

Canacol Energy Ltd.



May 11, 2011

Canacol Energy Ltd.

Consolidated Balance Sheets

As at
(US\$000s) (unaudited)

	March 31, 2011	June 30, 2010
Assets		
Current Assets:		
Cash and cash equivalents (note 14)	104,036	56,240
Cash - restricted (note 4a)	5,550	890
Accounts receivable	32,051	6,221
Prepaid expenses and deposits	2,635	563
Commodity contracts (note 11)	-	227
Inventory (note 5)	402	2,330
Income tax receivable	602	-
Cash call receivable short term (note 11)	4,234	1,045
	149,510	67,516
Cash call receivable long term	-	395
Cash reserved for asset retirement (note 8)	433	399
Property, plant and equipment (note 6)	116,555	90,452
	266,498	158,762
Liabilities and Shareholders' Equity		
Current Liabilities:		
Accounts payable and accrued liabilities	23,299	13,643
Payable on overlifted volumes (note 7e)	23,016	-
Royalty purchase payable (note 9e)	-	18,000
Operating lines of credit (note 4b)	616	322
Cash call payable	568	944
Taxes payable	-	292
Commodity contracts (note 11)	4,195	-
	51,694	33,201
Future income tax liability	4,779	7,864
Asset retirement obligation (note 8)	4,048	2,899
12% Convertible debentures (note 7a)	358	1,145
8% Convertible debentures (note 7b)	17,068	-
	77,947	45,109
Shareholders' equity:		
Share capital and warrants (note 9)	236,720	161,535
Contributed surplus (note 10)	18,454	12,088
12% Convertible debentures (note 7a)	40	159
8% Convertible debentures (note 7b)	12,015	-
Accumulated other comprehensive loss	389	(842)
Deficit	(79,067)	(59,287)
	(78,678)	(60,129)
	188,551	113,653
	266,498	158,762

Commitments and Contingencies (note 15)

Subsequent events (note 16)

See accompanying notes to the consolidated financial statements.

Canacol Energy Ltd.

Consolidated Statements of Loss and Comprehensive Loss and Deficit

For the three and nine months ended March 31,
(US\$000s, except per share amounts) (unaudited)

	Three months ended March 31,		Nine months ended March 31,	
	2011	2010	2011	2010
		(Restated - note 2)		(Restated - note 2)
Revenues:				
Petroleum and natural gas, net of royalties	23,452	4,992	54,340	10,334
Tariff revenue	8,677	1,607	11,468	4,452
Interest and other revenue	196	165	694	1,059
	32,325	6,764	66,502	15,845
Expenses:				
Operating and Transportation expenses	10,351	3,789	24,130	10,045
General and administrative	2,819	2,746	10,929	6,292
Interest and financial expense (note 7c)	887	696	3,592	2,227
Foreign exchange loss (gain), net (note 11)	1,918	78	(745)	(2,090)
Commodity contracts loss (gain), net (note 11)	2,724	(82)	4,678	148
Stock compensation expense (note 9f)	3,336	1,431	8,247	2,369
Depletion, depreciation and accretion	10,652	3,701	22,475	7,965
Loss on sale of promissory note	-	-	-	75
Unrealized loss on overlifting	2,137	-	2,137	-
Impairment on Brazilian properties (note 6)	-	-	9,673	-
	34,824	12,359	85,116	27,031
Income (loss) before income taxes	(2,499)	(5,595)	(18,614)	(11,186)
Current income tax expense	1,147	406	4,252	1,251
Future income tax recovery	(303)	(871)	(3,086)	(2,565)
	844	(465)	1,166	(1,314)
Net loss	(3,343)	(5,130)	(19,780)	(9,872)
Deficit, beginning of the period	(75,724)	(42,383)	(59,287)	(37,641)
Deficit, end of the period	(79,067)	(47,513)	(79,067)	(47,513)
Net loss	(3,343)	(5,130)	(19,780)	(9,872)
Other comprehensive loss:				
Foreign currency translation adjustment (note 2)	1,373	1,396	1,231	(325)
Comprehensive income (loss)	(1,970)	(3,734)	(18,549)	(10,197)

See accompanying notes to the consolidated financial statements.

Canacol Energy Ltd.

Consolidated Statements of Other Accumulated Comprehensive Loss

For the three and nine months ended March 31,

(US\$000s) (unaudited)

	Three months ended March 31,		Nine months ended March 31,	
	2011	2010	2011	2010
		(Restated - note 2)		(Restated - note 2)
Accumulated other comprehensive loss, beginning of the period	(984)	(2,375)	(842)	(654)
Foreign currency translation adjustment (note 2)	1,373	1,396	1,231	(325)
Accumulated other comprehensive income (loss), end of the period	389	(979)	389	(979)

See accompanying notes to the consolidated financial statements.

Canacol Energy Ltd.

Consolidated Statements of Cash Flows
For the three and nine months ended March 31,
(US\$000s) (unaudited)

	Three months ended March 31,		Nine months ended March 31,	
	2011	2010	2011	2010
		(Restated - note 2)		(Restated - note 2)
Cash provided by (used in):				
Operating Activities:				
Net loss from operations	(3,343)	(5,130)	(19,780)	(9,872)
Adjustments for non-cash items:				
Non-cash interest expense (note 7c)	1,040	301	2,272	949
Shares issued for services (note 9)	81	53	368	176
Shares issued for 12% convertible debenture interest (note 9)	13	115	83	225
Depletion, depreciation, and amortization	10,652	3,701	22,475	7,965
Stock compensation expense	3,336	1,431	8,247	2,369
Future income tax recovery	(303)	(871)	(3,086)	(2,565)
Impairment on Brazilian properties	-	-	9,673	-
Loss on sale of promissory note	-	-	-	75
Unrealized foreign exchange loss (gain)	1,985	(680)	460	(1,690)
Unrealized loss on overlifting payable	2,137	-	2,137	-
Unrealized commodity contract loss (gain)	2,426	(82)	4,355	148
	18,024	(1,162)	27,204	(2,220)
Change in non-cash operating working capital, (note 14)	(11,832)	(3,159)	(4,292)	(1,431)
Asset retirement obligations settled (note 8)	(4)	(240)	(4)	(235)
Cash flow from operating activities	6,188	(4,561)	22,908	(3,886)
Financing Activities:				
Issue of share capital	59,134	934	62,451	39,289
Issue of convertible debentures (note 7)	-	-	39,385	3,757
Draws (repayments) on line of credit	11	8	294	(4,757)
Repayment of long term debt	-	(1,233)	-	(7,001)
Financing and share issue costs	(3,008)	-	(4,900)	(2,038)
Cash flow from financing activities	56,137	(291)	97,230	29,250
Investing Activities:				
Property, plant, and equipment purchases	(20,665)	(4,153)	(51,309)	(15,742)
Purchase of Gemini royalty	-	-	(18,000)	8,854
Cash reserved for asset retirement	(12)	(7)	(34)	2
Cash - restricted	(5,550)	25	(4,660)	(548)
Change in non-cash investing working capital (note 14)	5,155	(3,302)	4,998	(1,547)
Cash flow used in continuing investing activities	(21,072)	(7,437)	(69,005)	(8,981)
Foreign exchange gain (loss) on cash and cash equivalents held in foreign currency	(2,365)	25	(1,200)	1,172
Unrealized loss on overlifted volume payables	(2,137)	-	(2,137)	-
Net increase (decrease) in cash and cash equivalents	36,751	(12,264)	47,796	17,555
Cash and cash equivalents, beginning the period	67,285	30,001	56,240	182
Cash and cash equivalents, end of the period	104,036	17,737	104,036	17,737
Supplementary disclosure of cash flow information:				
Interest paid	10	280	1,474	1,052
Taxes paid	3,879	-	5,084	-

See accompanying notes to the consolidated financial statements.

Notes to the Consolidated Financial Statements

For the three and nine months ended March 31, 2011 and March 31, 2010

(Unless otherwise stated, amounts presented are in thousands United States dollars currency) (unaudited)

1. BASIS OF PRESENTATION

Canacol Energy Ltd. (“Canacol” or the “Corporation”) and its subsidiaries are primarily engaged in petroleum and natural gas exploration and development activities in Colombia, Brazil and Guyana. The Corporation’s head office is located in Calgary, Alberta, Canada and the Corporation’s shares are traded on the TSX Exchange under the symbol CNE and Bolsa de Valores de Colombia (“BVC”) under the symbol CNE.C.

