

MANAGEMENT'S DISCUSSION & ANALYSIS

FORWARD LOOKING STATEMENTS

THIS MD&A OF FINANCIAL CONDITIONS AND RESULTS OF OPERATIONS FOR THE NINE-MONTHS ENDED 30 SEPTEMBER 2012 SHOULD BE READ IN CONJUNCTION WITH THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND NINE-MONTH PERIODS ENDED SEPTEMBER 30, 2012 AND NOTES THERETO AND THE AUDITED CONSOLIDATED FINANCIAL STATEMENTS AND NOTES THERETO AS AT AND FOR THE YEAR ENDED 31 DECEMBER 2011. THIS MD&A IS BASED ON THE INFORMATION AVAILABLE ON 29 NOVEMBER 2012.

CERTAIN STATEMENTS IN THIS MD&A INCLUDING (I) STATEMENTS THAT MAY CONTAIN WORDS SUCH AS "ANTICIPATE", "COULD", "EXPECT", "SEEK", "MAY", "INTEND", "WILL", "BELIEVE", "SHOULD", "PROJECT", "FORECAST", "PLAN" AND SIMILAR EXPRESSIONS, INCLUDING THE NEGATIVES THEREOF; (II) STATEMENTS THAT ARE BASED ON CURRENT EXPECTATIONS AND ESTIMATES ABOUT THE MARKETS IN WHICH ORCA EXPLORATION OPERATES AND (III) STATEMENTS OF BELIEF, INTENTIONS AND EXPECTATIONS ABOUT DEVELOPMENTS, RESULTS AND EVENTS THAT WILL OR MAY OCCUR IN THE FUTURE, CONSTITUTE "FORWARD-LOOKING STATEMENTS" AND ARE BASED ON CERTAIN ASSUMPTIONS AND ANALYSIS MADE BY ORCA EXPLORATION. FORWARD-LOOKING STATEMENTS IN THIS MD&A INCLUDE, BUT ARE NOT LIMITED TO, STATEMENTS WITH RESPECT TO FUTURE CAPITAL EXPENDITURES, INCLUDING THE AMOUNT, NATURE AND TIMING THEREOF, NATURAL GAS PRICES AND DEMAND.

SUCH FORWARD-LOOKING STATEMENTS ARE SUBJECT TO IMPORTANT RISKS AND UNCERTAINTIES, WHICH ARE DIFFICULT TO PREDICT AND THAT MAY AFFECT ORCA EXPLORATION'S OPERATIONS, INCLUDING, BUT NOT LIMITED TO: THE IMPACT OF GENERAL WORLD ECONOMIC CONDITIONS AND SPECIFICALLY IN TANZANIA, ITALY AND CANADA; INDUSTRY CONDITIONS, INCLUDING THE ADOPTION OF NATURAL GAS POLICES AND LAWS, NEW ENVIRONMENTAL, SAFETY AND OTHER LAWS AND REGULATIONS AND CHANGES IN HOW THEY ARE INTERPRETED AND ENFORCED; SANCTITY OF CONTRACT; VOLATILITY OF OIL AND NATURAL GAS PRICES; OIL AND NATURAL GAS PRODUCT SUPPLY AND DEMAND, RIG AVAILABILITY; RISKS INHERENT IN ORCA EXPLORATION'S ABILITY TO GENERATE SUFFICIENT CASH FLOW FROM OPERATIONS, THIRD PARTY FINANCE OR ASSETS SALES TO MEET ITS CURRENT AND FUTURE OBLIGATIONS; INCREASED COMPETITION; THE FLUCTUATION IN FOREIGN EXCHANGE OR INTEREST RATES; STOCK MARKET VOLATILITY; COST POOL AUDITS AND OTHER FACTORS, MANY OF WHICH ARE BEYOND THE CONTROL OF ORCA EXPLORATION.

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NON-GAAP MEASURES

THE COMPANY EVALUATES ITS PERFORMANCE USING A NUMBER OF NON-GAAP (GENERALLY ACCEPTED ACCOUNTING PRINCIPLES) MEASURES. THESE NON-GAAP MEASURES ARE NOT STANDARDISED AND THEREFORE MAY NOT BE COMPARABLE TO SIMILAR MEASUREMENTS OF OTHER ENTITIES.

- **FUNDS FLOW FROM OPERATING ACTIVITIES** IS A TERM THAT REPRESENTS CASH FLOW FROM OPERATIONS BEFORE WORKING CAPITAL ADJUSTMENTS. IT IS A KEY MEASURE AS IT DEMONSTRATES THE COMPANY'S ABILITY TO GENERATE CASH NECESSARY TO ACHIEVE GROWTH THROUGH CAPITAL INVESTMENTS.
- **OPERATING NETBACKS** REPRESENT THE PROFIT MARGIN ASSOCIATED WITH THE PRODUCTION AND SALE OF ADDITIONAL GAS AND IS CALCULATED AS REVENUES LESS PROCESSING AND TRANSPORTATION TARIFFS, GOVERNMENT PARASTATAL'S REVENUE SHARE, OPERATING AND DISTRIBUTION COSTS FOR ONE THOUSAND STANDARD CUBIC FEET OF ADDITIONAL GAS. THIS IS A KEY MEASURE AS IT DEMONSTRATES THE PROFIT GENERATED FROM EACH UNIT OF PRODUCTION, AND IS WIDELY USED BY THE INVESTMENT COMMUNITY.
- **FUNDS PER SHARE FROM OPERATING ACTIVITIES** IS CALCULATED ON THE BASIS OF THE FUNDS FLOW FROM OPERATIONS AND THE WEIGHTED AVERAGE NUMBER OF SHARES.
- **NET CASH FLOWS PER SHARE FROM OPERATING ACTIVITIES** IS CALCULATED AS CASH FLOW FROM OPERATIONS OVER THE WEIGHTED AVERAGE NUMBER OF SHARES.

