revolving operating facility. The Credit Facility is syndicated between two banks and replaced Arcan's \$50.0 million credit facilities from prior to May 2010. The Credit Facility has a revolving period of 364 days from the closing

date, extendible annually. If not extended, the Credit Facility will automatically convert to a one year non-revolving term loan. This Credit Facility has been reflected in the Balance Sheet for the period ended September 30, 2010, which now classifies the Credit Facility as long term debt, moving Arcan's bank debt out of current liabilities. The Credit Facility is secured by a charge on all of Arcan's assets. The Credit Facility includes customary positive and negative covenants by Arcan in favour of the lenders.

On March 24, 2010 Arcan issued 26 million subscription receipts at \$2.50 per subscription receipt for gross proceeds of \$65.0 million. Each subscription receipt entitled the holder to receive, without payment of additional consideration, one common share of Arcan on the exercise or deemed exercise of the subscription receipt. All of the subscription receipts were exercised on March 31, 2010. The proceeds of this equity deal were primarily used to fund the Acquisition (at a cost of \$52.8 million) with the balance applied to Arcan's capital program. On November 5, 2010 Arcan issued 10.4 million common shares of Arcan at \$4.80 per common share for gross proceeds of \$50.0 million. The proceeds of this equity will be applied to Arcan's capital program.

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

Arcan estimates that it will be able to drill approximately one additional horizontal well per month inside of its existing cash flow base and is expanding its drilling activities based on expanding its Credit Facility and recent equity issuance going into the first quarter of 2011. As at November 18, 2010, Arcan has approximately \$21.5 million drawn under its Credit Facility.

Arcan expects its capital expenditure program to be significantly higher in 2010 than in 2009 and anticipates the expenditures to be financed through its Credit Facility and available funds from operations. Additional equity may be available in 2011 if the condition of the equity markets permit; however, the Corporation does not forecast requiring this cash inflow to complete its capital program. The capital program can be curtailed with no fixed commitments to ensure management of net debt levels.

Arcan will need to engage in a substantial capital expenditure program to develop its core oil and natural gas properties to their full potential. Arcan anticipates that future capital requirements will be funded through a combination of internal cash flow, debt and equity financing. There is no assurance that debt or equity financing will be available on terms acceptable to the Corporation to meet its capital requirements. To support its cash flow, Arcan purchased four costless collar financial oil contracts for a total of 2,000 barrels per day. The contracts are each for 500 barrels per day of oil with a floor price of \$70 per barrel and a ceiling price of approximately \$100.00 per barrel. These contracts are for the period from January 1, 2011 to December 31, 2011 and are all Canadian dollar WTI.

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

(\$ 000's)	Quarter Ended September 2010	Quarter Ended September 2009	Quarter Ended December 2009
Current assets	18,805	8,130	10,947
Less:			
Accounts payable and accrued liabilities	40,915	8,861	17,140
Bank loan	55,141	41,360	28,586
Fair value of commodity contracts	1,019	531	-
Working capital (deficiency)	(78,270)	(42,622)	(34,779)

The change in current assets and accounts payable reflect the higher activity levels incurred since the end of 2009. The change to the classification of the bank loan to long term in the first quarter of 2010 from current liabilities on the balance sheet in the financial statements reflects the change in nature of the Credit Facility from the previous revolving loan. The increase in working capital deficiency from year end reflects the increased capital expenditures and the Acquisition partially offset by the issuance of equity.

Related Party Transactions

In conjunction with the equity issuance by way of short form prospectus during the three months ended March 31, 2010, certain officers and directors acquired 68,000 common shares at \$2.50 per share.

In conjunction with the equity issuance by way of short form prospectus during the year ended December 31, 2009, certain officers and directors acquired an aggregate of 340,000 common shares at \$1.25 per share.

A share purchase loan of \$100,000 (2009 - \$100,000) is due from an officer of Arcan for the purchase of 40,000 common shares at a price of \$2.50 per common share. This loan is repayable, with interest calculated at the "Prescribed Rate" as determined by the Canada Revenue Agency, currently 1%, on or before April 3, 2012. This loan is secured by the underlying common shares.

Contractual Obligations

The Corporation has previously entered into, or is involved in, farm-in and/or farm-out agreements in the normal course of its business in 2010. As of the date of this MD&A, Arcan has no farm-in and/or farm-out commitments.

Arcan has the following commitments:

- (a) Future minimum lease payments relating to operating lease commitments are:

	\$
2010	59,625
2011	244,125
2012	249,750
2013	249,750
2014	249,750
2015 and thereafter	374,625

- (b) As a requirement of a sublease for office premises, Arcan has provided a letter of guarantee in favour of the lessor for a three year period on a declining basis. The remaining amount under the letter of guarantee is:

	\$
March 2010 to February 2011	60,000

Off-Balance Sheet Obligations

There were no off-balance sheet obligations at September 30, 2010.