The interim consolidated financial statements do not include all disclosures required for annual financial statements and should be read in conjunction with the most recent audited consolidated financial statements and the notes thereto for the year ended June 30, 2010. The significant accounting policies are consistent with those in the audited annual consolidated financial statements.

2. CHANGE IN REPORTING CURRENCY

Effective June 30, 2010, management changed the reporting currency of the Corporation from Canadian dollars (C\$) to United States dollars (\$) or (US\$), as this currency was considered to be more appropriate for the Corporation’s investors and other users of the financial statements. In making this change in reporting currency, the Corporation has followed the recommendations of the Emerging Issues Committee (“EIC”) of the Canadian Institute of Chartered Accountants (“CICA”) set out in EIC-130, “*Translation Method when the Reporting Currency Differs from the Measurement Currency or there is a Change in the Reporting Currency*”.

Financial statements for fiscal year 2010 presented as comparative herein have been translated from Canadian dollars into United States dollars using the current rate method. Using this method, all consolidated assets and liabilities have been translated using the exchange rate at the balance sheet date. The consolidated statements of loss and comprehensive loss and deficit and cash flows have been translated using the prevailing average exchange rates for the periods. Any resulting exchange rate difference due to this translation has been included in Other Accumulated Comprehensive Income, a separate component of Shareholders’ Equity. All comparative financial information being presented has been restated to reflect the Corporation’s financial statements as if they had been historically reported in United States dollars.

All supplementary information in the notes to the consolidated financial statements has been translated using the current rate method as is consistent with the consolidated financial statements.

3. CHANGE IN ACCOUNTING POLICIES

The following represent the changes in accounting policies as a result of new GAAP pronouncements:

International Financial Reporting Standards (“IFRS”)

On February 13, 2008, the Canadian Accounting Standards Board (“AcSB”) confirmed the mandatory changeover date to International Reporting Standards (“IFRS”) for Canadian profit-orientated publicly accountable entities (“PAEs”) such as Canacol. The AcSB requires that IFRS compliant financial statements be prepared for annual and interim financial statements commencing on or after January 1, 2011. Canacol has a June 30 year-end, thus the first unaudited interim financial statements under IFRS will be for the quarter ending September 30, 2011, with comparative financial information for the quarter ending September 30, 2010. The first audited consolidated financial statements will be for the year ending June 30, 2012, with comparative financial information for the year ending June 30, 2011.

Notes to the Consolidated Financial Statements

For the three and nine months ended March 31, 2011 and March 31, 2010

(Unless otherwise stated, amounts presented are in thousands United States dollars currency) (unaudited)

4. CASH RESTRICTED AND BANK DEBT

a. Cash restricted

As at March 31, 2011, the Corporation, through its wholly subsidiary Canacol Energy Colombia S.A. (formerly Rancho Hermoso S.A.) has placed funds in trust accounts in a Colombian bank for a total of \$5,550 as required by the Agencia Nacional de Hidrocarburos (“ANH”) to ensure the payment of its obligations pursuant to the exploration agreements for the Cedrela, Tamarin and Pacarana exploration blocks. As at June 30, 2010, \$890 was restricted cash reserved for principal instalments due within the next two months on the Corporation’s debt facilities. The cash restricted as at June 30, 2010 was released to the Corporation on July 15, 2010 after the repayment in full of the outstanding balance on the reserve credit facility.

b. Revolving operating lines of credit

The Corporation, through its wholly owned subsidiary Canacol Energy Colombia S.A. has revolving operating lines of credit. These lines of credit bear interest at the Depósitos a Término Fijo (“DTF”) interest rate, a Colombian benchmark interest rate, plus spreads of 2% per annum on the balance outstanding resulting in an average rate of 5.5% for the three and nine months ended March 31, 2011 (Three and nine months ended March 31, 2010 – average of 9.9% and 10.5%, respectively). At March 31, 2011, \$616 had been drawn on these facilities (June 30, 2010 – \$322). The operating lines of credit are unsecured. The limits on the lines of credit are based on regular negotiations with the Colombian banks on a draw by draw basis.

In addition to the lines of credit discussed above, the Corporation, through its subsidiary Canacol Energy Colombia S.A., also obtained three additional unsecured revolving lines of credit with an aggregate borrowing base of \$5,675 (COP\$ 10.6 billion). The lines of credit have similar interest rates as described above. The Corporation has not drawn down any amounts under these lines of credit.

5. INVENTORY

	As at March 31, 2011	As at June 30, 2010
	\$	\$
Crude oil - Hocol	402	2,330

The Hocol S.A. (“Hocol”) crude oil marketing agreement stipulates that Canacol retains ownership of oil in transit until it reaches the export pipeline which can take several days whereupon ownership of the oil transfers from Canacol to Hocol. At March 31, 2011, there was approximately 42,000 bbls of oil in transit. These barrels have been included in the Corporation’s production volumes. However, revenue of \$3,825 and expenses of \$402 associated with these barrels will be reported as April sales when title transfer occurred. This timing difference in revenue recognition has the effect of deferring \$3,423 cash flow net of earnings from oil produced in March to the following month.

Additionally, as March 31, 2011, the Corporation holds 37,326 bbls of oil in tanks, due to Ecopetrol, relating to their share of the participation contract.

Notes to the Consolidated Financial Statements

For the three and nine months ended March 31, 2011 and March 31, 2010

(Unless otherwise stated, amounts presented are in thousands United States dollars currency) (unaudited)

6. PROPERTY, PLANT AND EQUIPMENT

	As at March 31, 2011			As at June 30, 2010		
	Cost	Accumulated Depreciation	Net Book Value	Cost	Accumulated Depreciation	Net Book Value
	\$	\$	\$	\$	\$	\$
Petroleum and natural gas properties ("P&NG")	159,253	(43,474)	115,779	111,987	(22,860)	89,127
Office equipment	1,250	(512)	738	520	(276)	244
Equipment & other	55	(17)	38	1,098	(17)	1,081
	160,558	(44,003)	116,555	113,605	(23,153)	90,452

The costs excluded from the depletion calculation include undeveloped land costs, completion equipment inventory, and drilling in progress. As at March 31, 2011, total costs excluded from the depletion calculation and ceiling test were \$26,459 (June 30, 2010 - \$11,913). The Corporation has capitalized \$1,208 indirect overhead costs for the three and nine months ended March 31, 2011. No indirect overhead costs were capitalized for the three and nine months ended March 31, 2010.

In November 2010, the Corporation negotiated the disposition of its non-core, non-operated producing properties in Brazil for cash consideration of approximately \$3.8 million, subject to approval by Brazilian regulatory authorities and other conditions of closing. There is no assurance as to when these conditions will be satisfied. Management determined that since the Corporation will not realize the carrying value of these assets, an impairment charge of approximately \$9.7 million would be recorded for nine month period ended March 31, 2011.

As at March 31, 2011 no impairments were required or recorded on Colombian proved and unproved properties or the remaining Brazilian undeveloped properties.

7. DEBT

a. 12% Convertible debentures

In September 2009, the Corporation raised aggregate gross proceeds of \$3,688 (C\$4,000) through the issuance of Canadian dollar denominated convertible unsecured subordinate debentures (the "Debentures"). The Debentures bear interest at 12% per annum, payable quarterly through the issue of common shares at a price equal to a 10% discount to the volume weighted average trading price of the Corporation's common shares for the 10 trading days immediately preceding the quarterly interest payment date. The Debentures mature within 24 months of the issuance, and are convertible into common shares of the Corporation at the holder's option at a conversion price equal to \$0.33 (C\$0.36) per common share. At maturity, the Corporation has the right to repay all or part of the Debentures through the issuance of common shares at price equal to 95% of weighted average trading price of the shares for 20 consecutive trading days ending on the 5th trading day immediately preceding the maturity date.

Notes to the Consolidated Financial Statements

For the three and nine months ended March 31, 2011 and March 31, 2010

(Unless otherwise stated, amounts presented are in thousands United States dollars currency) (unaudited)

As the Debentures are convertible, the liability and equity components have been presented separately. The liability component of the conversion feature was determined to be \$3,046 and has been recorded as long-term debt with the remaining \$642 allocated to equity. The debt component was measured at the issue date as the present value of cash payments of interest and principal under the terms of Debentures using a discount rate of 26%.

During the three and nine months ended March 31, 2011, 41,667 and 3,377,484 (during three and nine months ended March 31, 2010 – “Nil”) common shares were issued as a result of the conversion of \$15 and \$1,081 face amount of 12% convertible debentures in each period respectively.

