

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 company until January 1, 2007, maintaining a June 30 year end. On January 1, 2007 Arcan amalgamated with Desco Energy Ltd. with the amalgamated entity's year end established as December 31. The amalgamation resulted in Arcan becoming a public company and a reporting issuer, with its shares trading on the TSX Venture Exchange under the symbol 'ARN' beginning on January 9, 2007.

This management's discussion and analysis ("**MD&A**") is an explanation, through the eyes of management ("**Management**"), of how Arcan performed during the periods covered by the annual audited 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 months and year ended December 31, 2010, as compared to the same periods ended December 31, 2009. This MD&A complements and supplements the audited financial statements of Arcan for the years ended December 31, 2010 and 2009, together with the notes related thereto. For a full understanding of the financial position and results of operations of the Corporation, this MD&A should be read in conjunction with Arcan's audited financial statements for the years ended December 31, 2010 and 2009, together with the notes related thereto as well as Arcan's historical annual and interim financial statements, the information circular relating to the Corporation's annual general and special meeting to be held on June 1, 2011 and the Corporation's annual information form for the year ended December 31, 2010. These documents will be available at www.sedar.com under the Corporation's SEDAR profile.

Arcan's financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("**GAAP**") and, unless otherwise indicated, all amounts are in Canadian dollars. All estimates of reserves and future net revenue are derived from the independent oil and gas reserve report prepared by Arcan's independent reserve engineers GLJ Petroleum Consultants Ltd. ("**GLJ**") dated effective December 31, 2010 (the "**GLJ Report**"). Estimates of future net revenue and net asset value do not represent fair market value. Readers should carefully read the section "Non-GAAP Measurements" below and the sections "Legal Advisories" and "Forward-Looking Information and Statements" at the end of this MD&A.

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

Arcan's Board of Directors and Audit Committee have reviewed and approved the financial statements and MD&A. This MD&A is dated April 5, 2011.

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 is divided by the basic weighted average number of common shares of Arcan (each, a "**share**") 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.

These measures do not have any standardized meaning prescribed by GAAP and therefore may not 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.

Please see the section "Annual and Fourth Quarter Results of Operations – Netbacks" for a reconciliation between both operating netbacks and corporate netbacks to revenue.

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

Funds from Operations (\$000's)	Quarter Ended December 2010	Quarter Ended December 2009	Year Ended December 2010	Year Ended December 2009
Cash flow from (used in) operating activities (per GAAP)	8,044	(371)	19,631	4,327
Change in non-cash working capital	(285)	1,038	3,108	1,018
Funds from operations	7,759	667	22,739	5,345

Readers are cautioned that this MD&A contains the term "net asset value" ("NAV") which Management believes is a useful supplemental measure as it provides a measure of a value of the Corporation. Arcan's method for calculating NAV of \$5.56 per share (found by adding Arcan's \$467.9 million present value of proved plus probable reserves discounted at 10 percent, plus seismic of \$1.2 million at cost, plus land valued by Arcan at \$1,000 per acre for 86,400 acres in the Swan Hills totalling \$86.4 million, plus proceeds from 8.6 million stock options exercisable below the year end stock price of \$5.45 per share, less \$48.6 million of back debt and working capital deficiency for a total value of \$534.2 million divided by 96.1 million shares) may differ from that of other companies, and, accordingly, may not be comparable. This measure does not have any standardized meaning prescribed by GAAP and therefore are unlikely to be comparable to similar measures presented by other companies. Arcan's Management believes there is no GAAP measure that is comparable to the NAV calculation, although there are GAAP financial statement amounts used in the calculation that have been articulated in that section of the MD&A, and readers are cautioned in their use of the measure.

2010 Highlights

Highlights	Year Ended December 31, 2010	Year Ended December 31, 2009	Year Ended December 31, 2008
Financial (\$000's, except per share amounts)			
Petroleum and natural gas revenues	55,575	27,290	48,657
Cash provided by operating activities	19,631	4,328	23,969
Funds from operations ⁽¹⁾	22,739	5,345	24,553
Per share – basic ⁽¹⁾	0.32	0.14	0.65
Net income (loss)	(5,068)	(5,743)	7,001
Per share – basic	(0.07)	(0.15)	0.19
Per share – diluted	(0.07)	(0.15)	0.18
Bank loan	20,823	28,586	29,633
Total assets	289,775	151,251	149,724
Total liabilities	80,602	55,784	61,493
Shareholders' equity	209,174	95,468	88,231
Capital expenditures, net – cash	148,334	11,495	34,922
Shares outstanding	87,670	47,940	37,869
Weighted average – basic	70,306	39,502	37,543
Weighted average – diluted ⁽³⁾	70,306	39,502	38,525
Sales Volumes			
Crude oil and NGLs (bbls per day)	1,983	1,021	1,128
Natural gas (Mcf per day)	1,557	2,124	2,220
BOE per day ⁽²⁾	2,243	1,375	1,498

Notes:

- (1) The reader is referred to the section "Non-GAAP Measurements" in this MD&A.
- (2) The reader is referred to the section "Legal Advisories" in this MD&A.
- (3) Basic and diluted weighted average shares are the same in 2010 and 2009 as the Corporation incurred a loss in these periods. In 2008, 982,107 shares were included as dilutive securities as the outstanding warrants, stock options, and performance options were anti-dilutive.

Corporate Overview – The New Swan Hills

Currently, Arcan has a total of 24 horizontal wells covering over 30 kilometres, 15 (12.9 net) of which were multi-stage fractured and tested during 2010. Arcan's pace of operations has picked up significantly through 2010, and just recently, it has added operational engineering and geological staff to advance growth going into 2011. Activities through 2010 also translated to NAV growth to \$5.56 per share at December 31, 2010 from \$3.08 per share at December 31, 2009. Arcan believes that there is significant potential in its Swan Hills Beaverhill Lake ("**Swan Hills**") land base and that its first 24 wells have just begun to highlight the viability of its assets. To date, Arcan has identified over 400 additional drilling locations and expects that the continued development of its land base will secure further drilling locations.

Arcan's wells, on average, for the wells that were on for 30 days produced 360 BOE per day each, the 13 wells that were on for 60 days produced an average of 330 BOE per day each, the 13 wells that were on for 90 days produced an average of 280 BOE per day each and the nine wells that were on for 180 days produced an average of 200 BOE per day each. These wells, which were on for six months, produced about five percent natural gas and 95 percent light oil and had cumulative production of 36,000 BOE. On average, Arcan's wells are drilled to a total depth of approximately 4,000 meters with 1,000 to 1,500 meter horizontal legs and multi stage acid fractures utilizing ten to 15 stages. The average cost per well for drilling and multi-stage fracture, along with all associated equipment and tie-in was approximately \$4.7 million in the Deer Mountain Unit #2 ("**the Unit**"). To date, Arcan's wells have utilized Arcan-operated existing facilities including the recently upgraded 8,000 BOE per day oil battery at the Unit. The use of multi-stage fractured wells represents a shift in

the exploitation of the Swan Hills reef complex. These wells typically exhibit productive capability of up to eight times that of an average vertical producer at only two times the cost.

Arcan expended \$148.3 million on its properties and infrastructure during the year ended December 31, 2010, adding \$321.3 million to its reserves value, expanding its net asset value to \$534.2 million and increased average production to 2,243 BOE per day. For 2010, Arcan had record funds from operations of \$22.7 million and an operating netback of \$36.36 per BOE. For the three months ended December 31, 2010 production averaged 2,800 BOE per day as compared to the 1,352 BOE per day average production for the three months ending December 31, 2009. Arcan estimates production in the first quarter of 2011 to be approximately 2,600 BOE per day as compared to 1,468 BOE per day in the first quarter of 2010. For 2011, Arcan has budgeted capital expenditures of \$135 million. Arcan's 2011 budget contemplates adding 20 to 25 horizontal wells (nine of which have occurred in the first quarter) as well as pipeline and waterflood infrastructure. Arcan also expects that by early in 2012, it will significantly expand its water injection from the Unit into the Ethel area and has begun construction of production infrastructure to tie-in Ethel wells into the Unit's existing oil handling facilities.

Arcan experienced production issues in the first quarter of 2011. A third party pipeline which had shut-in approximately 700 BOE of production for the first quarter was repaired and the impacted Arcan production was back on-stream by the end of the quarter. Arcan also experienced well production issues with six of its horizontal wells in the Unit. Arcan has conducted workover operations on three of these wells in order to determine the reason behind the production issues. These operations have utilized several techniques to address these production issues. Two of these wells have been put back on production with the average well production increasing from 40 BOE per day to 100 BOE per day. Production is expected to increase with additional optimization of the pumping equipment and operations. The third well is currently back on-line and is recovering load fluid used during the workover. Initial results are positive with the well producing at rates of more than 125 barrels of oil ("**bbls**") per day with significant volumes of load fluid left to recover. Based on the results of these workovers Arcan has developed a plan to address production impairments in the remaining three wells currently experiencing production issues. As well, the technical staff has initiated a review of current drilling, completion, and production practices applied in the Swan Hills area. Based on the initial findings, Arcan believes that these production issues can be eliminated in order to ensure long term stable production and reserve recovery. Arcan's current stabilized production at the start of the second quarter of 2011 is 3,000 BOE per day with four producing horizontal wells shut-in due to drilling and completion activities being conducting on those pad-sites.

With its largest asset residing in the Swan Hills play, Arcan continues to strategically balance out its short and long term goals. In the short term, Arcan has focused much of its efforts close to existing facilities; however, over the longer term Arcan is working to balance this approach through proving up the center and corners of its asset base. Arcan has already conducted work on over 30 kilometres of the Swan Hills play, including the central portion, the western edge of the land block, as well as the northern portion. In the past few weeks Arcan has also added information on the southern portion with encouraging initial results from the re-entry well at 6-36-65-09W5 which tested over 400 BOE per day, has had a pump installed and is producing at approximately 160 BOE per day.

As of December 31, 2010, Arcan had \$48.6 million in debt and working capital. Arcan continues to work to manage growth against dilution and debt. In 2010, Arcan replaced its existing \$50 million bank line of credit with a syndicated \$100 million two year banking facility (the "**Credit Facility**") and, subsequent to the end of the year, secured \$86.25 million through an offering of 6.25 percent convertible unsecured subordinated debentures due February 28, 2016 ("**Debentures**"). Arcan is evaluating the growth of its production base in 2011 through a prudent level of investment based on anticipated cash flow and anticipates remaining within cash flow and it's Credit Facility through 2011 and, in addition, has utilized hedges to stabilize operations for 2011 and 2012.