ADDITIONAL INFORMATION REGARDING ORCA EXPLORATION GROUP INC. IS AVAILABLE UNDER THE COMPANY'S PROFILE ON SEDAR AT www.sedar.com.

Background

Tanzania

Orca Exploration's principal operating asset is its interest in a Production Sharing Agreement ("PSA") with the Tanzania Petroleum Development Corporation ("TPDC") in Tanzania. This PSA covers the production and marketing of certain gas from the Songo Songo gas field.

The gas in the Songo Songo field is divided between Protected Gas and Additional Gas. The Protected Gas is owned by TPDC and is sold under a 20-year gas agreement (until July 2024) to Songas Limited ("Songas"). Songas is the owner of the infrastructure that enables the gas to be delivered to Dar es Salaam, which includes a gas processing plant on Songo Songo Island, 232 kilometers of pipeline to Dar es Salaam and a 16 kilometer spur to the Wazo Hill Cement Plant.

Songas utilizes the Protected Gas (maximum 45.1 MMcfd) as feedstock for its gas turbine electricity generators at Ubungu, for onward sale to the Wazo Hill cement plant and for electrification of some villages along the pipeline route. Orca Exploration receives no revenue for the Protected Gas delivered to Songas and operates the field and gas processing plant on a 'no gain no loss' basis.

Orca Exploration has the right to produce and market all gas in the Songo Songo field in excess of the Protected Gas requirements ("Additional Gas").

Italy

During 2010 Orca Exploration farmed in to an oil appraisal block in the Adriatic Sea in Italy and to a gas exploration prospect in the Po Valley in Northern Italy. In early August 2012, the operator of the La Tosca well in the Po Valley commenced drilling operations. On 27 August 2012 the well was plugged and abandoned having reached total depth, the gas shows encountered and data obtained during drilling having not warranted completion and testing of the well. The costs of the well have been written off in the current period.

Orca has earned a 70% working interest in the block and, subject to government approval, operatorship of the block. The Company intends to review the technical and drilling data to determine whether to continue exploration on the block.

Principal terms of the Tanzanian PSA and related agreements

The principal terms of the Songo Songo PSA and related agreements are as follows:

Obligations and restrictions

- (a) The Company has the right to conduct petroleum operations, market and sell all Additional Gas produced and share the net revenue with TPDC for a term of 25 years expiring in October 2026.
- (b) The PSA covers the two licenses in which the Songo Songo field is located ("Discovery Blocks"). The Proven Section is essentially the area covered by the Songo Songo field within the Discovery Blocks.
- (c) No sale of Additional Gas may be made from the Discovery Blocks if in Orca Exploration's reasonable judgment such sales would jeopardise the supply of Protected Gas. Any Additional Gas contracts entered into are subject to interruption. Songas has the right to request that the Company and TPDC obtain security reasonably acceptable to Songas prior to making any sales of Additional Gas from the Discovery Block to secure the Company's and TPDC's obligations in respect of Insufficiency (see (d) below).
- (d) "Insufficiency" occurs if there is insufficient gas from the Discovery Blocks to supply the Protected Gas requirements or is so expensive to develop that its cost exceeds the market price of alternative fuels at Ubungo.

Where there have been third party sales of Additional Gas by Orca Exploration and TPDC from the Discovery Blocks prior to the occurrence of the Insufficiency, Orca Exploration and TPDC shall be jointly liable for the Insufficiency and shall satisfy its related liability by either replacing the Indemnified Volume (as defined in (e) below) at the Protected Gas price with natural gas from other sources; or by paying money damages equal to the difference between: (a) the market price for a quantity of alternative fuel that is appropriate for the five gas turbine electricity generators at Ubungo without significant modification together with the costs of any modification; and (b) the sum of the price for such volume of Protected Gas (at US\$0.55/Mmbtu) and the amount of transportation revenues previously credited by Songas to the electricity utility, TANESCO, for the gas volumes.

- (e) The "Indemnified Volume" means the lesser of the total volume of Additional Gas sales supplied from the Discovery Blocks prior to an Insufficiency and the Insufficiency Volume. "Insufficiency Volume" means the volume of natural gas determined by multiplying the average of the annual Protected Gas volumes for the three years prior to the Insufficiency by 110% and multiplied by the number of remaining years (initial term of 20 years) of the power purchase agreement entered into between Songas and TANESCO in relation to the five gas turbine electricity generators at Ubungo from the date of the Insufficiency.

Access and development of infrastructure

- (f) The Company is able to utilise the Songas infrastructure including the gas processing plant and main pipeline to Dar es Salaam. Access to the pipeline and gas processing plant is open and can be utilised by any third party who wishes to process or transport gas. Ndovu Resources Limited which has a small gas field on Songo Songo Island has indicated that it wishes to tie its production into the gas processing plant. It is considered unlikely that this will occur during 2013.

Songas is not required to incur capital costs with respect to additional processing and transportation facilities unless the construction and operation of the facilities are, in the reasonable opinion of Songas, financially viable. If Songas is unable to finance such facilities, Songas shall permit the seller of the gas to construct the facilities at its expense, provided that, the facilities are designed, engineered and constructed in accordance with good pipeline and oilfield practices.



Revenue sharing terms and taxation

- (g) 75% of the gross revenues less processing and pipeline tariffs and direct sales taxes in any year (“Net Revenues”) can be used to recover past costs incurred. Costs recovered out of Net Revenues are termed “Cost Gas”.