	Debt Component	Equity Component	Total
	\$	\$	\$
Balance, June 30, 2010	1,145	159	1,304
Debentures issued	-	-	-
Transaction costs	-	-	-
Impact of foreign exchange	91	60	151
Accretion of debt component	73	-	73
Accretion of transaction expenses	130	-	130
Conversion to common shares	(1,081)	(179)	(1,260)
Balance, end of period	358	40	398

b. 8% Convertible debenture

On July 16, 2010, the Corporation closed an offering for gross proceeds of \$39,385 (C\$41,500) and net proceeds of \$37,540 (C\$39-,506) principal amount of Canadian dollar denominated convertible unsecured debentures with an interest rate of 8% per annum, payable semi-annually on the last day of June and December commencing on December 31, 2010, maturing June 30, 2015. The debentures are convertible at the holder’s option into common shares of the Corporation at any time prior to the earlier of either the maturity date or the business day immediately preceding the date fixed by the Corporation for redemption at a conversion price of \$1 (C\$1.0526) per common share, being the ratio of 950 common shares per C\$1,000 principal amount of debentures. Transaction costs incurred of \$1,845. The Debentures will not be redeemable prior to June 30, 2013.

As the debentures are convertible, the liability and equity components have been presented separately. The liability component of the conversion feature was determined to be \$21,394 and has been recorded as long-term debt with the remaining \$17,991 allocated to equity. The debt component was measured at the issue date as the present value of cash payments of interest and principal under the terms of Debentures using a discount rate of 26%.

During the three and nine months ended March 31, 2011, 2,360,750 and 11,068,450 common shares were issued as a result of the conversion of \$2,663 and \$12,121 face amount of 8% convertible debentures, respectively in each period.

Notes to the Consolidated Financial Statements

For the three and nine months ended March 31, 2011 and March 31, 2010

(Unless otherwise stated, amounts presented are in thousands United States dollars currency) (unaudited)

	Debt Component	Equity Component	Total
	\$	\$	\$
Balance, June 30, 2010	-	-	-
Debentures issued	21,394	17,991	39,385
Transaction costs	(1,002)	(843)	(1,845)
Impact of foreign exchange	1,678	10	1,688
Accretion of debt component	1,600	-	1,600
Accretion of transaction expenses	156	-	156
Conversion to common shares	(6,758)	(5,143)	(11,901)
Balance, end of period	17,068	12,015	29,083

c. Interest and financial expense

Interest and financial expense is comprised of both cash and non-cash components. The non-cash components relate to accretion of the debentures. Details of the cash and non-cash components of interest and financial expense are as follows:

	Three Months ended March 31		Nine months ended March 31	
	2011	2010	2011	2010
	\$	\$	\$	\$
Accretion of transaction costs on loan	-	231	-	704
Accretion of transaction costs on convertible debentures	417	41	599	94
Accretion of convertible debentures - debt portion	623	29	1,673	151
Non-cash interest expense	1,040	301	2,272	949
Cash interest expense	10	280	1,474	1,052
Interest expense paid in shares on convertible debentures	13	115	83	226
Impact of foreign exchange	(176)	-	(237)	-
Total interest and financial expense	887	696	3,592	2,227

d. Principal repayments

As at March 31, 2011, future repayments on the Corporation's outstanding debt and credit facilities for the next five calendar years are as follows:

	2011 (9 months)	2012	2013	2014	2015	Total
12% Convertible debenture (note 7a) ¹	\$398	-	-	-	-	\$398
	C\$400	-	-	-	-	C\$400
8% Convertible debenture (note 7b) ^{1,2}	\$1,847	\$2,463	\$2,463	\$2,463	\$30,785	\$40,021
	C\$1,791	C\$2,388	C\$2,388	C\$2,388	C\$29,849	C\$38,804
Line of credit (note 4b)	\$616	-	-	-	-	\$616
	C\$597	-	-	-	-	C\$597
Total	\$2,861	\$2,463	\$2,463	\$2,463	\$30,785	\$41,035
	C\$2,788	C\$2,388	C\$2,388	C\$2,388	C\$29,849	C\$39,801

¹ Assumes no conversion of the 12% and 8% convertible debentures after the quarter ended March 31, 2011.

² Includes cash interest payments of approximately \$9.2 million.

Notes to the Consolidated Financial Statements

For the three and nine months ended March 31, 2011 and March 31, 2010

(Unless otherwise stated, amounts presented are in thousands United States dollars currency) (unaudited)

e. Payable Overlifted volume

Included in overlifted volume payable is a provision, under a participation contract with Ecopetrol S.A., for repayment in barrels to Ecopetrol to replace volumes of crude oil sold for the Corporation's account during the period. The market value of the liability of \$23,016, net of transportation reimbursement, has been estimated as at March 31, 2011, based on the overlifted volume of 281,518 barrels.

8. ASSET RETIREMENT OBLIGATION

	Nine months ended March 31, 2011	Year ended June 30, 2010
	\$	\$
Asset retirement obligation, opening balance	2,899	1,992
Liabilities incurred and acquired	918	664
Liabilities settled	(4)	(23)
Revision of estimates	-	44
Accretion expense	235	217
Variance due to foreign exchange	-	5
Asset retirement obligation, ending balance	4,048	2,899

As at March 31, 2011, the estimated total undiscounted amount required to settle the asset retirement obligation was \$5,085 (June 30, 2010 - \$3,462) and these costs are expected to be settled over the useful lives of the underlying assets which currently extend up to 23 years into the future. Estimated cash flow has been computed using a credit-adjusted risk free discount rate of 9.5% and a country inflation rate as follows: Canada 2.0%, Brazil 5.0%, and Colombia 4.5%. In accordance with Brazilian and Colombian regulations, as of March 31, 2011, a total of \$433 (June 30, 2010 - \$399) of cash has been reserved for future asset retirement.

9. SHARE CAPITAL

a. Authorized

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

b. Issued

Notes to the Consolidated Financial Statements

For the three and nine months ended March 31, 2011 and March 31, 2010

(Unless otherwise stated, amounts presented are in thousands United States dollars currency) (unaudited)

	Nine months ended March 31, 2011		Year ended June 30, 2010	
	Number of Securities	\$	Number of Securities	\$
Issued and outstanding				
Common shares				
Common shares outstanding, opening balance	421,466,165	157,532	178,874,169	60,676
Issued on private placements (note 9d)	41,745,000	58,267	221,744,098	95,265
Issued for consulting services	320,533	368	503,678	213
Issued on purchase of royalty interests (note 9e)	4,421,260	3,405	166,667	59
Issued to agents on 12% convertible debentures	-	-	1,130,436	360
Issued to agents on private placement (note 9d)	-	-	333,333	49
Issued on interest payments for 12% convertible debentures	74,849	83	779,016	335
Stock options exercised	7,154,396	2,324	822,267	136
Warrants exercised	9,276,524	1,860	10,487,500	2,201
Issued to employees as signing bonus	104,999	174	-	-
Deferred Shares issued to employees	90,000	66	-	-
Debenture conversions	14,445,934	13,202	6,625,001	2,373
Contributed surplus reclassification related to warrants exercised	-	473	-	530
Contributed surplus reclassification related to stock options exercised	-	1,849	-	86
Share issuance costs	-	(3,008)	-	(4,751)
Common shares outstanding, ending balance	499,099,660	236,595	421,466,165	157,532
Shares to be issued ¹	-	-	4,421,260	3,405
	499,099,660	236,595	425,887,425	160,937
Warrants				
Warrants outstanding, opening balance	16,122,024	598	34,000,000	990
Issued on sale of promissory note (note 9c)	-	-	1,500,000	70
Issued on private placement (note 9c)	-	-	1,109,524	68
Cancelled	-	-	(10,000,000)	-
Exercised	(9,276,524)	(473)	(10,487,500)	(530)
Warrants outstanding, ending balance	6,845,500	125	16,122,024	598
Total share capital, ending balance		236,720		161,535

¹ In connection with the purchase of royalty interests, the Corporation issued 4,421,260 common shares of the Corporation on July 16, 2010. See note 9e.

c. Warrants

On July 7, 2009, the Corporation sold a \$1,000 promissory note receivable for proceeds of \$910 to an arm's length party. Canacol also issued to the lender 1,500,000 warrants, with each warrant being exercisable at a price of \$0.25 (C\$0.30) for 18 months. The fair value of the warrants was calculated to be \$70, using the Black Scholes pricing model based on the following assumptions: risk-free rate of 2.42%, expected life of 18 months, no dividends, and an expected volatility of 99.64%. These warrants were fully exercised during the year ended June 30, 2010.