Outstanding Share Data

Arcan's issued and outstanding share capital consists of the following:

	November 18, 2010	Quarter Ended September 30, 2010	Year Ended December 2009
Common shares	85,570,904	75,417,904	47,940,060
Warrants	-	123,500	586,631
Performance options	-	-	750,000
Stock options	8,458,501	7,285,167	4,671,166

Significant variations in share data and shareholders' equity from the year end of 2009 include the 26 million common shares issued as part of the Acquisition, 10.4 million shares issued on an equity deal on November 5, 2010, the exercise of 750,000 performance options, 535,000 warrants and 302,499 stock options and the grant of 2.9 million options on April 1, 2010 and a further 1.2 million options on November 5, 2010. Arcan warrants matured on October 22, 2010 at which time 60,000 unexercised warrants expired.

Other than the 750,000 performance options exercised by officers of the Corporation and the subsequent sale of 250,000 shares by one of those officers, none of the officers or directors of Arcan had exercised any stock options or sold any shares of Arcan during the year to date ended September 30, 2010, the year ended December 31, 2009 or during the period ended the date hereof.

Outlook

The repeatable application of the horizontal multi-stage acid fracture wells to Swan Hills is changing Arcan's asset base. The Acquisition and drilling, combined with water injection are expected to generate significantly increased production, recoveries and reserves. With investments in infrastructure already in place, Arcan now looks to continue to use its deep development inventory to increase value through horizontal multi-stage acid fracture wells in Swan Hills. Arcan's first round of drilling focused on the DM Unit lands. Arcan's plans for 2010 and 2011 include:

- increasing productive capacity at the battery and expanding its existing water injection scheme, expansion of drilling horizontal multi-stage fracture wells in Swan Hills on its 140 net sections of land outside of the DM Unit lands, building a road and pipeline system to connect production from the southern lands to existing infrastructure and tying in flared gas;
- continuing development and water injection in the Hamburg GG pool; and
- ongoing review of opportunities in the McLeod area.

Arcan plans to continue developing strategies to best exploit its land base over the long term. In the short term, Arcan intends to continue production on the 12 original horizontal wells drilled in Swan Hills, as well as drill an additional 12 horizontal wells using its existing debt and cash flow capabilities by the end of the first quarter of 2011. Management believes that the Corporation's strengths include over \$220 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.

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.

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 there from, will decline over time as the existing reserves are produced. A future increase in Arcan's reserves will depend not only on its 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 include competition, environmental factors, reservoir performance uncertainties, a complex regulatory and taxation environment and safety concerns.

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 since February 23, 2010. This limited time frame for data creates risks for unexpected production profiles. Arcan has the confidence that it can, due to production history through vertical well control, mitigate some of this operational risk.

Arcan attempts to manage its business risks. 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's management 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

For a full understanding of the Corporation's critical accounting estimates the MD&A should be read in conjunction with the audited financial statements for the years ended December 31, 2009 and 2008, together with the notes related thereto and the MD&A for the years ended December 31, 2009 and 2008.

Future Accounting Policies

International Financial Reporting Standards

Effective January 1, 2011, Canadian public companies are required to adopt International Financial Reporting Standards ("**IFRS**"). In the time leading up to the conversion date, some existing Canadian standards will change to converge with IFRS. Arcan's financial statements up to and including the December 31, 2010 financial statements will continue to be reported in accordance with GAAP as it exists on each reporting date. Financial statements for the quarter ended March 31, 2011, including comparative amounts, will be prepared on an IFRS basis.

A transition plan is in place to convert the financial statements to IFRS. Training has been provided to key employees and the Corporation continues to assess the effect of the transition on information systems, internal controls over financial reporting and disclosure controls and procedures. Systems and controls are being updated as IFRS accounting processes are implemented. Analysis and quantification of differences between IFRS and Arcan's current accounting policies is continuing. Some accounting policies may change on adoption of IFRS even though Arcan's current accounting policies are acceptable under IFRS. Changes in accounting policy may materially impact the financial statements.

In the first nine months of 2010, no changes were made to the Corporation's IFRS transition plan. Arcan began its conversion to IFRS during the second quarter and is continuing work on the project in the fourth quarter of 2010. Progress has been made regarding policy choices and quantification of differences, although adjustments require further work before being finalized.

There are several significant accounting policy changes anticipated on adoption of IFRS. Changes in IFRS prior to adoption may result in other accounting policy changes which could significantly impact the

financial statements. Numerous accounting policy changes will be made under IFRS, with the most significant changes expected to include accounting for petroleum and natural gas ("**P&NG**"), assets and equipment accounting for business combinations and accounting for future taxes.