As at December 31, 2010, Arcan had 17 full time office employees and four full time field employees. Arcan has added two new engineering staff, one geologist and one land person to its office employees since year end.

Overview of Arcan's Core Areas

Swan Hills –The Complex

The Swan Hills reef complex is located in north central Alberta, approximately 200 kilometres northwest of Edmonton. The main portion of Swan Hills was discovered and developed through vertical drilling in the 1950's and 1960's. The reef complex is over 50 miles 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 has undergone extensive waterflood operations and in many of its pools has recovered over 40 percent of the oil-in-place. 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 at low geological risk. The large original-oil-in-place and reservoir characteristics make this area a candidate for future development under a CO₂ flood, with pilot projects already underway.

Swan Hills – The Land

Arcan entered the Swan Hills play in 2005. Recognizing the potential of the play, Arcan started accumulating additional interests and in 2007, built new facilities to handle a large production base and implemented a waterflood in the Unit. This was followed by a large land purchase and farm-in during 2008. Rising oil prices since 2005 have helped solidify the economics in this area; however, the key change came with the successful application of horizontal drilling and multi-stage fracture technology. Arcan's land base extends over 40 kilometres along the Swan Hills reef trend. Arcan is utilizing the 70 pre-existing vertical well bores as well as a new 3D seismic program shot in the first quarter of 2011, to delineate its horizontal drilling activity. On March 31, 2010, Arcan acquired interests in 102 gross (81 net) sections of land with approximately 500 BOE per day of existing production for a cash purchase price of \$52.8 million (the "**Acquisition**"). An important part of the Acquisition was that these lands were additive to Arcan's current working interests and were adjacent to Arcan's existing land base. As a result of the closing of the Acquisition, Arcan has consolidated interests that total over 160 gross (150 net) sections of land on the Swan Hills play.

Swan Hills – The Reserves and Economics

Offsetting units with over 50 years of production history have recovered more than 35 percent of their estimated original oil-in-place, and are believed capable of 45 percent ultimate recovery under vertical well development and waterflood. These units have significant further upside potential from the application of multi-stage horizontal fracturing and possible future CO₂ injection schemes. Arcan's December 31, 2010 reserve report has 29 proven undeveloped locations with average gross proved plus probable net present value of \$6.1 million per horizontal well discounted at 10 percent. This does not reflect the significant upside in NPV that may be achieved through full waterflood development. Also identified in the reserve report is an additional five proven developed non-producing locations, bringing the total number of proved locations to 34 in the Swan Hills area. In 2010 horizontal drilling and capital expenditures were focused in the Unit where reserves had already been recorded on a vertical drilling basis. Drilling new horizontal wells in the Unit was not as effective in adding reserves as drilling outside of the Unit; however, they did significantly modify the production profile in the Unit and were in proximity to owned infrastructure and waterflood operations. The results from the waterflood and ten (8.1 net) wells in the Unit combined with proving the horizontal multi stage technology in five (4.8 net) wells outside of the Unit, translated into significant value growth in 2010. Further drilling off of the Unit and eventual waterflood on all of those lands is expected to continue to add to Arcan's recorded reserves. Operations for the first quarter of 2011 focused more heavily on the central portion of Arcan's land block in the Ethel area. Arcan estimates that for the remainder of 2011 it will prove up reserves as it continues to focus drilling in the Ethel area as well as including some drilling in the Morse River

Unit #1 and the undeveloped land base at Virginia Hills and South Swan Hills land blocks. By focusing drilling in these relatively undeveloped areas, Arcan anticipates strength in future reserve additions.

Swan Hills – Wells and Production

Arcan has drilled or re-entered 24 (21.3 net) horizontal wells to date, 23 (20.3 net) of which have been multi-stage fractured, and Arcan is currently drilling its 25th and 26th wells. In 2010, Arcan multi-stage fractured 15 (12.9 net) horizontal wells of which, ten (8.1 net) of the wells were in the Unit, two (2.0 net) wells were in Ethel and non-unit lands to the south of the Unit, one (0.8 net) well was in the Morse River Unit #1, one (1.0 net) well was at 04-02-66-9W5 and one (1.0 net) well was in the south west corner of Arcan's land base at 02-20-66-09W5.

In the first quarter of 2011 Arcan added nine (8.7 net) additional multi-stage fracture horizontal wells. Two (1.6 net) of the nine wells were drilled in the Unit with one (0.8 net) well drilling at the end of the quarter, six (6.0 net) wells were drilled in Ethel and one re-entry of older existing horizontal well was drilled at 06-36-68-08W5. Arcan anticipates further data and production volumes from these new wells throughout the second quarter of 2011. Arcan has identified additional re-entry candidates, anticipates utilizing two rigs during the break-up period and has a further ten to 15 horizontal wells budgeted for 2011, which will provide Arcan with an expected total of up to 40 multi-fractured wells in the Swan Hills play by the end of 2011.

Arcan has two types of well production profiles; wells on enhanced oil recovery ("EOR") recovery which are fully supported by waterflood and the new Ethel wells producing on primary recovery which are awaiting anticipated future implementation of an EOR scheme by early in the first quarter of 2012. Arcan's operations are focused on drilling wells and moving wells up this profile ladder to get them all fully supported by waterflood. Arcan believes that once these additional wells are fully supported by waterflood their production patterns will modify and move to a higher recovery of the original oil-in-place. Arcan's 12-29-68-8W5 ("12-29") well was Arcan's first horizontal multi-stage fractured well and has the longest production history of just over one year. The 12-29 well is fully supported by waterflood and has been tied into Arcan's operated facilities. The 12-29 well has a cumulative production of approximately 100,000 BOE to date. Arcan estimates that its new wells will reach pay-out at around 60,000 bbls factoring oil at \$100 per bbl less a \$5 royalty rate and operating costs of \$15 per bbl. A typical well producing under primary recovery without the benefit of an EOR scheme is Arcan's second well Ethel (5-34) 10-27-67-8W5 ("10-27") which came on-stream in May 2010. The 10-27 well averaged approximately 450 BOE per day over the first 30 days, 200 BOE per day over the first six months and cumulative production of almost 50,000 BOE on primary recovery in the first ten months. With current economics, Arcan estimates that its first quarter 2011 Ethel focused drilling program will have a pay-out of one year or less even on primary recovery and under a fully-developed waterflood recovery could ultimately recover 35 to 40 percent of the oil-in-place. Below are a series of charts and well-by-well details:

Wells Fractured in 2010 (Average 81% Working Interest in wells 2, 10, 14 and 15)

Well	Well ID	Date on	Cumulative (Gross BOEs)	BOE per day			Current or Capacity (Gross)
				First Month (Gross)	Average to date (hours) (Gross)	Average to date (calendar) (Gross)	
1	09-29-068-08W5	02/2010	93,294	400	300	240	200
2	10-27-067-08W5	05/2010	46,242	300	170	140	80
3	01-17-068-08W5	06/2010	38,620	350	190	130	100
4	08_30-068-08W5	07/2010	40,025	250	185	165	100

Well	Well ID	Date on	Cumulative (Gross BOEs)	BOE per day			Current or Capacity (Gross)
				First Month (Gross)	Average to date (hours) (Gross)	Average to date (calendar) (Gross)	
5	06-20-068-08W5	07/2010	30,029	300	150	110	125
6	05-28-068-08W5	07/2010	44,183	350	190	165	150
7	08-32-068-08W5	08/2010	26,371	200	125	115	75
8	09-30-068-08W5	07/2010	32,684	250	140	125	150
9	13-17-068-08W5	09/2010	36,418	400	325	190	100
10	06-09-068-08W5	09/2010	50,320	350	290	265	225
11	11-17-068-08W5	10/2010	22,141	300	175	125	100
12	06-30-068-08W5	10/2010	35,368	400	250	200	200
13	04-02-068-09W5	12/2010	21,303	200	290	235	200
14	13-31-066-09W5	02/2011	6,683	175	170	170	100
15	02-02-066-10W5 Re-entry	01/2011			-	-	80

Wells Fractured In 2011 To Date (100% Working Interest in Wells 17, 18, 21-23)

Well	Well ID	Date on	Cumulative (Gross BOEs)	BOE per day			Current or Capacity (Gross)
				First Month (Gross)	Average to date (hours) (Gross)	Average to date (calendar) (Gross)	
16	07-30-068-08W5 Dual Leg	03/2011		-	-	-	350
17	12-11-067-08W5			-	-	-	200
18	12-16-067-08W5			-	-	-	200
19	02-19-068-08W5			-	-	-	200
20	14-17-068-08W5			-	-	-	200
21	06-36-065-09W5 Re-entry			-	-	-	160
22	07-15-067-08W5	Fraced		-	-	-	200
23	02-20-067-08W5	Fraced		-	-	-	200

Wells Awaiting Fracture (81% Working Interest in Well 27, 100% Working Interest in Wells 22 to 26)

Well	Well ID	Date on	BOE per day				Current or Capacity (Gross)
			Cumulative (Gross BOEs)	First Month (Gross)	Average to date (hours) (Gross)	Average to date (calendar) (Gross)	
24	13-09-68-08W5	To Frac	-	-	-	-	200
25	08-20-068-08W5	Drilling	-	-	-	-	200
26	05-35-67-8W5	Drilling	-	-	-	-	200
27	02-27-065-08W5 Re-entry	To Frac	-	-	-	-	100
28	13-21-066-09W5 Re-entry	To Frac	-	-	-	-	100

Non- Horizontal Well Production:

Well	Well ID	Date on	BOE per day				Current or Capacity (Net)
			Cumulative (Gross BOEs)	First Month (Gross)	Average to date (hours) (Gross)	Average to date (calendar) (Gross)	
	Deer Mountain Unit #2 - Vertical Wells	-	-	-	-	-	600
	Morse River Unit #1 excluding well 14: 13-31	-	-	-	-	-	100
	Hamburg GG	-	-	-	-	-	400
	New13-08-96-9W6	-	-	-	-	-	100
	McLeod	-	-	-	-	-	50

To generally characterize the wells in the tables above under "current or capacity", Arcan has drilled or re-entered 24 (21.3 net) horizontal wells to date, 23 (20.3 net) of which have been multi-stage fractured, Arcan is currently drilling its 25th and 26th wells and two other wells have been identified for re-entry. In 2010, Arcan multi-stage fractured 15 (12.9 net) horizontal wells of which, ten (8.1 net) of the wells were in the Unit, two (2.0 net) wells were in the Ethel and non-unit lands to the south of the Unit, one (0.8 net) well was in the Morse River Unit #1, one (1.0 net) well was at 04-02-66-9W5 and one (1.0 net) well was in the south west corner of Arcan's land base at 02-20-66-09W5. Of the 23 wells which have been fractured to date, six wells experienced some operational issues, four wells are shut in to facilitate drilling off pad-sites, two new wells had initial test rates in excess of 600 BOE per day and the re-entry well tested over 400 BOE per day, all three of which are awaiting installation of production equipment, one drilled wells plus two re-entries are waiting fracture, two wells are currently drilling.