On July 23, 2009, the Corporation issued 1,109,524 warrants at an exercise price of \$0.28 (C\$0.30) per share in connection with a private placement. The fair value of the warrants issued on the private placement was calculated to be \$68 using the Black-Scholes pricing model based on the following assumptions: risk-free rate of 2.58%, expected life of 18 months, no dividends, and an expected volatility of 99.64%. These warrants were fully exercised during the quarter ended March 31, 2011.

On June 30, 2010, the Corporation cancelled warrants issued to a creditor upon repayment of the reserves based credit facility loan for \$1.2 million.

Notes to the Consolidated Financial Statements

For the three and nine months ended March 31, 2011 and March 31, 2010

(Unless otherwise stated, amounts presented are in thousands United States dollars currency) (unaudited)

	Nine months ended March 31, 2011		Year ended June 30, 2010	
	Number of Warrants	Weighted Average Exercise Price	Number of Warrants	Weighted Average Exercise Price
Opening	16,122,024	\$0.18	34,000,000	\$0.34
Issued	-	-	2,609,524	\$0.28
Exercised	(9,276,524)	\$0.18	(10,487,500)	\$0.19
Cancelled	-	-	(10,000,000)	\$0.75
Ending	6,845,500	\$0.18	16,122,024	\$0.18

Exercisable warrants as at March 31, 2011 have the following exercise prices and expiry dates:

Number of Warrants	Exercise Price	Expiry Date
5,667,500	\$0.17	May 14, 2011
1,178,000	\$0.18	May 28, 2011
6,845,500	\$0.18	2 months

d. Financings

The following financings occurred during the year ended June 30, 2010:

- On July 23, 2009, the Corporation closed a private placement equity financing for gross proceeds of \$345. The Corporation issued a total of 2,219,048 units at a price of \$0.15 (C\$0.17) per unit. Each unit issued pursuant to the private placement consisted of one common share of the Corporation and one-half of one common share purchase warrant, with each whole warrant entitling the holder to acquire one common share at a price of \$0.28 (C\$0.30) until January 23, 2011. Share issuance costs of \$94 were incurred in the offering.
- On October 15, 2009, the Corporation closed a private placement equity financing, including the exercise, in full, of the underwriters' option, for total gross proceeds of \$38,823 and net proceeds of \$36,797. Pursuant to the financing, the Corporation issued 142,858,000 common shares at a price of \$0.27 (C\$0.28) per common share. The Corporation issued 333,333 common shares as an agent commission in connection with the October 15, 2009 private placement.
- In May 2010, the Corporation closed a private placement financing, on a "bought deal" basis, for total gross proceeds of \$56,095 and net proceeds of \$53,465. Pursuant to the financing, the Corporation issued 76,667,050 common shares at a price of \$0.73 (C\$0.75) per common share.

Notes to the Consolidated Financial Statements

For the three and nine months ended March 31, 2011 and March 31, 2010

(Unless otherwise stated, amounts presented are in thousands United States dollars currency) (unaudited)

The following financings occurred in the nine months ended March 31, 2011:

- The Corporation issued \$39,385 (C\$41,500) of 8% convertible debentures during July 2010. See note 7b.
- In February 2011, the Corporation closed an equity financing, for total gross proceeds of \$58,267 (C\$57,608) and net proceeds of \$55,259 (C\$54,656). Pursuant to the financing, the Corporation issued 41,745,000 common shares at a price of C\$1.38.

e. Gemini purchase royalty interest

In 2009, the Corporation executed a series of agreements with Gemini Oil and Gas Fund II, L.P. (“Gemini”), whereby Gemini agreed, subject to certain preconditions, to invest up to \$9,000, to fund a portion of the Corporation’s development and appraisal programs on its producing assets in Colombia in exchange for royalties generating earnings from 11% to 31% in the Corporation’s interests in certain revenue after government royalties less field operating costs.

Effective June 30, 2010, the Corporation agreed to acquire the overriding royalty held by Gemini for \$21,405. On July 16, 2010, the Corporation issued 4,421,260 common shares of the Corporation in connection with the purchase of royalty interest from Gemini in addition to a \$18,000 cash payment to Gemini.

f. Stock Options

Outstanding options expire at various dates between November 2011 and January 2016. As at March 31, 2011, a total of 14,200,671 vested options were exercisable at a weighted average exercise price of \$0.55 per common share and a total of 34,184,005 options were issued and outstanding at a weighted average exercise price of \$0.76.

	Nine months ended March 31, 2010			Year ended June 30, 2010		
	Number of Stock Options	Weighted Average Exercise Price \$	Fair Value Assigned \$	Number of Stock Options	Weighted Average Exercise Price \$	Fair Value Assigned \$
Opening	24,909,401	0.36	6,721	12,494,334	0.23	2,115
Exercised	(7,154,396)	0.37	(1,953)	(822,267)	0.14	(81)
Cancelled	(410,000)	1.01	(313)	(736,666)	0.39	(9)
Granted	16,839,000	1.15	13,506	13,974,000	0.47	4,696
Ending	34,184,005	0.76	17,961	24,909,401	0.36	6,721

As at March 31, 2011, \$8,287 (June 30, 2010 - \$2,457) of stock based compensation expense remains unrecognized and will be recognized in future periods as options vest. During the three and nine months ended March 31, 2011, \$3,336 and \$8,247 stock based compensation expense (Three and nine months ended March 31, 2010 - \$1,431 and \$2,369) has been recognized in the consolidated statement of loss. Options granted in the period were valued using the Black-Scholes pricing model and the following assumptions:

Notes to the Consolidated Financial Statements

For the three and nine months ended March 31, 2011 and March 31, 2010

(Unless otherwise stated, amounts presented are in thousands United States dollars currency) (unaudited)

	Nine months ended March 31, 2010	Year ended June 30, 2010
Risk-free interest rate	1.97% - 2.6%	2.5% - 2.73%
Expected life of options	5 years	5 years
Dividend yield	Nil	Nil
Expected volatility	62% - 126%	100% - 116%
Weighted average fair value price	\$0.55	\$0.27

g. Per share amounts

For the three and nine months ended March 31, 2011 and 2010, diluted loss per share is the same as basic loss per share as the effect of the exercise of options, convertible debentures and warrants on loss per share would be anti-dilutive due to losses during the three and nine months ended March 31, 2011. In calculating the basic and diluted net loss per share for the three and nine month ended March 31, 2011 and 2010, the weighted average number of common shares used in the calculation of basic and diluted net income per share is shown below.

	Three months ended March 31,		Nine months ended March 31,	
	2011	2010	2011	2010
Basic	471,056,119	332,288,327	442,606,464	271,705,698
Diluted	471,056,119	332,288,327	442,606,464	271,705,698

h. Restricted Share Units

Obligations for common shares under the Corporation's share award plan for employees and officers at the Corporation are accrued as stock based compensation expense and contributed surplus over the vesting period. Fluctuations in the price of the Corporation's common share change the accrued stock compensation expense and are recognized over the remaining vesting period.

In May 2010, the Corporation issued 360,000 restricted share units to an officer. The restricted stock units will vest as to 25% every six months from the grant date over a period of two years. In November 2010, the Corporation issued 300,000 restricted share units to an employee. The restricted share unit will vest as to 33% every six months from the grant date over a period of 18 months.

As at March 31, 2011, the Corporation has outstanding balance of 570,000 restricted share units.

Restricted Shares Unit Outstanding	For the nine months ended March 31, 2011		Year ended June 30, 2010	
	Number of units	Grant Price	Number of units	Grant Price
Opening	360,000	\$ 0.75	-	\$ -
Granted	300,000	\$ 1.68	360,000	\$ 0.75
Converted	(90,000)	\$ 0.75	-	\$ -
Ending	570,000		360,000	\$ 0.75

Notes to the Consolidated Financial Statements

For the three and nine months ended March 31, 2011 and March 31, 2010

(Unless otherwise stated, amounts presented are in thousands United States dollars currency) (unaudited)

10. CONTRIBUTED SURPLUS

The following table reconciles the Corporation's contributed surplus:

	Nine months ended March 31, 2011	Year ended June 30, 2010
	\$	\$
Contributed surplus, opening	12,088	8,721
Impact of foreign exchange	(168)	-
Fair value of restricted share units	136	-
Stock compensation expense	8,247	3,453
Stock options exercised (note 9f)	(1,849)	(86)
Contributed surplus, ending	18,454	12,088

11. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Classifications of financial instruments remain consistent at March 31, 2011 with those at June 30, 2010. The carrying value and respective fair value of financial assets and liabilities are summarized as follows:

	As at March 31, 2011		As at June 30, 2010	
	Carrying Value	Fair Value	Carrying Value	Fair Value
	\$	\$	\$	\$
Assets held for trading				
Cash and cash equivalent, restricted cash, and cash reserved for asset retirement	110,019	110,019	57,529	57,529
Commodity contracts	-	-	227	227
Loans and receivables				
Accounts, promissory note and cash call receivable	36,285	36,285	7,661	7,661
Liabilities held for trading				
Commodity contracts	4,195	4,195	-	-
Other liabilities				
Accounts, interest and cash calls payable	46,883	46,883	32,587	32,587
12% Convertible debentures ⁽¹⁾	358	286	1,145	1,145
8% Convertible debentures	17,068	17,068	-	-
Debt facilities and operating line of credit	616	616	322	322

⁽¹⁾ Fair value of 12% Convertible debentures were recalculated using an 8% interest rate as at March 31, 2011.