The Company pays and recovers costs of exploring, developing and operating the Additional Gas with two exceptions: (i) TPDC may recover reasonable market and market research costs as defined under the PSA (US\$1.0 million as at 30 September 2012 for marketing costs that have been incurred by TPDC since start up); and (ii) TPDC has the right to elect to participate in the drilling of at least one well for Additional Gas in the Discovery Blocks for which there is a development program as detailed in the Additional Gas plans as submitted to the Ministry of Energy and Minerals (“MEM”) (“Additional Gas Plan”) subject to TPDC being able to elect to participate in a development program only once and TPDC having to pay a proportion of the costs of such development program by committing to pay between 5% and 20% of the total costs (“Specified Proportion”). If TPDC does not notify the Company within 90 days of notice from the Company that the MEM has approved the Additional Gas Plan, then TPDC is deemed not to have elected. If TPDC elects to participate, then it will be entitled to a rateable proportion of the Cost Gas and their profit share percentage increases by the Specified Proportion for that development program.

TPDC has indicated that they wish to exercise their right to ‘back in’ to the field development. The implications and workings of the ‘back in’ have been discussed with the Government Negotiation Team (“GNT”) and there may be the need for reserve and accounting modifications once these discussions are concluded. For the purpose of the reserves certification as at 31 December 2011, it has been assumed that they will ‘back in’ for 20% for all future new wells and other developments and this is reflected in the Company’s net reserve position.

- (h) On 27 February 2009, the energy regulator, Energy and Water Utility Regulatory Authority (“EWURA”), issued an order that saw the introduction of a flat rate tariff of US\$0.59/mcf from 1 January 2010. The Company’s long term gas price to the power sector as set out in the initialled ARGA and the Portfolio Gas Sales Agreement is based on the price of gas at the wellhead. As a consequence, the Company is not impacted by the changes to the tariff paid to Songas or other operators in respect of sales to the power sector.

During Q2 2011, the Company signed a Re-rating Agreement with TANESCO and Songas to run the gas processing plant at levels of up to 110 MMcfd (the pipeline and pressure requirements at the Ubungo power plant restrict the infrastructure capacity to a maximum of 102 MMcfd). Under the terms of the Re-rating Agreement, the Company effectively pays an additional tariff of US\$0.30/mcf for sales between 70 MMcfd and 90 MMcfd and US\$0.40/mcf for volumes above 90 MMcfd in addition to the tariff of US\$0.59/mcf payable to Songas as set by the energy regulator, EWURA.

The Re-rating Agreement will expire 31 December 2012. The Company is discussing an extension with the other parties to the agreement.

- (i) The cost of maintaining the wells and flowlines is split between the Protected Gas and Additional Gas users in proportion to the volume of their respective sales. The cost of operating the gas processing plant and the pipeline to Dar es Salaam is covered through the payment of the pipeline tariff.
- (j) Profits on sales from the Proven Section (“Profit Gas”) are shared between TPDC and the Company, the proportion of which is dependent on the average daily volumes of Additional Gas sold or cumulative production. The Company receives a higher share of the net revenues after cost recovery, based on the higher the cumulative production or the average daily sales. The Profit Gas share is a minimum of 25% and a maximum of 55%.

Average daily sales of Additional Gas	Cumulative sales of Additional Gas	TPDC’s share of Profit Gas	Company’s share of Profit Gas
<i>MMcfd</i>	<i>Bcf</i>	%	%
0 - 20	0 – 125	75	25
> 20 <= 30	> 125 <= 250	70	30
> 30 <= 40	> 250 <= 375	65	35
> 40 <= 50	> 375 <= 500	60	40
> 50	> 500	45	55

For Additional Gas produced outside of the Proven Section, the Company's Profit Gas share is 55%.

Where TPDC elects to participate in a development program, their profit share percentage increases by the Specified Proportion (for that development program) with a corresponding decrease in the Company's percentage share of Profit Gas.

The Company is liable to income tax. Where income tax is payable, there is a corresponding deduction in the amount of the Profit Gas payable to TPDC.

- (k) Additional Profits Tax is payable where the Company has recovered its costs plus a specified return out of Cost Gas revenues and Profit Gas revenues. As a result: (i) no Additional Profits Tax is payable until the Company recovers its costs out of Additional Gas revenues plus an annual return of 25% plus the percentage change in the United States Industrial Goods Producer Price Index ("PPI"); and (ii) the maximum Additional Profits Tax rate is 55% of the Company's Profit Gas when costs have been recovered with an annual return of 35% plus PPI return. The PSA is, therefore, structured to encourage the Company to develop the market and the gas fields in the knowledge that the profit share can increase with larger daily gas sales and that the costs will be recovered with a 25% plus PPI annual return before Additional Profits Tax becomes payable. Additional Profits Tax can have a significant negative impact on the project economics if only limited capital expenditure is incurred.

Operatorship

- (l) The Company is appointed to develop, produce and process Protected Gas and operate and maintain the gas production facilities and processing plant, including the staffing, procurement, capital improvements, contract maintenance, maintain books and records, prepare reports, maintain permits, handle waste, liaise with the Government of Tanzania and take all necessary safe, health and environmental precautions all in accordance with good oilfield practices. In return, the Company is paid or reimbursed by Songas so that the Company neither benefits nor suffers a loss as a result of its performance.
- (m) In the event of loss arising from Songas' failure to perform and the loss is not fully compensated by Songas, Orca Exploration, or insurance coverage, then Orca Exploration is liable to a performance and operation guarantee of US\$2.5 million when (i) the loss is caused by the gross negligence or wilful misconduct of the Company, its subsidiaries or employees, and (ii) Songas has insufficient funds to cure the loss and operate the project.