Arcan's production in Swan Hills averaged 1,648 BOE per day with \$42.65 per BOE operating netbacks for the year ended December 31, 2010 up from 623 BOE per day with \$28.93 per BOE operating netbacks in the year ended December 31, 2009.

Swan Hills – The Consolidated Outlook

Significant growth in 2010 was only the start of the development of Arcan's 160 (150 net) sections of land. Arcan has 24 new horizontal wells and estimates that it may have up to 400 more locations already available. The Swan Hills has long life light sweet 40° API oil that historically has provided up to 40 percent recoveries of the oil-in-place under waterflood. Arcan continues to work towards unlocking the potential magnitude of reserves to be booked and recovered through drilling and waterflood activities. The expected repeatability of the horizontal drilling and multi-stage fracturing technology is expected to convert the Swan Hills play from a long life light oil legacy resource play to a significant legacy growth opportunity. Vertical well control, combined with the new spring 2011 3D seismic shoot and geological mapping, increases Arcan's confidence in its development program. In addition to Arcan's development, offsetting area competitors continue to provide drilling, completion and operations data that Arcan will utilize to maximize its own understanding of the reef and ultimately shareholder value.

Hamburg, Alberta

In February 2006, Arcan discovered the Hamburg GG oil pool. Arcan now has a 50.25 percent working interest in the pool and is operator of the oil battery and waterflood in the GG pool. Arcan's wells in the Hamburg GG oil pool produce light sweet 41° API oil and natural gas and a majority are located within the waterflood scheme. Arcan enhanced its water injection in the pool in March of 2010 by converting a third well to an injector and added a free water knock out to enhance water and production capabilities. At the end of 2010, cumulative production from this pool was approximately 1.1 million bbls of oil and 2.4 billion cubic feet of natural gas. Also, 1.8 million barrels of water had been injected. Arcan is currently producing 400 BOE per day net from this pool.

Arcan owns a 100 percent interest in the three sections of land immediately offsetting the Hamburg GG oil pool on the southern boundary and drilled one well on lands in December of 2010. This well is on production and producing approximately 100 BOE per day. Arcan currently has two to four infill development opportunities to drill in the Hamburg GG oil pool and will evaluate this program as economic conditions warrant. Longer-term plans call for additional exploration tests that have been selected based on 3D seismic. There is potential for Arcan to shoot additional 3D seismic and the possibility of drilling up-hole Bluesky and Montney natural gas targets, where competitors are producing in offsetting sections, is currently being considered.

Hamburg area production averaged 509 BOE per day on \$20.69 per BOE operating netbacks for the year ended December 31, 2010, down from 675 BOE per day on \$22.20 per BOE operating netbacks in the year ended December 31, 2009. Production declines were mainly attributable to natural declines from a high rate gas well that Arcan drilled in 2009.

McLeod, Alberta

The McLeod property is characterized by medium-risk, multi-zone liquids rich natural gas targets largely focused in Mannville Group and Jurassic-aged strata at depths of 1,800 to 2,200 metres. Arcan has drilled seven (5.2 net) Gething natural gas wells with 90 percent success at McLeod. These wells were producing approximately 50 BOE per day in total as of year-end 2010, which is down from 75 BOE per day in 2009 due to the normal declines of natural gas wells. Arcan has reduced capital allocations to this area as natural gas prices have remained weak compared to oil.

Annual and Fourth Quarter Results of Operations

Production Volumes

Sales Volumes	Quarter Ended December 2010	Quarter Ended December 2009	Year Ended December 2010	Year Ended December 2009
Crude oil and NGLs (bbls per day)	2,572	1,001	1,983	1,021
Natural gas (Mcf per day)	1,373	2,105	1,557	2,124
Total oil equivalent (BOE per day)	2,800	1,352	2,243	1,375
Oil as a percent of total volumes	92%	74%	88%	74%

Arcan produced 2,800 BOE per day in the fourth quarter of 2010, a 107 percent increase from 1,352 recorded in the fourth quarter of 2009 and up slightly from the 2,740 BOE per day produced in the third quarter of 2010. Production for the year ended December 31, 2010 averaged 2,243 BOE per day, up 63 percent from the 1,375 BOE per day for the year ended December 31, 2009. Production from Swan Hills was up 165 percent, McLeod was up 15 percent while production from Hamburg was down 25 percent for the 2010 year versus the year ended December 31, 2009.

Arcan's average production for the first quarter of 2011 is expected to be approximately 2,600 BOE per day. These production results have been negatively impacted by a non-operated pipeline failure from January 1, 2011 to March 1, 2011 and operational issues with six horizontal oil wells. Arcan continues to address the well operations and in spite of the pipeline outage, Arcan anticipates its production for 2011 will increase in 2011 to average up to approximately 4,000 BOE per day. Arcan has a substantial inventory of development wells to drill in its Swan Hills oil property. For the balance of 2011, Arcan will consider any additional expansions based on existing capital capacity, the business and economic climate and commodity price environment.

Netbacks

The Corporation considers corporate netbacks to be an indication of its ability to produce oil and natural gas profitably and to earn a return on capital invested. Netbacks are one of three possible sources of funding, the others being utilizing debt and issuing new equity. The largest impact to Arcan's netbacks was a result of an overall increase in production. Netbacks were also bolstered by a combination of an operating cost per BOE decline and commodity price increases for Arcan of 14 percent on oil and seven percent on natural gas. This is consistent with the Edmonton Par price increase from an average of \$66.30 per barrel for 2009 to an average of \$80.44 per barrel for 2010.

Netbacks \$ thousands	Quarter Ended December 2010	Quarter Ended December 2009	Year Ended December 2010	Year Ended December 2009
Revenue	18,420	7,804	55,575	27,290
Royalties	5,843	2,554	14,704	7,116
Operating expenses	3,567	2,672	11,110	8,082
Operating netbacks	9,010	2,578	29,761	12,092
Realized economic hedging loss	-	737	-	1,440
G&A	658	788	5,126	3,674
Interest expenses	486	379	1,756	1,540
Corporate netbacks	7,866	674	22,879	5,438
\$ per BOE				
Revenue	71.50	62.74	67.89	54.39
Royalties	22.68	20.53	17.96	14.18
Operating expenses	13.85	21.48	13.57	16.11
Operating netbacks	34.97	20.73	36.36	24.10
Realized economic hedging loss	-	5.92	-	2.87
G&A	2.55	6.34	6.26	7.32

Netbacks \$ thousands	Quarter Ended December 2010	Quarter Ended December 2009	Year Ended December 2010	Year Ended December 2009
Interest expenses	1.88	3.05	2.14	3.07
Corporate netbacks	30.54	5.42	27.96	10.84

Arcan's operating netback, defined as revenue, less royalties and operating expenses, was \$9.0 million in the fourth quarter of 2010 up from \$2.6 million recorded in the fourth quarter of 2009. The increase in operating netback for the fourth quarter was based on a 107 percent increase in production volumes leading to a 136 percent increase in revenues offset by increases in royalties and operating costs. Arcan's operating netback was down from \$10.1 million in the third quarter of 2010 due to a \$1.2 million royalty adjustment recorded in the fourth quarter of 2010. Operating netbacks for the year ended December 2010 were \$29.8 million, up 146 percent from \$12.1 million for the year ended December 31, 2009. The increase in operating netback in total for the year ended December 31, 2010 over 2009 was based on a 63 percent increase in production volumes leading to an increase in revenues and was moderately offset by increases in royalties and operating costs.

Arcan's operating netback on a per BOE basis was \$34.97 in the fourth quarter of 2010, representing a 69 percent increase from the \$20.73 recorded in the fourth quarter of 2009. The increase in operating netback related to an increase in price and a decrease in operating costs partially offset by an increase in royalties on a per BOE basis in the fourth quarter of 2010 as compared to the same period of 2009. Operating netbacks per BOE for the year ended December 31, 2010 were \$36.36, up 51 percent from \$24.10 for the year ended December 31, 2009. The increase in the operating netback per BOE for the year ended December 31, 2010 versus the prior period is due to an increase in prices combined with a decrease in operating costs offset by an increase in royalties. The move to oil weighting has continued to assist Arcan's exposure to price upside in the last few years, and is expected to continue in 2011. However, oil properties do present additional operating costs which can be higher on a BOE basis in the early stages of a waterflood than in natural gas. The net effect to Arcan was higher netbacks from oil in 2010 than would have been achieved through natural gas.

Operating netbacks from oil were \$35.87 per BOE and from natural gas were negative (\$15.97) per BOE in the fourth quarter of 2010 versus \$20.92 for oil and \$15.25 for natural gas in the fourth quarter of 2009. Operating netbacks from oil were \$37.47 per BOE and from natural gas were \$8.53 per BOE during the year ended December 31, 2010 versus operating netbacks from oil of \$25.43 per bbl and from natural gas of \$4.56 per BOE during the year ended December 31, 2009. Arcan's oil netbacks have been stronger than its natural gas netbacks for all periods since 2007 due primarily to commodity pricing.

Arcan's corporate netback, defined as operating netback, less realized economic hedging losses, G&A and interest (income less expense), was up to \$7.9 million in the fourth quarter of 2010 as compared to \$0.7 million in the fourth quarter of 2009 due primarily to higher volumes and prices. Arcan's corporate netback was \$22.9 million for the year ended December 31, 2010 versus \$5.4 million for the year ended December 31, 2009. The large increases for 2010 related mainly to an increase in production volumes combined with an increase in commodity prices. On a per BOE basis, Arcan's corporate netback was \$30.54 in the fourth quarter of 2010 as compared to \$5.42 in the fourth quarter of 2009 and \$30.41 in the third quarter of 2010. On a per BOE basis, the corporate netback was \$27.96 in 2010 as compared to \$10.84 in 2009. Changes in netbacks and the components thereof are detailed by category in the above table.