The Corporation categorizes its financial instruments carried at fair value into one of three different levels depending on the observability of the inputs employed in the measurement. At March 31, 2011, the Corporation valued cash and cash equivalents and restricted cash using Level 1 inputs and valued all derivative financial instruments using the level 2 inputs. At March 31, 2011, the Corporation did not have any assets and liabilities measured at fair value using Level 3 inputs.

Notes to the Consolidated Financial Statements

For the three and nine months ended March 31, 2011 and March 31, 2010

(Unless otherwise stated, amounts presented are in thousands United States dollars currency) (unaudited)

The Corporation classifies the fair value of these transactions according to the following hierarchy based on the amount of observable inputs used to value the instrument:

Level 1 – Quoted prices are available in active markets for identical assets or liabilities as of the reporting date. Active markets are those in which transactions occur in sufficient frequency and volume to provide pricing information on an ongoing basis.

Level 2 – Pricing inputs are other than quoted prices in active markets included in Level 1. Prices in Level 2 are either directly or indirectly observable as of the reporting date. Level 2 valuations are based on inputs, including quoted forward prices for commodities, time value and volatility factors, which can be substantially observed or corroborated in the marketplace.

Level 3 – Valuations in this level are those with inputs for the asset or liability that are not based on observable market data.

Credit risk

Credit risk reflects the risk of loss if counterparties do not fulfill their contractual obligations. The majority of the Corporation's accounts receivable balances relate to oil and gas sales. The Corporation's policy is to enter into agreements with customers that are well established and well-financed entities in the oil and gas industry such that the level of risk is mitigated. To date, the Corporation has not experienced any material credit loss in the collection of accounts receivable. All Brazilian oil sales made through the Joint Venture are to a single customer who is the government energy company (Petrobras), while in Colombia the majority of oil sales revenue and tariff oil revenue comes from three customers of which two are also government entities (Petrobras Colombia and Ecopetrol) and Hocol controlled by Ecopetrol. During the quarter ended December 31, 2010 the Corporation also entered into sales agreements with Meta Petroleum Corp ("Meta Petroleum"), a subsidiary of Pacific Rubiales Energy; C.I. Gravinal S.A. ("Gravinal"); Comergroup S.A. ("Comergroup") and Gasmocam S.A. ("Gasmocam").

As at March 31, 2011, approximately 63%, 19%, 15%, 2% and 1% of the outstanding receivables balances are owed by Hocol, Ecopetrol, Meta Petroleum, Petrobras and others customers, respectively. The Corporation's net share of the outstanding accounts receivable from these customers totalled \$28,586 at March 31, 2011 (June 30, 2010 - \$5,181).

Details of the Corporation's accounts receivable balances are as follows:

	As at	As at
	March 31, 2011	June 30, 2010
	\$	\$
<i>Trade and other receivable aging balances</i>		
Current < 30 days	28,586	5,181
30 to 60 days	-	-
60 to 90 days	-	-
Over 90 days	3,465	1,040
Total	32,051	6,221

The Corporation's aged receivables primarily relate to accounts receivable balances from customers and tax receivable balances that can be applied to future required tax payments. No provisions are required to be recorded for these balances.

The Corporation has a cash call receivable of \$355 (June 30, 2010 - \$700) relating to its joint venture operations in Colombia at March 31, 2011 and \$2,458 (June 30, 2010 - \$345) relating to its joint venture in Guyana and \$1,421 (June 30, 2010 - payable of \$395) relating to its joint venture in Brazil.

Notes to the Consolidated Financial Statements

For the three and nine months ended March 31, 2011 and March 31, 2010

(Unless otherwise stated, amounts presented are in thousands United States dollars currency) (unaudited)

In addition, the Corporation has a joint venture payable of \$13 relating to its joint venture in Ireland (June 30, 2010 - \$127) and \$555 (June 30, 2010 - \$422) relating to its joint venture in Colombia.

Market risk

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

a) Commodity price risk

Commodity price risk is the risk that the fair value of the future cash flows will fluctuate as a result of changes in commodity prices. Significant changes in commodity prices can also materially impact the Corporation's borrowing base under its reserve based credit facilities. Commodity prices are significantly impacted by world economic supply and demand of oil and natural gas. The Corporation has the following financial WTI oil collars outstanding on March 31, 2011 under the following terms:

Period	Volume	Type	Price Range
Jan 2010 – Aug 2011	114 bbls/day	Financial WTI Oil Collar	US\$55.00 - US\$80.25
May 2010 – Aug 2011	500 bbls/day	Financial WTI Oil Collar	US\$70.00 - US\$100.45
Nov 2010 – Oct 2011	500 bbls/day	Financial WTI Oil Collar	US\$70.00 - US\$100.00
Dec 2010 – Nov 2011	500 bbls/day	Financial WTI Oil Collar	US\$70.00 - US\$100.00

For the three and nine months ended March 31, 2011, the Corporation recognized a realized derivative loss of \$298 and \$323 (Three and nine months ended March 31, 2010 – \$Nil) and an unrealized derivative loss of \$2,426 and \$4,355 (Three and nine months ended March 31, 2010 – net gain of \$82 and loss of \$148) relating to its oil collar financial derivatives. The total fair value of these risk management assets at March 31, 2011 was liability of \$4,195 (June 30, 2010 – asset of \$227). For the three and nine months ended March 31, 2011, if oil prices had been \$1.00 higher/lower, with all other variables held constant, the change in fair value would have resulted in a decrease/increase in earnings of approximately \$206 and \$401.

b) Foreign currency risk

Currency risk is the risk that the value of financial instruments will fluctuate due to changes in foreign exchange rates. Currency risk arises when future commercial transactions and recognized assets and liabilities are denominated in a currency that is not the Corporation's reporting currency. The Corporation's management monitors the exchange rate fluctuations on a regular basis and acts accordingly. The Corporation operates in several geographic areas and is exposed to foreign currency risk primarily on the Colombia Pesos to United States dollar exchange rate. The Corporation does not use currency derivative instruments to manage the Corporation's exposure to foreign currency fluctuations. As March 31, 2011, the Corporation had the following balances held deposits and account receivable and account payable in foreign currency:

Notes to the Consolidated Financial Statements

For the three and nine months ended March 31, 2011 and March 31, 2010

(Unless otherwise stated, amounts presented are in thousands United States dollars currency) (unaudited)

	As at March 31, 2011		As at June 30, 2010	
Deposit in Brazilian reais	\$1,379	BRL \$2,343	\$202	BRL \$363
Deposit in Colombian pesos	\$1,724	COP\$13,587,925	\$7,465	COP\$ 14.3 billion
Deposit in Canadian dollars	\$1,047	C\$1,080	\$42,207	C\$44,934
Deposit in United States dollars	\$99,886		\$6,366	-
	\$104,036		\$56,240	
Account receivable in Brazilian reais	\$402	BRL \$723	\$549	BRL \$987
Account receivable in Colombian pesos	\$27,171	COP\$52,005,315	\$2,975	COP\$ 5.7 billion
Account receivable in Canadian dollars	\$69	C\$73	\$58	C\$62
Account receivable in United States dollars	\$4,409		\$2,639	-
	\$32,051		\$6,221	
Account payable in Brazilian reais	\$395	BRL \$670	\$331	BRL \$593
Account payable in Colombian pesos	\$40,610	COP\$77,727,513	\$9,175	COP\$ 17.5 billion
Account payable in Canadian dollars	\$2,152	\$2,220	\$4,137	C\$4,404
Account payable in United States dollars	\$3,158	-	\$18,000	-
	\$46,315		\$31,643	

For the three and nine months ended March 31, 2011, the Corporation had a foreign exchange loss of \$1,918 and gain \$745 respectively (three and nine months ended March 31, 2010 – loss of \$78 and gain \$2,090) predominantly due to fluctuations in the Canadian dollar compared to the US dollar in which the revenue and expenses are incurred in the Colombian subsidiaries and conversion from Brazilian operations to US dollars using the temporal method. For the three months ended March 31, 2011, a 1% increase/decrease in the US dollar vis-à-vis the Canadian dollar, Brazilian real and Colombian pesos is estimated to increase/decrease the earnings of the Corporation by \$1,024, \$35, \$1,815, respectively. For nine months ended March 31, 2011, a 1% increase/decrease in the US dollar vis-à-vis the Canadian dollar, Brazilian real and Colombian pesos is estimated to increase/decrease the earnings of the Corporation by and \$1,265, \$114, \$3,751, respectively.