Consolidation

The companies that are being consolidated are:

Company	Incorporated
Orca Exploration Group Inc.	British Virgin Islands
Orca Exploration Italy Inc.	British Virgin Islands
Orca Exploration Italy Onshore Inc.	British Virgin Islands
PAE PanAfrican Energy Corporation	Mauritius
PanAfrican Energy Tanzania Limited	Jersey
Orca Exploration UK Services Limited	United Kingdom

RESULTS FOR THE QUARTER ENDED 30TH SEPTEMBER 2012

Operating Volumes

The sales volumes for the quarter were 5,292 MMcf or 57.5 MMcfd. This represents an increase of 3% over Q3 2011. The total sales volumes for the nine months ended 30 September 2012 were 15,101 MMcf or 55.1 MMcfd an increase of 24% over 2011.

The Company sales volumes were split between the industrial and power sectors as follows:

OPERATING VOLUMES	THREE MONTHS ENDED		NINE MONTHS ENDED	
	30 Sep 2012	30 Sep 2011	30 Sep 2012	30 Sep 2011
Gross sales volume (MMcf):				
Industrial sector	1,022	719	2,686	1,957
Power sector	4,270	4,442	12,415	10,201
<i>Total volumes</i>	5,292	5,161	15,101	12,158
Gross daily sales volume (MMcfd):				
Industrial sector	11.1	7.8	9.8	7.2
Power sector	46.4	48.3	45.3	37.4
<i>Total daily sales volume</i>	57.5	56.1	55.1	44.6

Industrial sector

Industrial sales volumes of 1,022 MMcf (11.1 MMcfd) were recorded in Q3 2012. This represents an increase of 42% over the 719 MMcf (7.8 MMcfd) recorded in Q3 2011. The increase is primarily due to increased sales to a major glass manufacturer as a result of supplying Additional Gas for its power generation, as well as to a significant cement producer in the Dar es Salaam area.

Industrial sales volumes for the nine months ended 30 September 2012 have increased by 37% to 2,686 MMcf from 1,957 MMcfd in 2011, with the sales to the glass manufacturer and the cement plant accounting for 57% and 46% of the total industrial sales recorded in the first nine months of 2012 and 2011 respectively.

Power sector

Power sector sales volumes of 4,270 MMcf (46.4 MMcfd) were recorded in Q3 2012. This represents a decrease of 4% over the 4,442 MMcf (48.3 MMcfd) recorded in Q3 2011. With production at full capacity, increased consumption by the industrial sector led to a small reduction in the volume available to the Power sector, which received the minimum contract volumes.

Power sector sales volumes for the nine months ended 30 September 2012 have increased by 22% to 12,415 MMcf (45.3 MMcfd) from 10,201 MMcf (37.4 MMcfd) in 2011.

Songo Songo deliverability

In Q4 2010 the Company reduced the deliverability from its Songo Songo wells following receipt of results of a corrosion logging survey. Orca suspended production from SS-5, reduced flow rates from the other wells and expedited the tie in of the new onshore well SS-10. As at 30 September 2012, the Company had a production capacity of approximately 113 MMcfd, restricted to 102 MMcfd by the available infrastructure.

The new production well SS-11 was successfully brought on stream on 3 October 2012 and is currently producing approximately 38 MMcfd. As planned SS-9, which was producing approximately 30 MMcfd, has been suspended. The Company has also permanently suspended SS-3 as a result of production tubing problems and rising casing annulus pressures. The condition of SS-4 is being monitored and it may have to be suspended in the future.

The Company plans to make up the production shortfall with additional volumes from SS-10 and SS-11. As a result no material change in field production levels of approximately 101 MMcfd is currently anticipated. There will, however, be no redundant capacity in the facility or pipeline until additional wells can be drilled in the field and facilities expanded. A loss or material reduction in the production of any given well will have a material adverse effect on the total production and funds flow from operations of the Company.

Production equipment originally installed in the SS-9, SS-5, SS-3 and SS-4 wells drilled by TPDC between 1976 and 1983 and has reached the end of its useful life. The SS-10 well was drilled by the Company in 2007. Plans for an additional development well, SS-12, have been placed on hold until the re-negotiation of certain terms of the Songo Songo Production Sharing Agreement and related issues arising from the GNT discussions have been fully resolved as well as the significant outstanding TANESCO receivable having been paid.

Commodity Prices

The commodity prices achieved in the different sectors during the quarter are shown in the table below:

US\$/mcf	THREE MONTHS ENDED		NINE MONTHS ENDED	
	30 Sep 2012	30 Sep 2011	30 Sep 2012	30 Sep 2011
Average sales price				
Industrial sector	9.21	10.47	9.62	10.10
Power sector	3.55	2.76	3.03	2.69
<i>Weighted average price</i>	4.64	3.83	4.20	3.88

Industrial sector

The average sales price achieved for Q3 2012 was US\$ 9.21/mcf compared to US\$10.47/mcf in Q3 2011. The decrease in sales price is a consequence of the reduction in world energy prices. The price of gas for the industrial sector (with the exception of the gas supplied to the cement plant) continued to be set at a discount to the price of Heavy Fuel Oil ("HFO") landed in Dar es Salaam. Additionally there was an increase in volumes supplied to a local cement plant and glass producer which both have a lower fixed pricing structure set by reference to the supply of imported coal.