Operations by area for the years ended December 31, 2010 and 2009 are as follows:

Area Operating Netbacks Area	Year ended December 31, 2010			Year ended December 31, 2009		
	Swan Hills	Hamburg	McLeod	Swan Hills	Hamburg	McLeod
Daily Production (BOE per day)	1,648	509	86	623	675	75
Revenue (\$/BOE)	71.82	60.68	35.23	63.75	48.28	32.37
Royalties (\$/BOE)	16.16	25.88	5.74	19.42	10.93	(3.09)
Operating Costs (\$/BOE)	13.01	14.12	20.95	15.40	15.15	30.90
Operating Netbacks (\$/BOE)	42.65	20.68	8.54	28.93	22.20	4.56

Arcan focused on its oil properties in 2009 and 2010 as netbacks from its oil properties provided higher margins than the natural gas properties.

Revenues

Petroleum and Natural Gas Revenues (\$)	Quarter Ended December 2010	Quarter Ended December 2009	Year Ended December 2010	Year Ended December 2009
Oil and liquids (000's)	17,882	6,797	52,822	23,798
Per bbl	75.58	73.80	72.97	63.89
Natural gas (000's)	539	1,007	2,753	3,492
Per Mcf	4.26	5.20	4.84	4.50
Oil and liquids as a percent of total revenue	92%	87%	88%	87%
Benchmark Prices				
WTI (U.S.\$ per bbl)	85.16	76.03	78.84	61.99
Edmonton Light Sweet (\$Cdn. per bbl)	80.70	76.73	80.44	66.30
Alberta Plant Gate (per Mcf)	3.47	4.50	4.78	3.85
Cdn\$ per U.S.\$	0.99	0.95	0.96	0.88

Arcan posted higher production revenues for the year ended December 31, 2010. A 63 percent increase in production volume combined with a 25 percent increase in prices Arcan received for its products, resulted in an increase in revenue for the year ended December 31, 2010 as compared to the year ended December 31, 2009. In the fourth quarter of 2010, revenues increased to \$18.4 million from the \$7.8 million recorded in the fourth quarter of 2009 and increased to \$55.6 million from \$27.3 million for the year over year comparison. Revenues increased in the fourth quarter from \$17.1 million in the third quarter of 2010 due primarily to price and volume increases. Based on estimated production volume impacts related to pipeline outages in January and February as well as prices, Arcan expects to have approximately the same revenues in the first quarter of 2011. Arcan expects improvements in production volumes after the first quarter of 2011 and anticipates that overall production in 2011 will be higher than 2010.

Commodity Prices

Oil continues to grow as a percentage of Arcan's total revenues as Arcan invests in increasing its oil production, with the fourth quarter of 2010 production weighted 92 percent towards light oil. The average price for West Texas Intermediate ("**WTI**") gained 12 percent in the fourth quarter of 2010 versus the same quarter in 2009 and gained 27 percent on average for the year ended December 31, 2010 over the year ended December 31, 2009. Meanwhile, Edmonton Par has only increased five percent in the fourth quarter of 2010 versus the same quarter in 2009 and gained 21 percent in the year ended December 31, 2010 over the year ended December 31, 2009 due to the impact of the weakening U.S. currency against the Canadian dollar.

In the fourth quarter of 2010 Arcan realized average revenue per BOE of \$71.50 as compared to \$62.74 recorded in the fourth quarter of 2009 and \$67.87 in the third quarter of 2010. Arcan realized an average of \$75.58 per bbl of oil and NGL in the fourth quarter of 2010, an increase from the \$73.80 per bbl realized in the fourth quarter of 2009 and up from the \$71.55 per bbl received in the third quarter of 2010. The increase in Arcan's oil price for the fourth quarter of 2010 compared to 2009 is consistent with the increase in the Edmonton Light Sweet price for the same period as is the change from the third quarter of 2010 to the fourth. The Corporation realized an average natural gas price of \$4.26 per thousand cubic feet ("**Mcf**") in the fourth quarter of 2010, an 18 percent decrease from the \$5.20 per Mcf averaged in the fourth quarter of 2009 and an increase from the \$4.18 per Mcf received in the third quarter of 2010. This is consistent with the price changes at the Alberta Plant gate for the same periods. The changes in Arcan's oil and gas prices for the year ended December 31, 2010 compared to the year ended December 2009 are also consistent with the changes shown in the Edmonton Light Sweet price and the Alberta Plant Gate price. Arcan anticipates oil prices will remain in

the U.S.\$75 to U.S.\$100 WTI range for 2011 due to issues in the middle east and uncertainty on global economic growth and that gas prices will remain soft through 2011 at 2010 price levels.

Royalty Expense (\$ 000's except per BOE)	Quarter Ended December 2010	Quarter Ended December 2009	Year Ended December 2010	Year Ended December 2009
Total	5,843	2,554	14,704	7,116
Per BOE	22.68	20.53	17.96	14.18
Royalties as a percent of revenue	31.7%	32.7%	26.5%	26.1%

Royalty expense in the fourth quarter of 2010 was \$5.8 million, compared to \$2.6 million in the fourth quarter of 2009, and for the year ended December 31, 2010 was \$14.7 million, compared to \$7.1 million for the year ended December 31, 2009. Royalties were unexpectedly high in the fourth quarter as two wells that had been given royalty free status were re-classified by the Crown and Arcan thereby incurred a \$1.2 royalty adjustment during the period. Excluding the adjustment, royalties as a percentage of revenue would have been 25 percent for the quarter and 24 percent for the year. The increase in the gross royalty amounts, year over year, was primarily the result of increased revenues based on higher commodity prices and volumes. On a per BOE basis, changes were attributable to decreases in royalty rates in Alberta for 2010 offset by price increases Arcan received which increased 14 percent year over year. Royalties were \$4.0 million or 23 percent of revenue in the third quarter of 2010 compared to \$5.8 million or 32 percent of revenue in the fourth quarter. Royalties have increased on a percentage of revenue basis from the third quarter primarily as a result of the change in royalty status on two Arcan wells.

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

Operating Expenses (\$ 000's except per BOE)	Quarter Ended December 2010	Quarter Ended December 2009	Year Ended December 2010	Year Ended December 2009
Total	3,567	2,672	11,110	8,082
Per BOE	13.85	21.48	13.57	16.11

In the fourth quarter of 2010, Arcan incurred operating costs of \$13.85 per BOE or \$3.6 million, up from the \$2.7 million recorded in the fourth quarter of 2009 but were down on a BOE basis to \$21.48 per BOE from the higher volumes in the fourth quarter of 2011. Operating costs increased to \$11.1 million or \$13.57 per BOE for the year ended December 31, 2010, from \$8.1 million or \$16.11 per BOE for the year ended December 31, 2009. A significant portion of the overall decrease in operating costs per BOE was related to higher production volumes. Operating costs on a per BOE basis increased from the \$11.95 per BOE experienced in the third quarter of 2010 due to winter conditions.

Arcan expects that it's per BOE operating expenses will decrease in 2011 as a result of higher production volumes. Going forward through 2011, Arcan's continued transition towards oil-weighted production, including costs to operate the EOR, is anticipated to result in \$10 to \$15 per BOE average operating costs per unit of production.

Realized and unrealized losses on commodity contracts and financial instruments

(\$ 000's except per BOE)	Quarter Ended December 2010	Quarter Ended December 2009	Year Ended December 2010	Year Ended December 2009
Total realized losses	-	737	-	1,440
Per BOE	-	5.92	-	2.87
Total unrealized losses (gain)	1,215	(531)	2,233	-
Per BOE	4.71	(4.27)	2.73	-

Periodically Arcan utilizes economic hedges to protect a portion of its cash flows. Arcan has hedged 2,000 bbls per day from January 1, 2011 to December 31, 2011 by purchasing Canadian dollar WTI put contracts establishing a \$70.00 floor. As payment Arcan sold four 500 bbl per day Canadian dollar WTI call contracts two of which are at \$100.00, one at \$100.05 and the last one was priced at \$100.30. These contracts were entered into in the third quarter of 2010 and as the volumes relate to 2011, no realized amounts were recorded however an unrealized loss of \$2.2 million was recorded for the year ended December 31, 2010. Arcan will mark-to-market these contracts at the end of each quarter with realized and/or unrealized gain or losses, if any, recorded in the statement of operations for each reporting period, using the price curve for that instrument on the last day of that month and comparing it to the price curve on the day the hedge was acquired. For 2009, Arcan had entered into a fixed price oil swap contract to receive \$64.40 per bbl in exchange for Canadian dollar WTI on oil production of 500 bbls per day for the period from April 1 to December 31, 2009. There were no hedging contracts for 2010 production volumes.

Subsequent to December 31, 2010 Arcan has hedged 1,000 bbls per day from January 1, 2012 to December 31, 2012 by purchasing Canadian dollar WTI put contracts establishing a \$75.00 floor. As payment Arcan sold two 500 bbl per day Canadian dollar WTI call contracts, one of which is at \$126.00 and one priced at \$127.50. All hedges are approved by the Board of Directors.

There was no realized loss on commodity contracts for the quarter or for the year ended December 31, 2010, respectively as compared to \$0.7 million for the fourth quarter of 2009 and \$1.4 million of year ended December 31, 2009. At December 31, 2010 Arcan had outstanding hedge contracts for 2011 that were recorded as an unrealized losses of \$1.2 million or \$4.71 per bbl for the quarter ended December 31, 2010 and \$2.2 million or \$2.73 per bbl for the year ended December 31, 2010.