Petroleum and Natural Gas Assets

IFRS standards require that a Corporation choose to report their 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 will record P&NG assets at historic cost as calculated under GAAP on January 1, 2010.

Under GAAP, all P&NG assets are accounted for under the full cost accounting guideline. Under IFRS, P&NG assets will be divided into exploration and evaluation properties ("**E&E assets**") and petroleum and natural gas properties and equipment ("**development assets**"). E&E assets will initially be capitalized and accumulated pending determination of technical feasibility and economic viability. E&E assets will not be depreciated and will be carried at cost less any accumulated impairment losses. Development assets will be measured at cost less accumulated depletion and depreciation and any accumulated impairment losses.

Both E&E assets and development assets will be assessed to determine whether impairment losses exist under IFRS as at January 1, 2010. These impairment tests will differ from the current GAAP full cost ceiling test in several significant ways. Assets (including goodwill) will be allocated to Cash Generating Units ("**CGUs**") and a separate impairment test will be completed for each CGU identified. Under current GAAP the ceiling test is a two step test. The carrying value of assets is first compared to the undiscounted future cash flows. If the carrying value of the assets exceeds the undiscounted future cash flows, then the second step of the test is required whereby the assets are 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 of the assets and the value-in-use of the assets, which is a discounted cash flow measure. As a result, impairments will be 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.

Depreciation under GAAP is 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 will still be depleted using a unit of production method; however, significant components with different useful lives will be 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.

Under the full cost accounting guideline, gains or losses are 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.

The quantitative impact to Arcan of these changes to accounting for P&NG assets has not been finalized.

Business Combinations

Accounting for business combinations also differs under IFRS. Arcan intends to elect 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 under GAAP will be expensed under IFRS.

Deferred Income Taxes

Deferred income taxes are calculated under IFRS using a liability approach which is conceptually similar to GAAP however there are differences in the manner in which deferred income taxes are calculated. The impact of these changes is being assessed and has not been quantified.

Other Items

There are other accounting policy changes with potentially material impacts, including accounting for asset retirement obligations ("**ARO**") and accounting for Stock Based Compensation. The ARO calculation differs under IFRS in some respects. On initial adoption of IFRS, the ARO liability will be recorded at its revised amount and the difference from the amount recorded under GAAP will be recorded as an adjustment to retained earnings at January 1, 2010. Under IFRS – Stock Based Compensation, Arcan's options that vest in three instalments must be accounted for as though each instalment is a separate option issue. This will result in front end loading of compensation expense. In addition, an estimate of forfeitures must be taken into consideration in the expense.

Business Combinations

In January 2009, the Canadian Institute of Chartered Accountants issued Section 1582, Business Combinations. This section is effective January 1, 2011 and applies prospectively to business combinations for which the acquisition date is on or after the first annual reporting period beginning on or after January 1, 2011 for the Corporation. This section replaces Section 1581, Business Combination and harmonizes the Canadian standards with IFRS.

Consolidated Financial Statements and Non-Controlling Interest

In 2009, Section 1601 and Section 1602 were issued which replace the existing guidance under Section 1600, Consolidated Financial Statements. These standards provide guidance for preparing consolidated financial statements and for accounting for non-controlling interest in a subsidiary to a business combination. These standards are effective for business combinations occurring on or after January 1, 2011.

Legal Advisories

*Boes may be misleading, particularly if used in isolation. The calculation of barrels of oil equivalent ("**boe**") is based on a conversion ratio of six thousand cubic feet of natural gas to one barrel of oil based on an energy conversion primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.*

Additional information about the Corporation, including the Corporation's annual information form for the year ended December 31, 2009, is available 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 (collectively, "forward-looking information"). The use of any of the words "expect", "anticipate", "continue", "estimate", "guidance", "objective", "ongoing", "may", "will", "project", "should", "believe", "plans", "intends" and similar expressions are intended to identify forward-looking information. In particular, but without limiting the foregoing, this MD&A contains forward-looking information pertaining to the following: Arcan's income taxes, tax liabilities and tax pools; production volumes and product mix of Arcan's oil and gas production; the rate at which Arcan's existing wells will be tied in; Arcan's drilling inventory; oil and natural gas prices and Arcan's risk management programs; resource recovery; the timing and results of drilling operations; the impact of the Acquisition; the amount of asset retirement obligations; future liquidity and financial capacity and resources; cost and expense estimates; results from operations and financial ratios; cash flows; operating costs; financing of expenditures; expectations respecting commodity prices; royalty rates and their impact on Arcan's operations and results; future capital requirements; production methods including the use of certain technologies; and future growth, including development, exploration, and acquisition and development activities and related expenditures