Power sector

The average sales price to the power sector was US\$3.55/mcf for the quarter compared to US\$2.76/mcf in Q3 2011. The increase in the sales price over Q3 2011 is the result of applying contractually agreed annual indexation together with a change in the base price as set forth in the Portfolio Gas Sales Agreement between the Company and the state utility.

Operating Revenue

Under the terms of the Songo Songo PSA with TPDC, Orca Exploration is responsible for invoicing, collecting and allocating the revenue from Additional Gas sales.

Orca Exploration is able to recover all costs incurred on the exploration development and operations of the project out of 75% of the Net Revenues ("Cost Gas"). Any costs not recovered in any period are carried forward for recovery out of future revenues. Once the cost pool has been recovered TPDC will again be able to recover its past marketing costs, an estimated US\$1.0 million has been accrued to date in accordance with the terms of the PSA. TPDC marketing costs are treated as a reduction to Orca Exploration's Cost Gas entitlement.

The Additional Gas sales volumes were in excess of 50 MMcfd for Q3 2012 and Q3 2011. Consequently, in accordance with the terms of the PSA, the revenue less cost recovery share of revenue ("Profit Gas") was 55% for both periods.

From January 2011, a significant proportion of the gas production was from the SS-10 well, which has been deemed "backed into" by TPDC. As a result TPDC's profit share increased by 20% for the production attributable to SS-10. The implications and workings of the 'back in' have been discussed with the GNT, but further discussion is required to finalise the arrangement by way of an amendment to the PSA.

Orca Exploration had recoverable costs throughout the quarter and accordingly was allocated 88.0% (Q3 2011: 68.3%) of the Net Revenues as follows:

<i>Figures in US\$'000</i>	THREE MONTHS ENDED		NINE MONTHS ENDED	
	30 Sep 2012	30 Sep 2011	30 Sep 2012	30 Sep 2011
Gross sales revenue	24,544	19,754	63,468	47,154
Gross tariff for processing plant and pipeline infrastructure	(3,975)	(3,717)	(11,120)	(7,845)
Gross revenue after tariff	20,569	16,037	52,348	39,309
<i>Analysed as to:</i>				
Company Cost Gas	15,426	4,844	39,261	17,150
Company Profit Gas	2,673	6,113	6,926	9,801
Company operating revenue	18,099	10,957	46,187	26,951
TPDC share of revenue	2,470	5,080	6,161	12,358
	20,569	16,037	52,348	39,309

The Company reported revenue for the quarter of US\$22,425 (Q3 2011: US\$10,457) after adjusting the Company's operating revenue of US\$18,099 (Q3 2011: US\$10,957) by:

- US\$5,226 (Q3 2011: US\$659) for revenue recovery relating to current income tax. The Company is liable for income tax in Tanzania, but the income tax is recoverable out of TPDC's share of Profit Gas when the tax is payable. To account for this, revenue is adjusted to reflect the current income tax charge.
- US\$900 (Q3 2011: US\$1,159) for the deferred effect of Additional Profits Tax. This tax is considered a royalty and is netted against revenue.

The substantial increase in revenue compared to Q3 2011 is the result of several factors. Volumes and prices have contributed to an overall increase, but the level of investment in 2012 has resulted in a significant increase in Cost Gas, reducing TPDC's share of profit. It has also resulted in a higher taxable profit which in turn increases the Company share of revenue.

Management expects the PSA cost pools to be fully recovered by the end of the year, which recovery will result in a significant decrease in Cost Gas until capital spending is resumed.

<i>Figures in US\$'000</i>	THREE MONTHS ENDED		NINE MONTHS ENDED	
	30 Sep 2012	30 Sep 2011	30 Sep 2012	30 Sep 2011
Industrial sector	9,392	7,517	25,841	19,763
Power sector	15,152	12,237	37,627	27,391
Gross sales revenue	24,544	19,754	63,468	47,154
Processing and transportation tariff	(3,975)	(3,717)	(11,120)	(7,845)
TPDC share of revenue	(2,470)	(5,080)	(6,161)	(12,358)
Company operating revenue	18,099	10,957	46,187	26,951
Additional Profits Tax	(900)	(1,159)	(2,289)	(1,946)
Current income tax adjustment	5,226	659	12,647	3,388
Revenue	22,425	10,457	56,545	28,393

Processing and Transportation Tariff

Since early 2011, the Company has paid a flat rate regulated gas processing and transportation tariff of US\$0.59/mcf to Songas. Under the terms of the gas contracts with the power sector, the Company will pass on any increase or decrease in the EWURA approved charges to its customers. This protocol insulates Orca Exploration from any increases in the gas processing and pipeline infrastructure costs.

During Q2 2011, the Company signed a Re-rating Agreement with TANESCO and Songas to run the gas processing plant at levels of up to 110 MMcfd (the pipeline and pressure requirements at the Ubungo power plant restrict the infrastructure capacity to a maximum of 102 MMcfd). Under the terms of this agreement, the Company effectively pays an additional tariff of US\$0.30/mcf for sales between 70 MMcfd and 90 MMcfd and US\$0.40/mcf for volumes above 90 MMcfd in addition to the regulated tariff of US\$0.59/mcf payable to Songas. The charge for the additional tariff was US\$0.9 million for the third quarter of 2012.

Production and distribution expenses

The well maintenance costs are allocated between Protected and Additional Gas based on the proportion of their respective sales during the quarter. The total costs for the maintenance for the quarter was US\$692 (Q3 2011: US\$690) and US\$457 (Q3 2011: US\$401) was allocated for the Additional Gas. The total allocated cost for well maintenance for the nine months ended 30 September 2012 was US\$797 compared to US\$612 for the nine months ended 30 September 2011.