Contract period	Pricing (Cdn\$ WTI)	Volume per day
January – December 2011	Collar \$70.00 floor – \$100.00 ceiling	1,000 bbls
January – December 2011	Collar \$70.00 floor – \$100.05 ceiling	500 bbls
January – December 2011	Collar \$70.00 floor – \$100.30 ceiling	500 bbls
January – December 2012	Collar \$75.00 floor – \$126.00 ceiling	500 bbls
January – December 2012	Collar \$75.00 floor – \$127.50 ceiling	500 bbls

Cash G&A (\$ 000's except per BOE)	Quarter Ended December 2010	Quarter Ended December 2009	Year Ended December 2010	Year Ended December 2009
Total	658	788	5,126	3,674
Per BOE	2.55	6.34	6.26	7.32

Cash G&A for 2010 of \$5.1 million net of \$1.9 million of recoveries, was primarily comprised of wages and bonuses of \$2.9 million, bank charges of \$1.3 million, rent of \$0.5 million, software of \$0.3 million, legal of \$0.3 million, and audit fees of \$0.2 million. The twelve month period of 2010 had higher cash G&A expenses than the twelve month period ended December 31, 2009, mainly related to bonuses, but lower cash G&A per BOE numbers resulting from the increased production volumes.

Cash G&A expenses for the fourth quarter of 2010 decreased on a per BOE basis to \$2.55 per BOE from \$6.34 per BOE in the fourth quarter of 2009 and decreased from \$7.50 per BOE in the third quarter of 2010 due mainly to decreased legal, insurance, consulting, and reserve evaluation costs. Cash G&A expense is expected to increase overall, but is expected to decline on a per BOE basis on average for 2011 due to increases in Arcan's activity levels. Arcan does not capitalize any G&A. 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.

Interest Expense (\$ 000's)	Quarter Ended December 2010	Quarter Ended December 2009	Year Ended December 2010	Year Ended December 2009
Total	506	380	1,780	1,543
Per BOE	1.96	3.05	2.17	3.08

Historically, Arcan's Management increased debt levels based on operational success and has subsequently reduced those debt levels through equity issuances. As Arcan has grown its asset base, its related borrowing capacity and ability to carry and service higher debt levels has increased. To provide stable and secure longer term financing, Arcan completed the Debenture offering in February 2011 for gross proceeds to Arcan of \$86.25 million. These funds are in addition to Arcan's existing Credit Facility. Arcan expects that its debt to cash flow ratio in 2011 will be higher as it continues to grow and that its interest expense will increase with higher debt levels and possible bank rate increases plus the inclusion of the Debentures.

Interest expense in the fourth quarter of 2010 of \$0.5 million was similar to the third quarter of 2010 of \$0.5 million. This was due to lower debt levels in the fourth quarter of 2010 compared to the third quarter of 2010 offset by higher interest rates in the fourth quarter. The increase in interest expense from the prior year resulted from an increase in average debt levels and interest rates. Arcan had an effective interest rate of 5.25 percent on its debt facility at December 31, 2010 and 4.75 percent at December 31, 2009.

Based on Arcan's assets, its Credit Facility was increased from \$50 million at the start of 2010 to \$100 million. The only financial covenant Arcan has on its Credit Facility is that combined debt and working capital cannot exceed \$100 million. There are no financial covenants associated with the Debentures. Arcan will review its Credit Facility in the near future in connection with the reserved reported in the GLJ report. Subsequent to the 2010 year end, Arcan has continued to increase its draws on its Credit Facility and expects to carry bank debt as required as part of routine operations on an ongoing basis.

Stock-Based Compensation (\$ 000's except per BOE)	Quarter Ended December 2010	Quarter Ended December 2009	Year Ended December 2010	Year Ended December 2009
Total	1,172	391	3,856	942
Per BOE	4.55	3.14	4.71	1.88

Stock-based compensation is a non-cash expense, which represents the estimated fair value of performance and other stock options granted to employees as a motivational incentive. Arcan expects that its stock-based compensation will increase as options that have been issued are expensed and new options are issued. This increase may be further magnified as a result of share price volatility. No stock-based compensation is capitalized.

Arcan recorded stock-based compensation expense of \$1.2 million in the fourth quarter of 2010, calculated using the Black-Scholes option-pricing model. During the fourth quarter of 2010 Arcan granted 2,880,000 options, 1,767,167 options were exercised and Arcan cancelled 7,500 options that were forfeited. Arcan's stock-based compensation expense increased for the three month period and year ended December 2010 compared to the same periods in 2009 were due to option grants in the fourth quarter of 2009, and a greater number of options being issued in the third and fourth quarter of 2010 versus 2009 and the escalated fair value of each option due to the increase in share trading price over that period.

**Depletion, Depreciation and Accretion
("DD&A")**
(\$ 000's except per BOE)

	Quarter Ended December 2010	Quarter Ended December 2009	Year Ended December 2010	Year Ended December 2009
Total	7,496	2,899	22,211	11,707
Per BOE	29.10	23.31	27.13	23.34

DD&A is calculated based upon capital expenditures, production rates and reserves. Arcan recorded \$7.5 million or \$29.10 per BOE in DD&A expense in the fourth quarter of 2010 based on production volumes of 257,636 BOE. The increase in DD&A expense per BOE as compared to the fourth quarter and year ended 2009 is due to acquisitions completed during 2010, including the Acquisition, as well as an increase in capital intensity for reserves found in 2010. The increase in overall DD&A expense as compared to the fourth quarter and year ended 2009 is due to higher production volumes and increased capital intensity for reserves found in 2010 compared to 2009.

Arcan's DD&A rate reflects proportionately higher cumulative capital expenditures, including significant facility investments and the large acquisition Arcan completed in March of 2010, relative to recognized reserves. Arcan's two main properties are in the early stages of enhanced recovery schemes and substantial amounts of capital have been invested in infrastructure and land. The Corporation expects to decrease the depletion per BOE amount in future years by adding reserves through a development program that has a lower capital intensity as a large portion of infrastructure investments have already been incurred.

The Corporation excluded from its depletion and depreciation calculation costs associated with undeveloped land and seismic of \$26.1 million and included future development costs of \$141.2 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 increased each reporting period due to the passage of time and the amount of accretion is charged to earnings in the period.

Income Taxes (\$ 000's)	Quarter Ended December 2010	Quarter Ended December 2009	Year Ended December 2010	Year Ended December 2009
Future income tax reduction (expense)	100	354	354	1,469

The difference between the expected income tax provision based on the combined federal and provincial statutory tax rate and the amount actually provided for is as follows:

(\$ 000's)	Year Ended December 2010	Year Ended December 2009
Combined federal and provincial statutory rate	28.0%	29.0%
Expected future income tax (recovery) expense	(1,518)	(2,091)
Stock-based compensation	1,080	273
Future tax rate reductions and other	84	349
Future income tax (reduction) expense	(354)	(1,469)

A future tax reduction of approximately \$0.1 million has been recognized in the financial statements for the fourth quarter of 2010, which relates to the Corporation experiencing a pre-tax loss of \$1.9 million for the quarter. The provision for income taxes differs from the amount obtained by applying the combined federal and provincial income tax rate for 2010, which was 28.0 percent and is calculated on the loss before income taxes. The difference is mainly due to non-deductible stock-based compensation and future tax rate differences.

The future income tax liability on the balance sheet decreased by \$1.9 million during 2010 due to the future income tax reduction of \$0.4 million and a future income tax asset from share issue costs of \$1.9 million. The decreases were slightly offset by an increase of \$0.4 million for the tax effect of common shares that were issued on a "flow-through" basis under the *Income Tax Act* (Canada) ("**Flow-Through Shares**"). Prior to the December 31, 2010 deadline, Arcan had completed the \$1.5 million of qualifying expenditures required to meet its 2010 Flow-Through Share obligations based on the 1,071,500 Flow-Through Shares Arcan issued on November 20, 2009 at \$1.40 per Flow-Through Share.

The components of the future income taxes are as follows:

(\$ 000's)	Year Ended December 2010	Year Ended December 2009
Share issue costs	(1,704)	(389)
Asset retirement obligations	(2,712)	(1,343)
Non-capital losses	(7,585)	(7,552)
Fair value of commodity contracts	(592)	-
Property, plant and equipment	15,432	13,971
Future income taxes	2,839	4,687

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

Estimated Tax Pools

(\$ millions) Type	December 31, 2010	Rate of Claim (%)
Canadian exploration expense	16.2	100
Non-capital losses	30.3	100
Canadian development expense	84.0	30
UCC	51.5	20 - 100
Share issue	6.7	20
Canadian oil and natural gas property expense	58.5	10
Total	247.2	

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

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

(\$ 000's except per share)	Quarter Ended December 2010	Quarter Ended December 2009	Year Ended December 2010	Year Ended December 2009
Net income (loss)	(1,917)	(1,730)	(5,068)	(5,743)
Per share	(0.02)	(0.04)	(0.07)	(0.15)
Funds from operations	7,759	667	22,739	5,345
Per share	0.09	0.02	0.32	0.14
Cash flow from (used in) operating activities (per GAAP)	8,044	(371)	19,631	4,328
Per share	0.10	(0.01)	0.28	0.11

Arcan is generating funds from the operations of its three properties. Net loss has been realized in 2010 due to higher commodity prices, volumes, royalties and operating costs as well as non-cash items such as stock-based compensation and DD&A charges. As Arcan continues to develop these properties, it anticipates that

additional revenues will be generated resulting in additional funds from operations as well as additional net earnings.