The forward-looking information contained in this MD&A reflects 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 general continuance of current or, where applicable, assumed industry conditions; 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 accuracy of the estimates of Arcan's reserve volumes; future oil, natural gas and NGL prices; and certain commodity price and other cost assumptions. Specifically, Arcan bases the number of wells it will drill in the short term on current estimated rig availability and drilling locations that are estimated to be ready to be drilled. Arcan bases estimates of ultimate per well recoveries on evaluations, estimates and projections from historical per well recoveries in the Swan Hills, adjusted for internally interpreted impacts of horizontal multi-stage fracture applications. Arcan also recognizes that ongoing waterflood activities are important and attempts to incorporate the impact, timing and costs of these activities into its projection processes, again based on historical evidence and experience in the Swan Hills and the Western Canadian Sedimentary Basin. Arcan believes the material factors, expectations and assumptions reflected in the forward-looking information 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 included in this MD&A is not a guarantee of future performance and should not be unduly relied upon. Such forward-looking information involves 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 including, without limitation: the early stages of production for a number of Arcan's producing wells; uncertainty relating to future production levels; changes in commodity prices; unanticipated operating results or production declines; 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; 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 Arcan's annual information form for the year ended December 31, 2009, copies of which are available on Arcan's SEDAR profile at www.sedar.com. Readers are cautioned that the foregoing lists are not exhaustive. The impact of any one risk, uncertainty of factor on forward-looking information is not determinable with certainty as these factors are interdependent and management's future course of action will depend on the assessment of all information at that time.

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

ARCAN RESOURCES LTD.

Balance Sheets
(Unaudited)

	September 30, 2010	December 31, 2009
Assets		
Current assets:		
Accounts receivable	\$ 17,569,717	\$ 10,011,769
Prepays and deposits	950,201	935,313
Future income taxes	285,177	–
	<u>18,805,095</u>	<u>10,947,082</u>
Property, plant, and equipment (note 1)	251,027,472	140,304,312
	<u>\$ 269,832,567</u>	<u>\$ 151,251,394</u>
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 40,914,992	\$ 17,140,125
Bank loans (note 2)	–	28,585,629
Fair value of commodity contracts (note 7)	1,018,491	–
	<u>41,933,483</u>	<u>45,725,754</u>
Bank loans (note 2)	55,141,230	–
Asset retirement obligations (note 3)	10,315,237	5,370,818
Future income taxes	3,970,923	4,687,265
	<u>111,360,873</u>	<u>55,783,837</u>
Shareholders' equity:		
Share capital (note 4)	157,665,351	93,714,116
Share purchase loan (note 4)	(100,000)	(100,000)
Contributed surplus (note 5)	6,283,617	4,080,040
Deficit	(5,377,274)	(2,226,599)
	<u>158,471,694</u>	<u>95,467,557</u>
Commitments (notes 4 and 8)		
Subsequent event (note 9)		
	<u>\$ 269,832,567</u>	<u>\$ 151,251,394</u>

See accompanying notes to financial statements.

ARCAN RESOURCES LTD.

Statements of Operations, Comprehensive Loss and Retained Earnings (Deficit)
(Unaudited)

	Three months ended		Nine months ended	
	September 30,		September 30,	
	2010	2009	2010	2009
Revenue:				
Petroleum and natural gas	\$ 17,106,874	\$ 6,545,846	\$ 37,154,415	\$ 19,485,841
Interest and other revenue	252	254	4,125	2,446
Royalties	(4,017,365)	(2,010,170)	(8,861,119)	(4,562,536)
Unrealized gain (loss) on commodity contracts (note 7)	(1,018,491)	1,227,835	(1,018,491)	(531,496)
Realized loss on commodity contracts (note 7)	-	(481,180)	-	(703,016)
	12,071,270	5,282,585	27,278,930	13,691,239
Expenses:				
Operating	3,011,677	2,464,765	7,542,633	5,409,925
General and administrative	3,012,768	1,228,950	7,151,583	3,437,253
Interest	521,937	493,630	1,274,385	1,163,537
Accretion	202,208	104,746	503,763	310,497
Depletion and depreciation	6,853,621	2,680,240	14,211,066	8,497,855
	13,602,211	6,972,331	30,683,430	18,819,067
Loss before income taxes	(1,530,941)	(1,689,746)	(3,404,500)	(5,127,828)
Future income tax reduction	175,990	281,343	253,825	1,114,781
Loss and comprehensive loss	(1,354,951)	(1,408,403)	(3,150,675)	(4,013,047)
Retained earnings (deficit), beginning of period	(4,022,323)	911,377	(2,226,599)	3,516,021
Deficit, end of period	\$ (5,377,274)	\$ (497,026)	\$ (5,377,274)	\$ (497,026)
Loss per share (note 4):				
Basic	\$ (0.02)	\$ (0.04)	\$ (0.05)	\$ (0.11)
Diluted	\$ (0.02)	\$ (0.04)	\$ (0.05)	\$ (0.11)

See accompanying notes to financial statements.