Other field and operating costs include an apportionment of the annual PSA licence costs, regulatory fees and some costs associated with the evaluation of the reserves and the cost of personnel that are not recoverable from Songas.

Distribution costs represent the direct cost of maintaining the ringmain distribution pipeline and pressure reduction station (security, insurance and personnel).

In the context of the GNT negotiations and the recently announced draft Natural Gas Policy, TPDC and MEM have indicated that they wish Orca to unbundle the downstream distribution business in Tanzania. The methodology for this is currently being discussed with the government and may lead to future modifications to the accounts.

These costs are summarized in the table below:

<i>Figures in US\$'000</i>	THREE MONTHS ENDED		NINE MONTHS ENDED	
	30 Sep 2012	30 Sep 2011	30 Sep 2012	30 Sep 2011
Share of well maintenance	457	401	797	612
Other field and operating costs	380	776	1,535	1,484
	837	1,177	2,332	2,096
Ringmain distribution pipeline	660	623	2,292	1,913
Production and distribution expenses	1,497	1,800	4,624	4,009

Operating netbacks

The netback per mcf before general and administrative costs, overheads, tax and Additional Profits Tax may be analysed as follows:

<i>Amounts in US\$/mcf</i>	THREE MONTHS ENDED		NINE MONTHS ENDED	
	30 Sep 2012	30 Sep 2011	30 Sep 2012	30 Sep 2011
Gas price – industrial	9.21	10.47	9.62	10.10
Gas price – power	3.55	2.76	3.03	2.69
Weighted average price for gas	4.64	3.83	4.20	3.88
Processing and transportation tariff	(0.75)	(0.72)	(0.74)	(0.65)
TPDC share of revenue	(0.47)	(0.98)	(0.41)	(1.02)
Net selling price	3.42	2.13	3.05	2.21
Well maintenance and other operating costs	(0.16)	(0.23)	(0.15)	(0.17)
Ringmain distribution pipeline	(0.12)	(0.12)	(0.15)	(0.16)
Operating netback	3.14	1.78	2.75	1.88

The operating netback for the quarter was US\$3.14/mcf (Q3 2011: US\$1.78/mcf) and for the first nine months of 2012 was US\$2.75/mcf (Q3 2011: US\$1.88/mcf).

The increase in the weighted average selling price from US\$3.83/mcf to US\$4.64/mcf in Q3 2012 is partly a consequence of a change in the sales mix resulting in lower average industrial prices, offset by a 42% increase in volume, and partly the result of a substantial increase in the Power price which offset a small volume reduction.

TPDC's share of revenue in Q3 2012 decreased as a result of capital investment which entitled the Company to claim 75% of Net Revenues as Cost Gas, before allocating Profit Gas. This was not the case in Q3 2011 when the cost pool had been fully recovered, which also allowed TPDC to recover past marketing costs.

Administrative Expenses

The administrative expenses ("G&A") may be analysed as follows:

<i>Figures in US\$'000</i>	THREE MONTHS ENDED		NINE MONTHS ENDED	
	30 Sep 2012	30 Sep 2011	30 Sep 2012	30 Sep 2011
Employee & related costs	2,011	2,818	6,735	6,197
Office costs	849	561	2,782	1,810
Marketing costs including legal fees	279	630	828	1,703
Reporting, regulatory and corporate	1,252	390	1,977	1,026
	4,391	4,399	12,322	10,736

The G&A includes the costs of running the gas distribution business in Tanzania which is recoverable as Cost Gas and is relatively fixed in nature.

G&A averaged approximately US\$1.47 million per month for Q3 2012 compared to US\$1.47 million in Q3 2011. G&A per mcf decreased to US\$0.83/mcf (Q3 2011: US\$0.85/mcf).

The main variances for both the quarter and the nine months ended 30 September 2012 compared to the same periods in 2011 are summarized below:

Employee & Related costs

Employee costs in Q3 have fallen following a reduction in the number of expatriate personnel in Tanzania. Q3 2011 was also inflated by search fees for senior executives of US\$0.3 million.

Office costs

The increase results primarily from the establishment of an Orca UK Services office.

Marketing costs and legal fees

The decrease in marketing and legal fees compared to 2011 is a consequence of finalizing the Portfolio Gas Agreement which was signed at the end of Q2 2011.

Reporting, regulatory and corporate costs

The increase of US\$0.9 million is the result of several factors. A tax penalty of US\$0.4 million; and directors fees of US\$0.5 million, relating to Q2/Q3.

Stock based compensation

A total of 2,172,400 stock options were outstanding at the end of Q3 2012 compared to 2,807,400 at the end of Q3 2011. Of these options 1,422,400 were issued in 2004 and were fully expensed by the end of 2007; 100,000 were issued during 2007 and were fully expensed by the end of 2010; 250,000 were issued during 2007 and were fully expensed by the end of 2011; 400,000 were granted in 2012 and were fully expensed during Q2, resulting in a charge of US\$0.7 million.

A total of 415,000 stock appreciation rights were outstanding at the end of Q3 2012, compared to 930,000 at the end of Q3 2011. Of these 300,000 were issued in June 2010 to non-executive directors with an exercise price of CDN\$4.20 per share. These rights have a five year term and vest in five equal instalments, the first fifth vesting on the anniversary of the grant date. 15,000 were issued in September 2008 with an exercise price of CDN\$5.30 and 100,000 were issued in August 2012 with an exercise price of CDN\$2.70 to executive management. These rights have a five year term and vest in three equal instalments, the first third on the anniversary of the grant date.