Country currency	Canada	Colombia	Brazil
As at March 31, 2011 rate per USD	1.0314	0.0005353	0.5885
As at June 30, 2010 rate per USD	0.9429	0.000522	0.5563

c) Interest rate risk

Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in prevailing market interest rates. The Corporation was exposed to interest rate risk on certain variable interest rate COP denominated debt instruments which were based upon an underlying DTF interest rate (note 4). The remainder of the Corporation's financial assets and liabilities are not exposed to interest rate risk. During the three and nine months ended March 31, 2011, the Corporation did not enter into any interest rate swaps or other financial arrangements that mitigate the Corporation's exposure to interest rate fluctuations. The effect of a 1% increase/decrease in DTF interest rates is estimated to have \$2 and \$5 decrease/increase in

Notes to the Consolidated Financial Statements

For the three and nine months ended March 31, 2011 and March 31, 2010

(Unless otherwise stated, amounts presented are in thousands United States dollars currency) (unaudited)

earnings for the three and nine months ended March 31, 2011.

d) Liquidity risk

Liquidity risk is the risk that the Corporation will not be able to meet its financial obligations as they become due and describes the Corporation's ability to access cash. The Corporation requires sufficient cash resources in order to finance operations, fund capital expenditures, and to repay debt and other liabilities of the Corporation as they come due.

The following table outlines the contractual maturities of the Corporation's financial liabilities and main contractual commitments as of March 31, 2011:

	Recognized on Financial Statements	Payments Due By Period ^{1,2}				Total
		Less than 1 year	1 -2 years	2-5 years	After 5 years	
Accounts payable and accrued liabilities	Yes - Liability	23,299	-	-	-	23,299
Payable on overlifted volumes	Yes - Liability	23,016	-	-	-	23,016
Operating line of credit	Yes - Liability	616	-	-	-	616
Cash call payable	Yes - Liability	568	-	-	-	568
12% Convertible debentures	Yes - Liability	398	-	-	-	398
8% Convertible debentures ⁵	Yes - Liability	1,847	4,926	33,248	-	40,021
Work program commitments	No	29,075	-	-	-	29,075
Office and equipment leases	No	395	1,054	200	-	1,649
Round 10 Colombia work program commitments ³	No	19,298	7,251	7,251	-	33,800
Other minimum exploration commitments ⁴	No	24,603	-	-	-	24,603
Total		123,115	13,231	40,699	-	177,045

¹ Payments exclude ongoing operating costs.

² Payments denominated in foreign currencies have been translated at the respective March 31, 2011 exchange rate.

³ In June 2010, the Corporation secured two Exploration and Production Contracts ("E&P Contracts") in the Upper Magdalena Basin of Colombia. Each block has a six year exploration term divided into two 36 month exploration phases.

⁴ Minimum work commitments reflect financial liability if not satisfied through the completion of exploration work in Colombia (Cedrela, Tamarin, Pacarana and Sangretoro).

⁵ Includes cash interest payment of approximately \$9.2 million.

12. CAPITAL DISCLOSURES

The Corporation's objectives when managing capital are to ensure the Corporation will have sufficient financial capacity, liquidity, and flexibility to fund its operations, growth, and ongoing exploration and development commitment activities on its oil and gas assets. The Corporation is dependent upon funding these activities through a combination of debt and equity financings. Due to operational shortfalls and long lead cycles of some of its exploration and developments activities, the Corporation's capital requirements currently exceed its operational cash flow generated. As such, the Corporation is dependent upon existing cash resources and financing in order to maintain its financial flexibility and liquidity.

The Corporation regularly monitors its capital structure and as necessary adjusts to changing economic circumstances and the underlying risk characteristics of its assets in order to meet current and upcoming obligations and investments by the Corporation. The Corporation frequently reviews alternate financing options and arrangements to meet its current and upcoming commitments and obligations.

Notes to the Consolidated Financial Statements

For the three and nine months ended March 31, 2011 and March 31, 2010

(Unless otherwise stated, amounts presented are in thousands United States dollars currency) (unaudited)

Current plans include:

- For Colombia, development of the Ombu and Rancho Hermoso fields, plus exploration activities, the Corporation plans to use funds on hand, funds raised through credit facilities and funds raised through the equity financing that closed during the period ended March 31, 2011.
- For Guyana, the Corporation plans to use the funds on hand plus funds raised in the equity financing that closed during the period ended March 31, 2011.
- For Brazil, the Corporation is seeking a farmout arrangement as well as utilizing funds on hand plus funds from the equity financing that closed during the period ended March 31, 2011.

The Corporation defines and computes its capital employed as follows:

	As at March 31, 2011 \$	As at June 30, 2010 \$
Shareholders' equity	188,551	113,653
Line of credit facilities	616	322
12% Convertible debentures	358	1,145
8% Convertible debentures	17,068	-
Cash and cash equivalents	(104,036)	(56,240)
	102,557	58,880

The Corporation's financial objectives and strategies as described above have remained substantially consistent with previous periods. The objectives and strategies of the Corporation are reviewed on a regular basis.

13. SEGMENTED INFORMATION AND INTEREST IN JOINT VENTURE

The Corporation's reportable operating segments, as determined by management, are based on the core strategic business operations. Details of the reporting segments are as follows:

- Colombia includes the Corporation's exploration for, and development and production of, oil and natural gas through Rancho Hermoso, Entrerrios and the Corporation's interest in the Capella conventional heavy oil project (Ombu);
- Brazil includes the Corporation's exploration for, and development and production of, oil and natural gas in the Recôncavo, Sergipe, and Tucano basins of Brazil. Substantially all of the operating activities of the Brazil Exploration and Production ("E&P") segment are carried out through joint ventures;
- Guyana includes the Corporation's 65% net working interest in exploration for, and development and production of, oil and natural gas in the Takutu Basin in Guyana; and
- The Corporate segment provides management and administrative services to all of its subsidiaries and their respective operations and includes non-core operations.

Notes to the Consolidated Financial Statements

For the three and nine months ended March 31, 2011 and March 31, 2010

(Unless otherwise stated, amounts presented are in thousands United States dollars currency) (unaudited)

	Three months ended March 31, 2011				Total \$
	E&P Colombia	E&P Brazil	E&P Guyana	E&P Other, Corporate & Eliminations	
	\$	\$	\$	\$	
REVENUE					
Petroleum and natural gas sales	23,590	1,263	-	-	24,853
Sales tax	-	(50)	-	-	(50)
Royalties	(1,269)	(82)	-	-	(1,351)
Petroleum and natural gas, net	22,321	1,131	-	-	23,452
Tariff Revenue	8,677	-	-	-	8,677
Interest and other	214	-	-	(18)	196
Total Revenues	31,212	1,131	-	(18)	32,325
EXPENSES					
Operating expenses	9,812	570	-	(31)	10,351
General and administrative	502	467	-	1,850	2,819
Interest and financial expenses	65	-	-	822	887
Foreign exchange loss, net	167	106	-	1,645	1,918
Financial derivative loss (gain), net	2,928	-	-	(204)	2,724
Stock compensation expense	-	-	-	3,336	3,336
Depletion, depreciation and accretion	9,816	368	-	468	10,652
Unrealized loss on overlifting	2,137	-	-	-	2,137
Total Expenses	25,427	1,511	-	7,886	34,824
EARNINGS (LOSS)					
Income (loss) before income taxes	5,785	(380)	-	(7,904)	(2,499)
Current income tax expense	1,147	-	-	-	1,147
Future income tax recovery	(303)	-	-	-	(303)
Net income (loss)	4,941	(380)	-	(7,904)	(3,343)
Total assets	157,615	10,568	19,882	81,433	269,498
Capital expenditures	15,820	187	4,517	141	20,665