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

Fiscal quarter ended	2010				2009			
	Dec.	Sept.	June	March	Dec.	Sept.	June	March
Operating								
Oil and NGLs (bbbls per day)	2,572	2,523	1,674	1,142	1,001	913	1,061	1,110
Price (\$/bbl)	75.58	71.55	68.13	77.35	73.80	70.18	63.98	49.36
Natural gas (Mcf per day)	1,373	1,301	1,613	1,951	2,105	2,166	2,772	1,444
Price (\$/Mcf)	4.26	4.18	4.60	5.91	5.20	3.27	4.09	6.17
Bbls of oil equivalent (BOE per day)	2,800	2,740	1,943	1,468	1,352	1,274	1,523	1,350
Financial (\$000's, except per share amounts)								
Revenues								
Petroleum and natural gas	18,420	17,107	11,056	8,992	7,804	6,546	7,209	5,731
Royalties	(5,843)	(4,017)	(2,491)	(2,352)	(2,554)	(2,010)	(1,275)	(1,277)
Interest and other income	20	-	-	3	1	-	2	1
Realized loss on commodity contracts	-	-	-	-	(737)	(481)	(222)	-
Unrealized gain (loss) on commodity contracts	(1,215)	(1,019)	-	-	531	1,228	(1,115)	(644)
Net revenues	11,382	12,071	8,565	6,643	5,045	5,283	4,599	3,810
Expenses								
Operating	3,567	3,012	2,143	2,388	2,672	2,465	1,593	1,352
General and administrative	658	1,891	1,542	1,034	788	1,063	959	863
Stock-based compensation	1,172	1,122	1,124	438	391	166	193	193
Interest	506	522	370	382	380	494	398	272
Accretion	207	202	194	108	103	104	105	101
Depletion and depreciation	7,289	6,853	4,139	3,219	2,795	2,680	3,098	2,720
Total Expenses	13,399	13,602	9,512	7,569	7,130	6,972	6,346	5,501
Income (loss) before income taxes	(2,017)	(1,531)	(947)	(926)	(2,085)	(1,689)	(1,747)	(1,690)
Future income tax expense (reduction)	(100)	(176)	44	(122)	(354)	(281)	(433)	(400)
Net income (loss)	(1,917)	(1,355)	(991)	(804)	(1,730)	(1,408)	(1,314)	(1,290)
Net income (loss) per share- basic	(0.02)	(0.02)	(0.01)	(0.02)	(0.04)	(0.04)	(0.03)	(0.03)
Net income (loss) per share- diluted	(0.02)	(0.02)	(0.01)	(0.02)	(0.04)	(0.04)	(0.03)	(0.03)
Funds from operations	7,759	7,652	4,501	2,826	667	32	2,680	1,966
Per share – basic	0.09	0.10	0.06	0.06	0.02	0.00	0.07	0.05
Cash flow from (used in) operating activities (per GAAP)	8,044	5,371	3,669	2,548	(371)	1,235	2,102	1,361
Operating Netbacks (\$/BOE)								
Petroleum and natural gas revenues	71.50	67.87	62.52	68.07	62.74	55.85	52.01	47.16
Royalties	22.68	15.94	14.09	17.81	20.53	17.15	9.20	10.51
Operating and transportation expenses	13.85	11.95	12.12	18.08	21.48	21.03	11.50	11.12
Operating Netbacks	34.97	39.98	36.31	32.18	20.73	17.67	31.31	25.53
Total assets (\$000's)	289,775	269,833	244,234	227,067	151,251	146,130	145,729	150,398
Capital expended (\$000's)	27,874	28,386	21,240	70,835	4,979	3,111	229	3,177
Debt and working capital (\$000's)	(48,592)	(78,270)	(57,263)	(40,908)	(34,779)	(42,622)	(40,414)	(42,073)
Shares (000's)	87,670	75,418	75,173	74,928	47,940	37,869	37,869	37,869

Liquidity and Capital Resources

Arcan incurred \$148.3 million, including the \$52.8 Acquisition, of capital on its properties during the year ended December 31, 2010, up significantly from \$11.5 million for the year ended December 31, 2009. Arcan generated \$22.7 million in funds from operations in 2010, raised \$115.0 million through the issuance of equity securities and at December 31, 2010 had borrowed \$20.8 million from its Credit Facility and had a working capital deficit including bank debt of \$48.6 million as at December 31, 2010. With its solid asset base Arcan estimates that it has the ability to generate short-term and long-term cash flow to meet obligations as they become due. Arcan's Management increased debt levels from the fourth quarter of 2009 through increased capital expenditures in 2010 which was partially offset through the issuance of equity. Arcan's 2010 funds from operations to net debt was 1.6 to one. The ratio is expected to increase but remain under three to one by the end of 2011.

On March 24, 2010 Arcan issued 26,000,000 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).

On November 5, 2010 Arcan issued 10,421,875 common shares at a price of \$4.80 per share for gross proceeds of \$50,025,000.

Subsequent to year end, on February 14, 2011 Arcan issued \$75,000,000 Debentures and on February 22, 2011 issued an additional \$11,250,000 Debentures pursuant to the exercise of an over-allotment option by the underwriters. The Debentures are convertible into shares at a price of \$8.75 per share and mature on February 28, 2016.

As at the date hereof, the Corporation has \$100.0 million available under its Credit Facility. The Credit Facility is comprised of a \$90 million syndicated revolving credit facility and a \$10 million revolving operating facility which is based on Arcan's 2009 reserves report. The Credit Facility has a revolving period of 364 days from the closing date and is extendible annually. If not extended, the Credit Facility will automatically convert to a one year non-revolving term loan. Arcan is currently in compliance with its financial covenant to keep debt and working capital under the \$100 million loan maximum and the renewal date for the Credit Facility is May 31, 2011. The Credit Facility is secured by a charge on all of Arcan's assets and currently there are no amounts drawn on these facilities and Arcan has \$39.1 million in cash in the bank. Arcan has \$186.25 million in total credit capacity comprised of the \$100.0 million Credit Facility and the \$86.25 million in Debentures outstanding. Arcan estimates that at April 5, 2011, due to capital expenditures in the Swan Hills, its debt and working capital deficiency is approximately \$90 million, which is below its current and anticipated Credit Facility. Arcan estimates that it will have cash flow in excess of capital expended in the second quarter of 2011 and expects to be in a net debt position of \$50 to \$150 million throughout 2011.

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

Arcan expects its capital expenditure program to be lower in 2011 than in 2010 and expects the expenditures to be financed through its Credit Facility and available funds from operations. Additional equity may be available later if the condition of the equity markets permit; however, the Corporation does not currently forecast requiring 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.

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

(\$ 000's)	Year Ended December 2010	Year Ended December 2009
Current assets	17,731	10,947
Less:		
Accounts payable and accrued liabilities	45,500	17,140
Bank loan	20,823	28,586
Working capital (deficiency)	(48,592)	(34,779)

Capital Expenditures (\$ 000's)	Quarter Ended December 2010	Quarter Ended December 2009	Year Ended December 2010	Year Ended December 2009
Geological and geophysical	940	130	1,043	243
Land	748	33	7,246	504
Acquisitions	7	-	53,732	-
Drilling and completions	19,008	3,526	62,228	6,497
Equipment and facilities	7,151	1,286	23,965	4,167
Corporate assets	20	4	120	84
Total	27,874	4,979	148,334	11,495

Arcan significantly increased its capital expenditure program for the year ended December 31, 2010. During this period, Arcan drilled 20 (16.5 net) wells. In addition, Arcan converted three (2.5 net) wells into injectors, converted one (0.8 net) oil well to a source well and worked over several wells. Arcan has, as it did in 2010, budgeted capital expenditures to remain within cash flow and Credit Facility limitations for 2011. Additional equity may be available later in 2011 if the equity market conditions permit; however, the Corporation does not forecast requiring this cash inflow to complete its capital program. Arcan's currently budgeted capital program can be curtailed with no fixed commitments to ensure management of net debt levels and Arcan's budget will be reassessed during the 2011 break-up period based on Arcan's success and expansion in the Swan Hills reef light oil play.

Capital expenditures for the fourth quarter of 2010 were \$27.9 million. This was up from the \$5.0 million spent in the fourth quarter of 2009. During the fourth quarter Arcan expended \$19.0 million drilling six (5.4 net) wells and \$7.2 million on completing tie-in operations on these wells, on well re-entries and completing previously drilled wells.

Capital Expenditure Summary (\$ millions)	Q4 2010	Q3 2010	Q2 2010	Q1 2010	YTD December 31, 2010
Land and seismic	1.7	1.8	0.5	4.3	8.3
Acquisitions	-	-	1.0	52.8	53.8
Drilling and intangibles	19.0	18.0	16.2	9.0	62.2
Facilities and equipment	7.2	8.6	3.6	4.7	24.0
Total Capital	27.9	28.4	21.3	70.8	148.3

2010 Drilling Activity

2010	Exploration		Development		Total		Success Rate %	Working interest %
	Gross	Net	Gross	Net	Gross	Net		
Q1	1	0.3	3	2.5	4	2.8	75	70
Q2	-	-	7	5.7	7	5.7	100	81
Q3	-	-	3	2.6	3	2.6	100	87
Q4	-	-	6	5.4	6	5.4	100	90
Total	1	0.3	19	16.2	20	16.5	95	83

During the three month period ended December 31, 2010, Arcan drilled six (5.4 net) wells, which resulted in one (1.0 net) Hamburg oil well and five (4.4 net) horizontal Swan Hills oil wells.

During the three months ended March 31, 2011 Arcan drilled eight (7.4 net) successful horizontal multi-stage fracture wells on its Swan Hills play and re-entered and multi-stage fractured one (1.0 net) older existing horizontal well.

Insurance

Arcan purchases insurance to protect corporate assets from catastrophic events. There are many factors to consider when determining appropriate insurance levels, including risks, probability and costs. Arcan carries \$25 million in per well drilling, \$30 million in total production insurance for its main properties, \$70 million in general corporate liability insurance, as well as \$20 million in director's and officer's liability insurance. Insurance levels are reviewed annually in December and modified as required to maintain reasonable coverage for a range of possible situations. Arcan's insurance levels are similar to coverage levels maintained by its peer groups.

Related Party Transactions

In conjunction with the equity issuance pursuant to the prospectus during the year ended December 31, 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.

In conjunction with the debenture issuance in February 2011, certain officers and directors acquired \$1,335,000 in the debentures.

The share purchase loan of \$100,000 due from an officer of the Corporation for the purchase of 40,000 common shares at a price of \$2.50 per common share was repaid in December 2010.

Shareholder Rights Plan

On February 6, 2009, the Corporation adopted a shareholder rights plan (the "**Plan**"), similar to existing shareholder rights plans adopted by other Canadian public companies. The Plan is effected by a Shareholder Rights Plan Agreement (the "**Shareholder Rights Plan Agreement**") dated February 6, 2009 between Valiant Trust Company and the Corporation. This plan was presented and passed by shareholder vote at the annual and special meeting held on May 20, 2009.

The objectives of the Plan are to ensure that, to the extent possible, all Shareholders are treated equally and fairly in connection with any take-over bid for the Corporation. The Plan discourages discriminatory, coercive or unfair take-overs of the Corporation and gives the Corporation's board of directors time if, in the circumstances, the board of directors determines it is appropriate to take such time, to pursue alternatives to maximize Shareholder value in the event an unsolicited take-over bid is made for all or a portion of the outstanding Common Shares.