ARCAN RESOURCES LTD.

Statements of Cash Flows
(Unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Cash provided by (used in):				
Operating:				
Loss	\$ (1,354,951)	\$ (1,408,403)	\$ (3,150,675)	\$ (4,013,047)
Items not involving cash:				
Depletion and depreciation	6,853,621	2,680,240	14,211,066	8,497,855
Stock-based compensation	1,121,713	165,708	2,683,934	551,532
Accretion	202,208	104,746	503,763	310,497
Unrealized loss (gain) on commodity contracts	1,018,491	(1,227,835)	1,018,491	531,496
Future income tax reduction	(175,990)	(281,343)	(253,825)	(1,114,781)
Reclamation costs	(12,848)	(1,487)	(32,725)	(85,758)
	7,652,244	31,626	14,980,029	4,677,794
Change in non-cash working capital	(2,281,719)	1,203,517	(3,392,244)	20,875
	5,370,525	1,235,143	11,587,785	4,698,669
Financing:				
Bank loan	21,237,845	1,732,336	26,555,601	11,727,011
Issue of common shares, net of costs	461,394	-	62,723,184	-
	21,699,239	1,732,336	89,278,785	11,727,011
Investing:				
Property, plant and equipment	(28,386,244)	(3,110,880)	(67,657,657)	(6,516,387)
Property acquisition (note 1)	-	-	(52,803,188)	-
Change in non-cash working capital	1,316,480	143,401	19,594,275	(9,909,293)
	(27,069,764)	(2,967,479)	(100,866,570)	(16,425,680)
Change in cash	-	-	-	-
Cash, beginning of period	-	-	-	-
Cash, end of period	\$ -	\$ -	\$ -	\$ -
Supplementary disclosure:				
Interest paid	\$ 844,275	\$ 607,587	\$ 1,609,129	\$ 1,208,935

Cash is defined as cash and cash equivalents.

See accompanying notes to financial statements.

ARCAN RESOURCES LTD.

Notes to Financial Statements

Three and nine months ended September 30, 2010 and 2009
(Unaudited)

Arcan Resources Ltd. ("Arcan" or the "Company") is a publicly listed company involved in the business of oil and natural gas exploration, development and production in Canada. The interim financial statements of Arcan have been prepared by management in accordance with Canadian generally accepted accounting principles. The interim financial statements have been prepared following the same accounting policies and methods of computation as the financial statements for the year ended December 31, 2009. The following disclosure is incremental to the disclosure included with the December 31, 2009 financial statements. These interim financial statements should be read in conjunction with the financial statements and notes thereto for the year ended December 31, 2009.

In January 2006, the AcSB announced its decision to replace Canadian GAAP with International Financial Reporting Standards ("IFRS") for all Canadian Publicly Accountable Enterprises ("PAE"). On February 13, 2008, the AcSB confirmed January 1, 2011 as the official changeover date for PAE's to commence reporting under IFRS. Although IFRS is principles-based and uses a conceptual framework similar to Canadian GAAP, there are significant differences and choices in accounting policies, as well as increased disclosure requirements under IFRS. The Company continues to monitor and assess the impact of IFRS on its financial statements. The quantitative impact of IFRS on the Company's financial statements is not reasonably determinable at this time.

1. Property, plant and equipment:

	September 30, 2010	December 31, 2009
Petroleum and natural gas properties	\$ 309,371,028	\$ 184,436,802
Accumulated depletion and depreciation	(58,343,556)	(44,132,490)
	<u>\$ 251,027,472</u>	<u>\$ 140,304,312</u>

At September 30, 2010, petroleum and natural gas properties included undeveloped properties of \$26.7 million (September 30, 2009 - \$10.6 million), which have been excluded from the depletion calculation. Future development costs for proved reserves of \$42.8 million (September 30, 2009 - \$37.0 million) have been included in the depletion calculation.

During the nine months ended September 30, 2010, the Company acquired certain working interests in petroleum and natural gas properties for cash of \$52.8 million, with associated asset retirement obligations of \$4.1 million.

ARCAN RESOURCES LTD.

Notes to Financial Statements, Page 2

Three and nine months ended September 30, 2010 and 2009
(Unaudited)

2. Bank loans:

The Company has a \$90 million syndicated extendible, revolving term credit facility and a \$10 million non-syndicated extendible revolving operating term credit facility for total available credit facilities of \$100 million (the "Facilities"). The Facilities are available on a revolving basis until May 31, 2011. On May 31, 2011, 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 \$100 million borrowing base is subject to a semi-annual and annual review by the bank. 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. 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, 2010. This facility had an effective interest rate of 4.75% at September 30, 2010 (September 30, 2009 – 4.75%).