Notes to the Consolidated Financial Statements

For the three and nine months ended March 31, 2011 and March 31, 2010

(Unless otherwise stated, amounts presented are in thousands United States dollars currency) (unaudited)

	Nine months ended March 31, 2011				Total \$
	E&P Colombia \$	E&P Brazil \$	E&P Guyana \$	E&P Other, Corporate & Eliminations \$	
REVENUE					
Petroleum and natural gas sales	55,029	3,264	-	-	58,293
Sales tax	-	(131)	-	-	(131)
Royalties	(3,614)	(208)	-	-	(3,822)
Petroleum and natural gas, net	51,415	2,925	-	-	54,340
Tariff Revenue	11,468	-	-	-	11,468
Interest and other	642	7	-	45	694
Total Revenues	63,525	2,932	-	45	66,502
EXPENSES					
Operating expenses	22,477	1,653	-	-	24,130
General and administrative	3,050	1,469	-	6,410	10,929
Interest and financial expenses	88	-	-	3,504	3,592
Foreign exchange (gain) loss, net	(1,929)	(232)	-	1,416	(745)
Financial derivative loss, net	2,928	-	-	1,750	4,678
Stock compensation expense	-	-	-	8,247	8,247
Depletion, depreciation and accretion	19,210	2,514	-	751	22,475
Unrealized loss on overlofting	2,137	-	-	-	2,137
Impairments	-	9,673	-	-	9,673
Total Expenses	47,961	15,077	-	22,078	85,116
EARNINGS (LOSS)					
Income (loss) before income taxes	15,564	(12,145)	-	(22,033)	(18,614)
Current income tax expense	4,252	-	-	-	4,252
Future income tax recovery	(3,086)	-	-	-	(3,086)
Net income (loss)	14,398	(12,145)	-	(22,033)	(19,780)
Total assets	157,615	10,568	19,882	81,433	269,498
Capital expenditures	41,412	912	8,793	192	51,309

Notes to the Consolidated Financial Statements

For the three and nine months ended March 31, 2011 and March 31, 2010

(Unless otherwise stated, amounts presented are in thousands United States dollars currency) (unaudited)

	Three months months ended March 31, 2010				
	E&P Colombia	E&P Brazil	E&P Guyana	Corporate & Eliminations	Total
	\$	\$	\$	\$	\$
REVENUE					
Petroleum and natural gas sales	4,976	1,414	-	-	6,390
Sales tax	-	(83)	-	(906)	(989)
Royalties	(348)	(61)	-	-	(409)
Petroleum and natural gas, net	4,628	1,270	-	(906)	4,992
					-
Tariff Revenue	1,607	-	-	-	1,607
Interest and other	164	-	-	1	165
Total Revenues	6,399	1,270	-	(905)	6,764
EXPENSES					
Operating expenses	3,290	494	-	5	3,789
General and administrative	610	483	-	1,653	2,746
Interest and financial expenses	26	231	-	439	696
Foreign exchange (gain) loss, net	-	(90)	-	168	78
Realized loss on financial derivatives	-	-	-	(82)	(82)
Stock compensation expense	-	-	-	1,431	1,431
Depletion, depreciation and accretion	3,085	642	-	(26)	3,701
Total Expenses	7,011	1,760	-	3,588	12,359
EARNINGS (LOSS)					
Income (Loss) before income taxes	(610)	(489)	-	(4,496)	(5,595)
Current income tax	406	-	-	-	406
Future income tax	(871)	-	-	-	(871)
Net Loss	(145)	(489)	-	(4,496)	(5,130)
Total assets	32,437	30,707	5,739	27,183	96,066
Capital expenditures	2,042	1,623	488	-	4,153

Notes to the Consolidated Financial Statements

For the three and nine months ended March 31, 2011 and March 31, 2010

(Unless otherwise stated, amounts presented are in thousands United States dollars currency) (unaudited)

	Nine Months ended March 31, 2010				
	E&P Colombia	E&P Brazil	E&P Guyana	Corporate & Eliminations	Total
	\$	\$	\$	\$	\$
REVENUE					
Petroleum and natural gas sales	9,612	2,711	-	-	12,323
Sales tax	-	(130)	-	(1,008)	(1,138)
Royalties	(656)	(195)	-	-	(851)
Petroleum and natural gas, net	8,956	2,386	-	(1,008)	10,334
Tariff Revenue	4,452	-	-	-	4,452
Interest and other	1,034	-	-	25	1,059
Total Revenues	14,442	2,386	-	(983)	15,845
EXPENSES					
Operating expenses	9,042	993	-	10	10,045
General and administrative	1,421	1,390	-	3,481	6,292
Interest and financial expenses	301	703	-	1,223	2,227
Foreign exchange gain, net	-	(41)	-	(2,049)	(2,090)
Financial derivative loss, net	-	-	-	148	148
Stock compensation expense	-	-	-	2,369	2,369
Depletion, depreciation and accretion	6,370	1,530	-	65	7,965
Impairment on long-term assets	-	-	-	75	75
Total Expenses	17,134	4,575	-	5,322	27,031
EARNINGS (LOSS)					
Income (loss) before income taxes	(2,692)	(2,188)	-	(6,306)	(11,186)
Current income tax expense	1,251	-	-	-	1,251
Future income tax recovery	(2,565)	-	-	-	(2,565)
Net Loss	(1,378)	(2,188)	-	(6,306)	(9,872)
Total assets	32,437	30,707	5,739	27,183	96,066
Capital expenditures	11,529	2,175	1,961	77	15,742

Notes to the Consolidated Financial Statements

For the three and nine months ended March 31, 2011 and March 31, 2010

(Unless otherwise stated, amounts presented are in thousands United States dollars currency) (unaudited)

Included in the Corporation's consolidated balance sheets, and consolidated statements of loss and comprehensive loss and cash flows for the 47.5% Brazilian Joint Venture are the following balances:

	As at March 31, 2011 \$	As at June 30, 2010 \$
Assets		
Current	1,145	1,132
Long-term	14,120	14,642
Liabilities		
Current	176	166
Long-term	-	-

	Three months ended March 31		Nine months ended March 31	
	2011 \$	2010 \$	2011 \$	2010 \$
Revenues	1,132	1,270	2,933	2,385
Expenses	1,223	1,626	5,485	4,020
Net loss	(91)	(356)	(2,552)	(1,635)
Cash Flows				
Used in Operating	(1,033)	(269)	(3,099)	(816)
Used in Investing	(1,035)	(270)	(3,105)	(923)
Used in Financing	(7)	(2)	(21)	(37)
Net Cash Flows	(2,075)	(541)	(6,225)	(1,776)

Geographic information related to the Corporation's activities:

	Revenues		Revenues		Property, plant and equipment	
	Three months ended March 31		Nine months ended March 31		As at	
	2011 \$	2010 \$	2011 \$	2010 \$	March 31, 2011 \$	June 30, 2010 \$
Brazil	1,131	1,270	2,932	2,386	7,311	18,105
Colombia	31,212	6,399	63,525	14,442	77,586	52,389
Guyana	-	-	-	-	17,425	7,151
Canada & Other	(18)	(905)	45	(983)	14,233	12,807
	32,325	6,764	66,502	15,845	116,555	90,452

Notes to the Consolidated Financial Statements

For the three and nine months ended March 31, 2011 and March 31, 2010

(Unless otherwise stated, amounts presented are in thousands United States dollars currency) (unaudited)

14. SUPPLEMENTAL INFORMATION

The changes in non-cash working capital are as follows:

	Three months ended March 31,		Nine months ended March 31,	
	2011	2010	2011	2010
	\$	\$	\$	\$
Operating Activities				
Decrease (increase) in current assets				
Accounts receivable	(23,533)	(1,951)	(25,830)	(725)
Prepaid expenses and deposits	(1,919)	(812)	(2,072)	(832)
Increase (decrease) in current liabilities				
Accounts payable and accrued liabilities	15,607	(347)	24,504	358
Income taxes	(1,987)	(49)	(894)	(232)
	(11,832)	(3,159)	(4,292)	(1,431)
Investing activities				
Decrease (increase) in current assets				
Cash call and promissory notes receivable ⁽¹⁾	(600)	(2,264)	(2,794)	(2,620)
Increase (decrease) in current liabilities				
Accounts payable and accrued liabilities	5,755	(1,038)	7,792	1,073
	5,155	(3,302)	4,998	(1,547)