If a person, or a group acting in concert, acquires (other than pursuant to an exemption available under the Plan) or announces its intention to acquire 20 percent or more of the Common Shares, one rights (a "**Right**") (other than those held by such acquiring person which will become void) will separate from the Common Shares and permit the holder thereof to purchase Common Shares at a 50 percent discount to their market price. A person, or a group acting in concert, who is the beneficial owner of 20 percent or more of the outstanding Common Shares is exempt from the dilutive effects of the Plan provided such person (or persons) does not acquire more than one percent of the Common Shares in addition to those Common Shares already held by such person (or persons). At any time prior to the Rights becoming exercisable, the board of directors may waive the operation of the Plan with respect to certain events before they occur.

The issuance of the Rights is not dilutive until the Rights separate from the underlying Common Shares and become exercisable or until the exercise of the Rights. The issuance of the Rights will not change the manner in which Shareholders currently trade their Common Shares.

"Permitted bids" under the Plan must be made to all holders of Common Shares and must be open for acceptance for a minimum of 60 days. If at the end of 60 days at least 50 percent of the outstanding Common Shares other than those owned by the offeror and certain related parties have been tendered and not withdrawn, the bidder may take-up and pay for the shares but must extend the bid for a further ten days to allow other Shareholders to tender to the bid.

Contractual Obligations

The Corporation has entered into farm-in agreements in the normal course of its business in 2010.

Arcan has the following commitments, the changes from 2009 relating to the leasing of new office space in 2010 which Arcan expects to move into in June 2011:

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

	\$
2011	737,984
2012	1,096,365
2013	1,096,365
2014	1,096,365
2015	1,096,365
2016	477,631

The Corporation is also subject to contractual obligations in respect of the Credit Facility as disclosed in the section "Liquidity and Capital Resources".

Off-Balance Sheet Arrangements

There were no off-balance sheet obligations at December 31, 2010.

Outstanding Share and Debenture Data

Arcan's issued share capital consists of:	Year Ended December 2010	Year Ended December 2009	April 5, 2011
Common shares	87,670,446	47,940,060	88,110,446
Warrants	-	586,631	-
Performance warrants	-	750,000	-
Stock options	8,390,500	4,671,166	8,440,500
Debentures	-	-	\$86,250,000

In 2010, Arcan's number of issued and outstanding shares increased by 39,730,386 shares. The number of issued and outstanding shares increased as a result of offerings of 26.0 million shares in March and 10.4 million shares in November and various warrant, option and performance share exercises throughout the year for 3.3 million shares. All outstanding warrants and performance shares outstanding at the end of 2009 have been exercised or cancelled and none remain outstanding. The number of outstanding stock options changed primarily as a result of the issuance of 2.9 million options in the second quarter and the issuance of 2.9 million options in the fourth quarter of 2010 to officers, directors and employees of the Corporation. Since the end of 2010, Arcan issued \$86,250,000 aggregate amount of Debentures.

Officers or directors of Arcan exercised 1,215,500 options and sold the shares for the year ended at December 31, 2010. An officer of Arcan exercised 400,000 options and sold the shares in January 2011. Two officers and one employee of the Corporation exercised 750,000 performance warrants prior to their expiry on March

1, 2010. Other than the 400,000 options exercised by and officer and 2,000 shares sold by a Director, there have been no other sales or exercises of options since the end of 2010 by officers or directors of Arcan. Officers of the Corporation purchased an aggregate amount of \$1.3 million Debentures in the February, 2011 financing.

Outlook

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

- significant expansion of drilling horizontal multi-stage fracture wells in the Swan Hills reef light oil play on its 150 net sections of land. Arcan also intends increase and expand the existing water injection scheme;
- continued development and water injection in the Hamburg GG pool; and
- ongoing review of opportunities at in the McLeod area.

Arcan's 2011 capital program is expected to remain within cash flow, the Debenture issue and expanded debt capacities and will continue to focus mainly on rapid growth through in the Swan Hills. Arcan is currently developing a strategy to best exploit its land base over the long term. The Corporation's strengths include over \$247 million of tax pools, a strong slate of directors, experienced staff, excess productive capacity for tie-in, recently initiated and growing waterfloods, new drilling plans and significant growth potential.

Industry Trends

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

The first trend currently affecting the oil and gas industry, as well as many other industries, is the impact on capital markets caused by investor uncertainty in the credit markets and the global economy through 2010 and into 2011. Global economics ultimately dictate commodity demand and therefore prices. Arcan realizes that it is dependent on price fluctuations, is a price taker and therefore must maintain financial flexibility to deal with uncertain commodity prices. The current optimistic nature of the oil and gas industry has resulted in numerous opportunities for equity financings. Arcan has participated in these financings as it is unable to estimate the timing or magnitude of stock market corrections in the context of the evolving current global economic situation.

A second trend is the volatility of commodity prices. Crude oil is influenced by the world economy and the ability of the Organization of Petroleum Exporting Countries to adjust supply to world demand. Recently, crude oil prices have been kept high by increased demand from growing economies in China and India as well as the ongoing political events causing disruptions in the supply of oil, and concern over potential supply disruptions triggered by unrest in the Middle East. More recently, volatility has increased over short term supply concerns as a result of unrest in the Middle East. Concerns continue to rise regarding geopolitical control of energy resources and the relative stability of those energy sources. Significant concerns have also arisen on oil demands both in the short and medium term as impacts on economic development are uncertain related to the disastrous earthquake, tsunami and nuclear facility issues in Japan. Demands are also being questioned as the world endures financial uncertainty and possible bankruptcies of certain countries inside of the European Union.

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

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

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

Arcan's need for capital will be both short-term and long-term in nature. Short-term working capital will be required to finance accounts receivable, drilling deposits and other similar short-term assets, while the acquisition, exploration and development of oil and natural gas properties requires substantial amounts of long-term capital. In addition to equity financing, Arcan uses several sources of financing, including internally generated cash flow, debentures and bank debt. Current economic conditions including the variable global credit and equity markets have elevated the risks associated with this aspect of Arcan's business.

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

Business Risks

Arcan is engaged in the business of exploration, development, production and acquisition of crude oil and natural gas. This business has many risks that even a combination of knowledge, experience and careful evaluation may not be able to overcome. These risks may cause Arcan's actual performance and financial results in future periods to differ materially from any estimates or projections of future performance or results expressed or implied by forward-looking information in this MD&A. For a comprehensive discussion of the risk factors affecting Arcan and its business and operations, readers are encouraged to reference the risks covered in Arcan's annual information form for the year ended December 31, 2010 under the heading "Risk Factors" which risk factors are incorporated by reference herein.

Arcan's principal business risks are related to finding and developing economic hydrocarbon reserves efficiently and its ability to fund the capital expenditure program. Without the ongoing addition of new oil and natural gas reserves, any existing reserves Arcan has, and the production therefrom, will decline over time as the existing reserves are produced. A future increase in Arcan's reserves will depend not only on 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-stream since February 23, 2010. This limited time frame for data creates risks for unexpected production profiles.

Arcan attempts to manage its business risks. Firstly, Arcan has an experienced, talented, and highly motivated staff of oil and natural gas professionals. Arcan also operates almost all of its properties. This enables Arcan to control the timing, direction and costs related to exploration and development opportunities. Arcan's geological focus is on areas in which the prospects are well understood by Management. Technological tools are regularly used to reduce risk and increase the probability of success. Arcan closely follows all government regulations and has an up-to-date emergency response plan that has been communicated to field operations by Management. Arcan also carries insurance coverage to attempt to minimize potential losses.

Application of Critical Accounting Estimates

The significant accounting policies used by Arcan are disclosed in note 2 to the audited Financial Statements for the years ended December 31, 2010 and 2009. Certain accounting policies require that Management make appropriate decisions with respect to the formulation of estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Management reviews its estimates on a regular basis. The emergence of new information and changed circumstances may result in actual results or changes to estimated amounts that differ materially from current estimates. The following discussion identifies the critical accounting policies and practices of the Corporation and helps assess the likelihood of materially different results being reported.

Reserves

Under CSA Staff Notice 51-324 – *Glossary to NI 51-101*, "Proved reserves" are defined as those reserves that can be estimated with a high degree of certainty to be recoverable. It is likely that the actual remaining quantity recovered will exceed the estimated proved reserves.

The level of certainty should result in at least a 90 percent probability that the quantities actually recovered will equal or exceed the estimated Proved reserves. It does not mean that there is a 90 percent probability that the Proved reserves will be recovered; it means there must be at least a 90 percent probability that the given amount or more will be recovered.

"Probable reserves" are those additional reserves that are less certain to be recovered than provided reserves. It is equally likely that the actual remaining quantities recovered will be greater or less than the sum of the estimated Proved plus Probable reserves.

"Proved plus Probable" reserves are the most likely case and are based on a 50 percent certainty that they will equal or exceed the reserves estimated.

These oil and gas reserve estimates are made using all available geological and reservoir data, as well as historical production data. All of the Corporation's reserves were evaluated and reported on by an independent qualified reserves evaluator. However, revisions can occur as a result of various factors including: actual reservoir performance, changes in price and cost forecasts or, a change in the Corporation's plans. Reserve changes will impact the financial results as reserves are used in the calculation of depletion and are used to assess whether asset impairment occurs. Reserve changes also affect other non-GAAP measurements such as net asset value calculations.

Depletion and Depreciation

The Corporation follows the full cost method of accounting for oil and natural gas properties. Under this method, all costs related to the acquisition of, exploration for and development of oil and natural gas reserves are capitalized whether successful or not. Depletion of the capitalized oil and natural gas properties and depreciation of production equipment which includes estimated future development costs less estimated salvage values are calculated using the unit-of-production method, based on production volumes in relation to estimated proven reserves.

An increase or decrease in estimated proved reserves would result in a reduction or increase in depletion expense. A decrease or increase in estimated future development costs would also result in a reduction or increase in depletion expense.

Unproved Properties

The cost of acquisition and evaluation of unproved properties are initially excluded from the depletion calculation. An impairment test is performed on these assets to determine whether the carrying value exceeds the fair value. Any excess in carrying value over fair value is an impairment. When proved reserves are assigned or a property is considered to be impaired, the cost of the property or the amount of the impairment will be added to the capitalized costs for the calculation of depletion.