3. Asset retirement obligations:

The Company's asset retirement obligations result from net ownership interests in petroleum and natural gas assets including well sites, gathering systems and processing facilities. The Company estimates the total undiscounted amount of cash flows required to settle its asset retirement obligations at September 30, 2010 is \$20.3 million (December 31, 2009 - \$11.4 million), which will be incurred between 2011 and 2019. The majority of the costs will be incurred between 2011 and 2016. An inflation rate of 2% (December 31, 2009 – 2%) was used to inflate the costs, and a credit-adjusted risk-free rate of 8% - 10% (December 31, 2009 – 8% - 10%) was used to calculate the fair value of the asset retirement obligations.

ARCAN RESOURCES LTD.

Notes to Financial Statements, Page 3

Three and nine months ended September 30, 2010 and 2009
(Unaudited)

3. Asset retirement obligations (continued):

	September 30, 2010	December 31, 2009
Balance, beginning of period	\$ 5,370,818	\$ 4,785,428
Liabilities incurred	401,237	230,818
Liabilities incurred on acquisition (note 1)	4,072,144	-
Accretion expense	503,763	414,170
Changes in estimates	-	33,116
Reclamation costs	(32,725)	(92,714)
Balance, end of period	\$10,315,237	\$ 5,370,818

4. Share capital:

(a) Authorized:

Unlimited number of common shares without nominal or par value.

(b) Common shares issued and outstanding:

	Number of Shares	Amount
Balance, December 31, 2008	37,868,560	\$ 81,677,404
Issued pursuant to prospectus	9,000,000	11,250,000
Issued pursuant to flow-through private placement	1,071,500	1,500,100
Share issue costs	-	(973,244)
Tax effect of share issue costs	-	259,856
Balance, December 31, 2009	47,940,060	\$ 93,714,116
Issued pursuant to prospectus	26,000,000	65,000,000
Exercise of performance options	750,000	750,000
Exercise of warrants	452,011	866,217
Exercise of stock options	275,833	441,791
Stock-based compensation on exercise of warrants, performance options and stock options	-	480,357
Share issue costs	-	(4,334,824)
Tax effect of share issue costs	-	1,122,719
Tax effect of flow-through shares issued in 2009	-	(375,025)
Balance, September 30, 2010	75,417,904	\$157,665,351

ARCAN RESOURCES LTD.

Notes to Financial Statements, Page 4

Three and nine months ended September 30, 2010 and 2009
(Unaudited)

4. Share capital (continued):

(c) Warrants:

The Company has outstanding warrants that were issued to investors and agents, as commission, in certain equity financings. Each warrant is exercisable into one common share of the Company.

	Weighted average Exercise Price (\$)	Number of Warrants
Balance, at December 31, 2009 and 2008	1.93	586,631
Exercise of warrants	1.92	(452,011)
Expired	1.60	(11,120)
Balance, September 30, 2010	2.00	123,500

The following table indicates the number of exercisable warrants with exercise prices:

	Exercise Price (\$)	Number of Warrants
Issued July 2004	2.00	123,500

Subsequent to September 30, 2010, 63,500 warrants were exercised with the remaining 60,000 expiring on October 22, 2010.

(d) Flow-through shares:

On November 20, 2009, the Company issued 1,071,500 flow-through common shares for gross proceeds of \$1,500,100. Under the terms of the flow-through share agreements, the Company renounced the \$1,500,100 of qualifying petroleum and natural gas expenditures effective December 31, 2009 and has until December 31, 2010 to incur the expenditures. As at September 30, 2010, the Company has \$760,000 of qualifying expenditures remaining to incur.

(e) Share purchase loan:

A share purchase loan of \$100,000 (December 31, 2009 - \$100,000) is due from an officer of the Company for the purchase of 40,000 common shares at a price of \$2.50 per common share. This loan is repayable, with interest calculated at the "Prescribed Rate" as determined by the Canada Revenue Agency, currently 1%, on or before April 3, 2012. This loan is secured by the underlying shares.

ARCAN RESOURCES LTD.

Notes to Financial Statements, Page 5

Three and nine months ended September 30, 2010 and 2009
(Unaudited)

4. Share capital (continued):

(f) Stock options:

	Nine months ended September 30, 2010		Year ended December 31, 2009	
	Number of options	Weighted average exercise price	Number of options	Weighted average exercise price
Stock options outstanding, beginning of period	4,671,166	\$ 2.01	3,638,500	\$ 2.27
Granted	2,954,000	4.22	1,183,500	1.30
Exercised	(275,833)	1.60	-	-
Expired	(64,166)	3.06	(64,999)	2.96
Forfeited	-	-	(85,835)	2.93
Stock options outstanding, end of period	7,285,167	\$ 2.91	4,671,166	\$ 2.01
Exercisable at period-end	2,891,000	\$ 2.28	2,854,166	\$ 2.12

(g) Stock-based compensation:

The fair value of each option granted during the nine months ended September 30, 2010 was estimated on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions:

	2010	2009
Fair value of options granted (\$/option)	\$ 3.07	\$ -
Expected life of options (years)	5	-
Expected volatility (%)	94	-
Risk free rate of return (%)	2.88	-
Expected dividend yield (%)	Nil	-

(h) Performance options:

During the nine months ended September 30, 2010, 750,000 performance options were exercised at a price of \$1.00 per performance option for gross proceeds of \$750,000. No performance options remain at September 30, 2010.