As stock appreciation rights are settled in cash they are re-valued at each reporting date using the Black-Scholes option pricing model. As at 30 September 2012 the following assumptions were used: stock volatility 53% to 70%, a risk free interest rate of 1.50% and a closing stock price of CDN\$2.80. A charge of US\$0.08 million was recorded in Q3 2012 compared to a credit of US\$0.17 million in Q3 2011 in respect of these stock appreciation rights.

The total stock based compensation charges may be summarized as follows:

<i>Figures in US\$'000</i>	THREE MONTHS ENDED		NINE MONTHS ENDED	
	30 Sep 2012	30 Sep 2011	30 Sep 2012	30 Sep 2011
Stock options	-	661	720	661
Stock appreciation rights	80	(168)	(19)	(258)
	80	493	701	403

Net Finance Costs

The movement in net financing costs is summarized in the table below:

<i>Figures in US\$'000</i>	THREE MONTHS ENDED		NINE MONTHS ENDED	
	30 Sep 2012	30 Sep 2011	30 Sep 2012	30 Sep 2011
FINANCE INCOME				
Interest income	2	1	4	5
FINANCE CHARGES				
Loan interest and related financing costs	(47)	-	(143)	-
Net foreign exchange loss	(362)	(323)	(550)	(1,036)
	(409)	(323)	(693)	(1,036)
NET FINANCE COSTS	(407)	(322)	(689)	(1,031)

Taxation

Income Tax

Under the terms of the PSA with TPDC, the Company is liable for income tax in Tanzania at the corporate tax rate of 30%. However, where income tax is payable, this is recovered from TPDC by deducting an amount from TPDC's profit share. This is reflected in the accounts by increasing the Company's revenue by the appropriate amount.

As at 30 September 2012, there were temporary differences between the carrying value of the assets and liabilities for financial reporting purposes and the amounts used for taxation purposes under the Income Tax Act 2004. Applying the 30% Tanzanian tax rate, the Company has recognised a deferred tax liability of US\$19.3 million, which includes an additional deferred future income tax charge of US\$2.0 million for the quarter (Q3 2011: US\$0.7 million), resulting in a total charge for the nine months to 30 September of US\$4.1 million and US\$1.4 million for 2012 and 2011 respectively. This tax has no impact on cash flow until it becomes a current income tax at which point the tax is paid to the Commissioner of Taxes and recovered from TPDC's share of Profit Gas.

Additional Profits Tax

Under the terms of the PSA, in the event that all costs have been recovered with an annual return of 25% plus the percentage change in the United States Industrial Goods Producer Price Index ("PPI"), an Additional Profits Tax ("APT") is payable.

The Company provides for APT by forecasting the total APT payable as a proportion of the forecast Profit Gas over the term of the PSA. The effective APT rate of 31.8% (Q3 2011 20%) is then applied to Profit Gas of US\$2.7 million in Q3 2012 (Q3 2011: US\$6.1 million). Accordingly, US\$0.9 million (Q3 2011: US\$1.2 million) has been netted off revenue for the quarter ended 30 September 2012. The total adjustment for the nine months to 30 September was US\$2.3 million and US\$1.4 million for 2012 and 2011 respectively.

Management does not anticipate that any APT will be payable in 2012, as the forecast revenues will not be sufficient to cover the un-recovered costs brought forward as inflated by 25% plus the PPI percentage change and the forecast expenditures for 2012. The actual APT that will be paid is dependent on the achieved value of the Additional Gas sales and the quantum and timing of the operating costs and capital expenditure program.

The APT can have a significant negative impact on the Songo Songo project economics as measured by the net present value of the cash flow streams. Higher revenue in the initial years leads to a rapid payback of the project costs and consequently accelerates the payment of the APT that can account for up to 55% of the Company's profit share. Therefore, the terms of the PSA rewards the Company for taking higher risks by incurring capital expenditure in advance of revenue generation.

Depletion and Depreciation

The Natural Gas Properties are depleted using the unit of production method based on the production for the period as a percentage of the total future production from the Songo Songo proven reserves. As at 31 December 2011 the proven reserves as evaluated by the independent reservoir engineers, McDaniel & Associates Consultants Ltd., were 469.1 Bcf, after TPDC 'back-in', on a life of licence basis. This leads to an average depletion charge of US\$0.40/mcf for the year (2011: US\$0.47/mcf).

Non-Natural Gas Properties are depreciated as follows:

Leasehold improvements	Over remaining life of the lease
Computer equipment	3 years
Vehicles	3 years
Fixtures and fittings	3 years

Carrying Amount of Assets

Capitalised costs are periodically assessed to determine whether it is likely that such costs will be recovered in the future. To the extent that these capitalised costs are unlikely to be recovered in the future, they are impaired and recorded in the statement of comprehensive income (loss). In Q3 the Company recognised impairment of the La Tosca exploration well and has expensed the total cost of US\$7.5 million when it was determined that the well did not have commercially viable quantities of mineral resources.

Funds Generated by Operations

Funds flow from operating activities were US\$14.4 million for the quarter ended 30 September 2012 (Q3 2011: US\$5.3 million) and US\$34.3 million for the nine months ended 30 September 2012 (2011: US\$13.6 million).