Ceiling Test

The ceiling test is a cost recovery test intended to identify and measure potential impairment of the value of assets relative to the cost of those assets as carried on the Corporation's balance sheet. An impairment loss is recorded if the sum of the undiscounted cash flows (assuming certain commodity prices, operating costs, royalty rates and other deductions) expected from the production of the proved reserves and the lower of cost and market of unproved properties does not exceed the values of the petroleum and natural gas assets as carried in the Corporation's balance sheet. An impairment loss is recognized to the extent that the carrying value exceeds the sum of the discounted cash flows expected from the production of proved and probable reserves and the lower of cost and market of unproved properties. The cash flows are estimated using the future product prices and costs and are discounted using the risk free rate. By their nature, these estimates are subject to measurement uncertainty and the impact on the financial statements could be material. Any impairment as a result of this ceiling test will be charged to operations as additional depletion and depreciation expense.

A ceiling test was performed quarterly by the Corporation and at each testing period, the Corporation had sufficient value of the Corporation's proved and probable reserves under the formula to cover the value of the petroleum and natural gas assets as carried on the Corporation's balance sheet.

Asset Retirement Obligations

The Corporation records a liability for the fair value of legal obligations associated with the retirement of petroleum and natural gas assets. The liability is equal to the discounted fair value of the obligation in the period in which the asset is recorded with an equal offset to the carrying amount of the asset. The liability then accretes to its fair value with the passage of time and the accretion is recognized as an expense in the financial statements. The total amount of the asset retirement obligation is an estimate based on the Corporation's net ownership interest in all wells and facilities, the estimated costs to abandon and reclaim the wells and facilities and the estimated timing of the costs to be incurred in future periods. The total amount of the estimated cash flows required to settle the asset retirement obligation, the timing of those cash flows and the discount rate used to calculate the present value of those cash flows are all estimates subject to measurement uncertainty. Any change in these estimates would impact the asset retirement liability and the accretion expense.

Income Taxes

The determination of income and other tax liabilities requires interpretation of complex laws and regulations. All tax filings are subject to audit and potential reassessment after the lapse of considerable time. In addition, the Corporation estimates when its temporary differences are expected to reverse and recognizes its tax assets and liabilities based on the legislated tax rate in those periods. Accordingly, the actual income tax liability may differ significantly from that estimated and recorded by Management.

Stock-Based Compensation

The Corporation applies the fair value method for valuing stock option grants. This method requires the Corporation to make estimates of expected stock volatility, the expected hold period prior to exercising options, expected forfeitures of options and expected dividends to be declared by the Corporation. The calculation of the fair value of stock based compensation is not adjusted for the value actually received by the optionees. The stock-based compensation expense will not represent the actual fair value received by the optionees as the fair value is estimated at the time of grant and is not adjusted. Due to the time period and the number of estimates involved, it is likely that the actual value of the options will differ from what has been recorded in the financial statements.

Financial Instruments Valuation

The fair value of the Corporation's derivative contracts is determined using forward price curves as at the balance sheet date in combination with the remaining contracted petroleum and natural gas volumes and includes a volatility factor in the calculations. Changes in the forward price curves or volatility factor will result in a corresponding increase or decrease in the fair value of the derivative contacts.

Other Estimates

The accrual method of accounting requires management to incorporate certain estimates including estimates of revenues, royalties and operating costs as at a specific reporting date, but for which actual revenues and costs have not yet been received. In addition, estimates are made on capital projects which are in progress or recently completed where actual costs have not been received by the reporting date. The Corporation obtains the estimates from the individuals with the most knowledge of the activity and from all project documentation received. The estimates are reviewed for reasonableness and compared to past performance to assess the reliability of the estimates. Past estimates are compared to actual results in order to make informed decisions on future estimates.

Future Accounting Policies

International Financial Reporting Standards

Effective January 1, 2011, Canadian public companies are required to adopt International Financial Reporting Standards ("**IFRS**"). Arcan's financial statements up to and including the December 31, 2010 financial statements have been reported in accordance with GAAP as it existed on each reporting date. Financial statements for the quarter ended March 31, 2011, including comparative amounts, are being prepared on an IFRS basis.

The Corporation continues its work to finalize the impact on its financial statements of the transition from GAAP 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. As Arcan continues to assess the impacts of IFRS it does not anticipate any significant changes to the business practices of the Corporation. Also, Arcan does not anticipate and technical violations or defaults under the Credit Facility due to the adoption of IFRS.

In 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 first quarter of 2011. Progress has been made regarding policy choices and quantification of differences, although some 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. The Corporation, under the exemption, will allocate historic costs to cash generating units and components subject to depletion based on reserve values.

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. The Corporation has determined that it has \$10.7 million of exploration assets with the balance of \$129.6 million considered to be development assets on transition to IFRS as of January 1, 2010.

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. On transition, the Corporation will not recognize any impairment in its E&E assets or development assets.

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 which should result in a reduction to depreciation and depletion expense.

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 yet for the 2010 comparative year.

Decommissioning Liabilities

Under IFRS, decommissioning liabilities (referred to as "asset retirement obligations" under GAAP) are likely to increase as a result to the change from a credit-adjusted risk-free rate to a risk-free rate in the discounting of the liabilities to their present value. In addition, any change to the discount rate would affect the entire liability and not just current period additions. The Corporation estimates the impact on transition to be \$2.3 million with a corresponding increase to the deficit as allowed for under the IFRS elective exception.

Stock Based Compensation

IFRS standards require stock-based awards that vest in instalments, such as on anniversaries of the grant date, to be accounted for as though each instalment or vesting date were a separate award. This will result in stock-based compensation expense likely increasing in the earlier vesting periods immediately following new grants. Under IFRS, estimates of the number of stock-based awards expected to vest or expected to be forfeited prior to their expiry will also have a quantitative impact on the amount of stock-based compensation expense recorded over the vesting period. GAAP allowed for forfeitures to be recorded as they occurred and for the expense to be recognized on a straight line basis for the entire award. The Corporation does not expect a significant impact on transition.

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

GAAP and IFRS follow the liability method of accounting for income taxes whereby tax liabilities and assets are recognized on temporary differences. The Corporation's future income tax liability will be affected by the tax effects resulting from the IFRS changes discussed in this section. The tax effect resulting from the IFRS changes has not yet been finalized. In addition, while GAAP separated future income taxes between current and non-current, IFRS allows only for the presentation of non-current future income tax assets and liabilities.

IFRS also differs in the measurement of Flow-Through Shares by the Corporation, with the premium initially set-up as a liability when the Flow-Through Shares are issued and then released through earnings subsequently when the tax impact is recorded. The Corporation estimates this change to result in a deferred liability of \$0.1 million being recognized on transition, an increase to share capital of \$2.0 million with the offsetting \$2.1 million recognized against the deficit.

Legal Advisories

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

Please refer to the "Abbreviations" in the Corporation's annual information form for the year ended December 31, 2010 for meanings of certain abbreviations used in this MD&A.

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

Forward-Looking Information and Statements

This management's discussion and analysis ("MD&A") contains certain forward-looking information and statements within the meaning of applicable securities laws. The use of any of the words "expect", "anticipate", "continue", "estimate", "guidance", "objective", "ongoing", "may", "will", "project", "should", "believe", "plans", "intends", "possible" and similar expressions are intended to identify forward-looking information or statements. In particular, but without limiting the foregoing, this MD&A contains forward-looking information and statements pertaining to, among other things, the following: the timing, method and results of drilling and waterflood operations; estimated additional drilling locations; estimated waterflood of CO₂ recoveries; the timing and resolution of mechanical/operational issues faced by Arcan; future liquidity and financial capacity and resources; the potential inherent in Arcan's Swan Hills land base; expectations relating to increased shareholder value; results from operations and financial ratios; the volume and product mix of Arcan's oil and gas production; cost and expense estimates and expectations; Arcan's income taxes, tax liabilities and tax pools; oil and natural gas prices and Arcan's risk management programs; recovery; the impact of the Acquisition; the amount of asset retirement obligations; cash flow ratios and sensitivities; royalty rates and their impact on Arcan's operations and results; capital expenditures; Arcan's review of its Credit Facility; the reassessment of Arcan's 2011 budget; Arcan's move to a new office space; industry trends; expectations respecting the transition to IFRS and the impact of the transition to IFRS on Arcan and its financial statements; future growth including development, exploration, and acquisition, construction and development activities and related expenditures.

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

Arcan believes the material factors, expectations and assumptions reflected in the forward-looking information and statements are reasonable at this time but no assurance can be given that these factors, expectations and assumptions will prove to be correct. The forward-looking information and statements included in this MD&A are not guarantees of future performance and should not be unduly relied upon. Such information and statements involve known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking information or statements including, without limitation: changes in commodity prices; unanticipated operating results or production declines; for reasons currently unforeseen, the current drilling locations identified by Arcan may prove to be unsuitable or unavailable and drilling on the locations identified may not occur; Arcan may be unable to solve its mechanical/operational issues in the timelines anticipated, in the manner anticipated or at all; shareholder value may not be maximized in the manner suggested by Arcan or at all; 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; review's of Arcan's Credit Facility and/or budget may not occur on the timelines anticipated or at all; circumstances may arise, including changes in IFRS, regulations or economic conditions, which could change the assumptions, estimates or expectations or the information provided in respect of Arcan's transition to IFRS; 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, copies of which are available on Arcan's SEDAR profile at www.sedar.com.

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

Directors

Robert J. Dales
Independent Director

Andy Fisher
Executive Vice President, Arcan Resources Ltd.

Ed Gilmet
President and CEO, Arcan Resources Ltd.

Michael J. Laffin
Independent Director

J. Terry McCoy
Independent Director

Officers

Ed Gilmet
President and CEO

Andy Fisher
Executive Vice President

Doug Penner
CFO and Vice President Finance

Graeme Ryder
Controller

Michael J. Laffin
Corporate Secretary

Corporate Office

Suite 3200, 450 – 1st Street SW
Calgary, AB T2P 5H1
(403) 262-0321

Auditors

KPMG LLP

Evaluation Engineers

GLJ Petroleum Consultants Ltd.

Banking Syndicate Lead By

Alberta Treasury Branches

Legal Counsel

Blake, Cassels & Graydon LLP

Registrar and Transfer Agent

Valiant Trust Company

Stock Exchange Listings

TSX-V (symbol "ARN") – Common Shares

TSX-V (symbol "ARN.DB") – Debentures

Investor Relations Contact

Doug Penner
dpenner@arcanres.com
(403) 513-7234