ARCAN RESOURCES LTD.

Notes to Financial Statements, Page 6

Three and nine months ended September 30, 2010 and 2009
(Unaudited)

4. Share capital (continued):

(i) Per share amounts:

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

	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Weighted average number of shares – basic	75,245,426	37,828,560	66,296,618	37,828,560
Weighted average number of shares - diluted	75,245,426	37,828,560	66,296,618	37,828,560

In computing diluted per share amounts at September 30, 2010, 7,285,167 options (September 30, 2009 – 3,536,000 options), no performance options (September 30, 2009 – 750,000 performance options), and 123,500 warrants (September 30, 2009 – 586,631 warrants) were excluded for the calculation as their effect was anti-dilutive.

5. Contributed surplus:

	September 30, 2010	December 31, 2009
Balance, beginning of period	\$ 4,080,040	\$ 3,137,804
Stock-based compensation	2,683,934	942,236
Transfer to share capital on exercise of warrants, performance options and stock options	(480,357)	–
Balance, end of period	\$ 6,283,617	\$ 4,080,040

6. Related party transactions:

In conjunction with the equity issuance pursuant to the prospectus during the nine months ended September 30, 2010, certain officers and directors acquired 68,000 common shares at \$2.50 per share.

In conjunction with the equity issuance pursuant to the prospectus during the year ended December 31, 2009, certain officers and directors acquired 340,000 common shares at \$1.25 per share.

ARCAN RESOURCES LTD.

Notes to Financial Statements, Page 7

Three and nine months ended September 30, 2010 and 2009
(Unaudited)

7. Financial instruments:

Credit Risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Company's receivables from joint venture partners and petroleum and natural gas marketers. As at September 30, 2010 the Company's receivables consisted of \$8.1 million (December 31, 2009 - \$5.0 million) from joint venture partners, \$5.2 million (December 31, 2009 - \$2.0 million) of receivables from petroleum and natural gas marketers and \$4.3 million (December 31, 2009 - \$3.0 million) of other trade receivables.

The carrying amount of accounts receivable represents the maximum credit exposure. The Company has an allowance for doubtful accounts as at September 30, 2010 of \$0.1 million, consistent with the amount provided during the year ended December 31, 2009.

As at September 30, 2010 and December 31, 2009 the Company considers its receivables to be aged as follows:

Aging	September 30, 2010	December 31, 2009
Not past due (less than 120 days)	\$ 15,793,056	\$ 9,048,157
Past due (over 120 days)	1,776,661	963,612
Total	\$ 17,569,717	\$10,011,769

Liquidity risk

Accounts payable are considered due to suppliers in one year or less. Derivative contracts are also due to be settled with the respective counter-parties in one year at the estimated fair value on the balance sheet. Bank loans, which are subject to renewal after a 364-day revolving period, could be potentially due on May 31, 2012, if the Facilities are not renewed for the 364 day period, in which case the Facilities are converted to a one year term loan.

ARCAN RESOURCES LTD.

Notes to Financial Statements, Page 8

Three and nine months ended September 30, 2010 and 2009
(Unaudited)

7. Financial instruments (continued):

Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, commodity prices, and interest rates will affect the Company's net income or the value of financial instruments.

Foreign currency exchange rate risk

Foreign currency exchange rate risk is the risk that the fair value or future cash flows will fluctuate as a result of changes in foreign exchange risks.

The Company had no forward exchange rate contracts in place as at or during the nine months ended September 30, 2010 or the year ended December 31, 2009.

Commodity price risk

Commodity price risk is the risk that the fair value of future cash flows will fluctuate as a result of changes in commodity prices.

During the nine months ended September 30, 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. Two of the contracts have ceiling prices of \$100.00 per barrel Canadian and the other two contracts have ceiling prices of \$100.05 and \$100.30 per barrel Canadian, respectively. All contracts are for the period from January 1, 2011 to December 31, 2011. The Company recognized an unrealized loss of \$1,018,491 on the contracts as at and for the nine months ended September 30, 2010.

During the nine months ended September 30, 2009 the Company entered into a fixed price oil swap contract to receive \$64.40 per barrel in exchange for Canadian dollar WTI on oil production of 500 barrels per day for the period from April 1 to December 31, 2009. The Company recognized an unrealized loss of \$531,496 on the contract as at and for the nine months ended September 30, 2009. The Company also realized a loss on the contract of \$703,016 for the nine months ended September 30, 2009.