⁽¹⁾ Includes long and short term cash calls

As at March 31, 2011, \$67,475 (June 30, 2010 - \$20,968) of the cash and cash equivalents balance was held in short-term investments, the remainder of \$36,561 (June 30, 2010 - \$35,272) was held in cash, totalling \$104,036 (June 30, 2010 - \$56,240). All investments had original maturity dates of less than 90 days and the investments were convertible into cash at any time by the Corporation. Details of the cash balances and the interest rates earned on those balances as at March 31, 2011 and June 30, 2010 are as follows:

As at March 31, 2011		As at June 30, 2010	
Balance	Average Interest Rate	Balance	Average Interest Rate
C\$2,002	0.02 - 0.27%	C\$9,712	0.02 - 0.27%
US\$1,996		US\$9,123	
US\$59,164	0.02 - 0.27%	US\$6,037	0.02 - 0.27%
US\$59,164		US\$6,037	
COP\$11,796,420	10.27%	COP\$11,130,526	10.27%
US\$6,315		US\$5,808	
BRL\$0	N/A	BRL\$0	N/A
US\$0		US\$0	
US\$67,475		US\$20,968	

Notes to the Consolidated Financial Statements

For the three and nine months ended March 31, 2011 and March 31, 2010

(Unless otherwise stated, amounts presented are in thousands United States dollars currency) (unaudited)

15. COMMITMENTS AND CONTINGENCIES

Minimum exploration program (Brazil)

As at March 31, 2011, the Corporation had minimum exploration program (“MEP”) work unit commitments to complete negotiated exploration work on its onshore blocks awarded by the Agência Nacional do Petróleo, Gás Natural e Biocombustível (“ANP”), Brazil’s National Petroleum Agency. MEP work units are satisfied through completion of exploration wells, seismic programs, and other exploration survey methods all of which have prescribed work units for completion. Therefore, although actual dollars spent on projects do not directly correlate to reducing the MEP work units, the financial guarantees related to non-performance are shown in the table below. The commitment is reduced as work is performed.

Bid Round	Basin/Block	Commitment Date	Extension	Gross Remaining MEP		Net Remaining MEP		Net Financial Guarantee ¹
				Work Units	Gross Financial Guarantee	Work Units	Guarantee ¹	
						\$1,766		\$662
9	Recôncavo - Block 170 ²	June 5, 2010	(special extension)	1,000	BRL \$3,000		375	BRL \$1,125
						\$1,059		\$212
9	Recôncavo - Block 169	March 12, 2011	December 2, 2011	600	BRL \$1,800		120	BRL \$360

¹ Net financial guarantee based on currently Canacol’s net working interest. Canacol is in the process of acquiring the operator’s interest and operatorship in the REC-T-170 contract, which upon completion will give the Corporation a 75% operated working interest and operatorship contract.

² ANP has granted an special extension to the Corporation on the agreement BT-REC-60, Block-T-170. Block 170 expires six months after permitting approval is received from the landowner to access the land.

The round 9 (Reconcavo Basin) commitments are planned to be satisfied through a combination of the execution of an exploration drilling program and through financial settlement of MEP work units.

Work program commitments (Colombia)

Round 10

The Corporation has secured two Exploration and Production Contracts (“E&P Contracts”) in the Upper Magdalena Basin of Colombia via its wholly owned subsidiary Rancho Hermoso S.A.. Canacol secured 100% operated working interest in each of COR-11 and COR 39 E&P contracts which were awarded by the Agencia Nacional de Hidrocarburos (“ ANH”). Each of the two blocks has a six year exploration term divided into two 36 month exploration phases. The phase 1 work program commitments associated with each of blocks are summarized below:

Bid Round	Basin	Commitment Date	Block	Working Interest	Work program commitments	Financial Guarantee ¹
10	Upper Magdalena Basin	July 1, 2013	COR-11	100%	155 kms of 2D seismic and 1 exploration well	\$ 12,200
10	Upper Magdalena Basin	July 1, 2013	COR-39	100%	90 kms of 2D seismic and 2 exploration well	\$ 15,600

¹ The Corporation will place a total of \$13.3M in letters of credit with ANH.

The Corporation signed three agreements with the ANH in February 2011 (Sangretoro, COR 11 and COR 39). The Sangretoro, E&P contract is located in the Putumayo – Caguan Basin of southern Colombia, and was previously part of the Pacarana Technical Evaluation Area (“TEA”) that was award in 2009 to the Corporation. The Phase 1 commitment associated with the Sangretoro block in summarized below:

Notes to the Consolidated Financial Statements

For the three and nine months ended March 31, 2011 and March 31, 2010

(Unless otherwise stated, amounts presented are in thousands United States dollars currency) (unaudited)

Phase	Basin	Commitment Date	Working Interest	Work program commitments	Financial Guarante
1	Putumayo-Caguan Basin	August 31, 2012	100%	300 kms of 2D seismic	\$ 6,000

Cedrela E&P Contract

On May 2010, the Corporation was awarded the Cedrela Exploration and Production Contract (“Cedrela E&P Contract”) by the ANH of Colombia. The Cedrela E&P contract is located in the Putumayo-Caguan Basin, and is approximately 50 kilometres directly southwest of the Ombu E&P contract which contains Capella heavy oil discovery. The Corporation has a 100% working interest in the Cedrela E&P Contract, which is 129,418 hectares (319,799 acres) in size. The terms of the 6 year contract are as follows:

Phase	Basin	Commitment Date	Working Interest	Work program commitments	Financial Guarantee
1	Putumayo-Caguan Basin	December 31, 2011	100%	250 kms of 2D seismic	\$ 5,400
2	Putumayo-Caguan Basin	June 30, 2013	100%	Drill 1 exploration well	\$2,000
3	Putumayo-Caguan Basin	December 31, 2014	100%	60 kms of 3D seismic	\$3,000
4	Putumayo-Caguan Basin	June 30, 2016	100%	Drill 1 exploration well	\$2,000

Based upon the results of the Phase 1 exploration activities, the Corporation has the option to proceed to the Phase 2 exploration period and associated activities or relinquish the contract. This option also applies phase 3 and 4.

Other Commitments

In Guyana, the Corporation has work program commitments totalling approximately \$8,500 due within a year or less.

In addition, the Corporation has commitments for leases and its office premises. As of March 31, 2011, the payments required in each of the next five calendar years on these lease are as follows:

<u>Leases</u>	<u>\$</u>
2011	395
2012	527
2013	527
2014	108
2015	92

The Corporation is currently disputing certain amounts claimed by a joint venture operator. As adequate supporting financial documents have not been provided by the operator, the Corporation continues to record revenues, expenses and any amounts receivable from or payable to the operator using the Corporation’s best estimates as of and for the three and nine months ended March 31, 2011. Any adjustments required upon final settlement in the joint venture operation will be recorded in the period as amounts owing to or receivable from the operator are settled. As part of the negotiation for disposition of non-core, non-operated producing properties in Brazil, these issues will be resolved.

Notes to the Consolidated Financial Statements

For the three and nine months ended March 31, 2011 and March 31, 2010

*(Unless otherwise stated, amounts presented are in thousands United States dollars
currency) (unaudited)*

16. SUBSEQUENT EVENTS

Subsequent to March 31, 2011, 334,900 shares were issued on exercise of options, 5,327,500 shares were issued on exercise of warrants and 20,050 common shares were issued to consultants for services.

On May 3, 2011, the Corporation's common shares and convertible debentures commenced trading on the Toronto Stock Exchange ("TSX") under symbols "CNE" and "CNE.DB", respectively.

Corporate Information

Management Team

Charle Gamba – President & Chief Executive Officer

Mark Holliday - Chief Operating Officer

Mark Teare – Vice President Exploration

Brian Hearst – Chief Financial Officer

Kevin Flick – Vice President of Capital Markets and Investor Relations

Luis Baena – Vice President of Business Development, Colombia

Board of Directors

Michael Hibberd, Chairman

Luis Baena

Alvaro Barrera

Jason Bednar

Charle Gamba

Stuart Hensman

David Winter

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Bankers

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HSBC Bank Brasil - Rio de Janeiro, Brazil

Citibank, Bogota, Colombia

Independent Reserve Engineers

DeGolyer and MacNaughton Canada Limited

Legal Counsel

Davis LLP - Canada

Schmidt, Valois, Miranda, Ferreira & Agel – Brazil

Salazar Asociados Abogados - Colombia

Stock Exchange Listing

Common Shares:

Toronto Stock Exchange : CNE

BVC Colombia: CNE.C

8% Debentures:

Toronto Stock Exchange : CNE.DB

Transfer Agent & Registrar

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