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, 2010, if the forward price of crude had been \$1.00 higher, net income for the period would have been approximately \$547,500 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.

ARCAN RESOURCES LTD.

Notes to Financial Statements, Page 9

Three and nine months ended September 30, 2010 and 2009
(Unaudited)

7. Financial instruments (continued):

Interest rate risk

Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in market interest rates. The Company is exposed to interest rate fluctuations on its bank debt which bears a floating rate of interest. As at September 30, 2010, if interest rates had been one hundred basis points lower with all other variables held constant, net income for the three and nine months ended would have been approximately \$93,000 (2009 - \$74,000) and \$216,000 (2009 - \$214,000) higher, respectively, due to lower interest expense. An equal and opposite impact would have occurred to net income had interest rates been one hundred basis points higher. The sensitivity is higher in 2010 as compared to 2009 because of an increase in outstanding bank debt.

The Company has no interest rate swap or financial contracts in place as at or during the nine months ended September 30, 2010 or the year ended December 31, 2009.

Capital management

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 \$158.5 million (December 31, 2009 - \$95.5 million), bank debt of \$55.1 million (December 31, 2009 - \$28.6 million) and a working capital deficiency excluding bank debt, of \$23.1 million (December 31, 2009 - \$6.2 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 or minus working capital, divided by funds from operations for the most recent calendar quarter, annualized (multiplied by four). Funds from operations is 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. 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.

ARCAN RESOURCES LTD.

Notes to Financial Statements, Page 10

Three and nine months ended September 30, 2010 and 2009
(Unaudited)

7. Financial instruments (continued):

As at September 30, 2010 and December 31, 2009, the Company's ratio of net debt to quarterly annualized funds from operations was 2.6 to 1 and 13.0 to 1, respectively. The Company's ratio of net debt to quarterly annualized funds from operations at quarter end and year end was above the 2 to 1 ratio that management targets to maintain due to significant capital spending in 2010 and decreased commodity prices combined with higher operating costs due to workovers in 2009.

The Company's bank completed its semi-annual borrowing base review on September 30, 2010, and the bank credit facility has been established at \$100 million. The next scheduled renewal is on or before May 31, 2011. The Company continually monitors its financing alternatives, and expects to finance its 2010 cash capital expenditures program from internally generated funds from operations, bank debt, and equity. Subsequent to September 30, 2010, the Company issued 10,421,875 common shares at a price of \$4.80 per share for gross proceeds of \$50,025,000, which will help to reduce the Company's net debt to quarterly annualized funds from operations ratio.

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

	September 30, 2010	December 31, 2009
Working capital deficiency (including bank debt)	\$ 78,269,618	\$ 34,778,672
Cash flow from operating activities	5,370,525	130,393
Change in non-cash operating working capital	2,281,719	537,141
Funds from operations	7,652,244	667,534
Annualizing factor	x4	x4
Annualized funds from operations	\$ 30,608,976	\$ 2,670,136
Ratio	2.6 to 1	13.0 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 subject to certain financial covenants (see note 2). 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.

ARCAN RESOURCES LTD.

Notes to Financial Statements, Page 11

Three and nine months ended September 30, 2010 and 2009
(Unaudited)

7. Financial instruments (continued):

Fair value of financial instruments

The Company's financial instruments as at September 30, 2010 and December 31, 2009 includes accounts receivable, accounts payable and accrued liabilities, derivative contracts, and bank debt. The fair value of accounts receivable and accounts payable and accrued liabilities approximate their carrying amounts due to their short-terms to maturity.

The fair value of financial contracts is determined by discounting the difference between the contracted price and published forward price rate curves as at the balance sheet date, using the remaining contracted notional volumes.

Bank debt bears interest as a floating market rate and accordingly the fair market value approximates the carrying value.

8. Commitments:

(a) Future minimum lease payments relating to operating lease commitments are:

2010	\$ 59,625
2011	244,125
2012	249,750
2013	249,750
2014	249,750
2015 and thereafter	374,625

(b) As a requirement of a sublease for office premises, the Company has provided a letter of Guarantee in favour of the lessor as follows:

March 2010 to February 2011	\$ 60,000
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9. Subsequent event:

Subsequent to September 30, 2010, the Company issued 10,421,875 common shares at a price of \$4.80 per share for gross proceeds of \$50,025,000.

Corporate Office

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Andy Fisher
Executive Vice President, Arcan Resources Ltd.

Robert J. Dales
Independent Director

J. Terry McCoy
Independent Director

Michael J. Laffin
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Corporate Secretary

Registrar and Transfer Agent

Valiant Trust Company

Stock Exchange Listing

TSX-V (symbol "**ARN**")

Legal Counsel

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