Figures in US\$'000	THREE MONTHS ENDED		NINE MONTHS ENDED	
	30 Sep 2012	30 Sep 2011	30 Sep 2012	30 Sep 2011
Profit after taxation	1,266	(54)	12,825	2,719
Adjustments ⁽ⁱ⁾	13,113	5,377	21,425	10,842
Funds from operations before working capital changes	14,379	5,323	34,250	13,561
Working capital adjustments ⁽ⁱ⁾	(5,291)	(7,780)	(12,820)	(10,381)
Net cash flows from operating activities	9,088	(2,457)	21,430	3,181
Net cash flows used in investing activities	(11,618)	(3,772)	(38,424)	(5,852)
Net cash flows from financing activities	5,800	–	5,800	–
Effect of change in foreign exchange	(175)	(132)	(197)	(216)
Net (decrease)/increase in cash and cash equivalents	3,095	(6,361)	(11,391)	(2,887)

⁽ⁱ⁾ Please refer to consolidated statement of cash flows for breakdown

The US\$3.1 million increase in cash and cash equivalents for the quarter is a result of the US\$14.4 million of funds from operations before working capital changes during the quarter being offset by US\$11.6 million of capital expenditure incurred, a net cash reduction of US\$5.3 million in working capital and a net loan receipt of US\$5.8 million.

The US\$11.4 million decrease in cash and cash equivalents for the nine months ended 30 September 2012 is a result of the US\$34.3 million of funds generated from operations before working capital changes during the period being offset by US\$38.4 million of capital expenditure, an overall net decrease in working capital of US\$12.8 million and a net loan receipt of US\$5.8 million.

Capital Expenditure

Gross capital expenditures amounted to US\$15.0 million during the quarter (Q3 2011: US\$3.9 million) and US\$52.2 million for the nine months ended 30 September 2012 (2011: US\$6.9 million).

The capital expenditure may be analysed as follows:

Figures in US\$'000	THREE MONTHS ENDED		NINE MONTHS ENDED	
	30 Sep 2012	30 Sep 2011	30 Sep 2012	30 Sep 2011
Geological and geophysical and well drilling	14,749	3,463	50,898	5,486
Pipelines and infrastructure	261	421	1,043	1,147
Power development	22	–	197	15
Other equipment	1	41	107	226
	15,033	3,925	52,245	6,874

Geological and geophysical and well drilling

US\$9.7 million related to completion, including rig demobilization, tie-in and commissioning of the SS-11 development well; US\$5.0 million to drilling of the La Tosca exploration well.

Pipelines and infrastructure

A total of US\$0.2 million of expenditure was incurred during the quarter in relation of the ringmain and related distribution facilities in Dar es Salaam.

Working Capital

Working capital as at 30 September 2012 was US\$37.7 million compared with US\$56.0 million as at 31 December 2011 and may be analyzed as follows:

	30 Sep 2012	31 Dec 2011
Cash and cash equivalents	23,289	34,680
Trade and other receivables	62,284	40,348
Taxation receivable	15,078	5,880
Prepayments	499	302
	101,151	81,210
Trade and other payables	50,753	22,801
Loan	5,800	–
Taxation payable	6,868	2,403
Working capital	37,730	56,006

The level of working capital has decreased by 33% during the nine months ended 30 September 2012.

At 30 September 2012 the majority of the Company's cash was held in Tanzania. There are no restrictions in Tanzania for converting Tanzania Shillings into US dollars.

Trade and other receivables at 30 September 2012 comprise trade receivables US\$50.7 million (Q4 2011: US\$35.7 million) and other receivables US\$11.6 million (Q4 2011: US\$4.7 million). Of the trade receivables US\$31.2 million (Q4 2011: US\$24.9 million) relates to sales to TANESCO. The increase in other receivables, relates principally to an increase in the amount due from Songas for operation of the gas processing plant and associated projects. The increase in the tax related receivable is a consequence of the increased level of current taxation. The tax related receivable represents an additional share of revenue based on the current tax charge. The tax charge for the nine months ended 30 September 2012 is US\$8.2 million (2011: US\$2.6 million). This sum is grossed up for income tax at 30% and recovered from TPDC once tax has been paid.

Under the contract terms with the industrial customers, the Additional Gas payments must be received within 30 days of the month end. Collection of the arrears owed by TANESCO has presented difficulties, which are not wholly resolved. However, during Q3 the utility paid US\$13.2 million and since the end of Q3 a further US\$9.5 million has been received. At the end of Q3, the TANESCO receivable stood at US\$31.2 million (including arrears of US\$26.8 million), up 5% from US\$29.6 million (including arrears of US\$25.6 million) at the end of Q2. As at the date of this report TANESCO arrears total US\$21.7 million. The balance due from Songas has increased but is offset by a similar increase in amounts due to Songas.

Bank Loan

In September 2012, the Company closed a US\$10 million 18-month bridge loan facility with a Tanzania bank to finance the Company's working capital requirements in Tanzania. The facility is secured by an assignment of accounts receivable and a fixed and floating charge on the assets of the Company. As at 30 September the Company has drawn down US\$6.0 million under the facility and paid US\$0.2 million in financing fees. Principal amounts drawn under the facility are repayable in 12 equal monthly instalments commencing in March 2013. Interest is payable monthly at three-month US LIBOR plus 8%. An additional interest rate of 2% will be applied for any period in which the TANESCO receivable is greater than 240-days.

Future operations

The Company generates in excess of 50% of its operating revenue from sales to the power sector companies, Songas and TANESCO. Songas' financial security is heavily reliant on the payment of capacity and energy charges by TANESCO. TANESCO is dependent on the Government of Tanzania for some of its funding. Prior to 2012, despite having a history of delayed payments TANESCO had settled in full the outstanding balance subsequent to each quarter end.

At 30 September 2012, TANESCO owed the Company US\$31.2 million (including arrears of US\$26.7 million) compared to US\$24.2 million (including arrears of US\$20.2 million) as at 31 December 2011. During the third quarter changes took place within TANESCO management which have led to constructive dialogue with the Company. TANESCO's new management has assured the Company of its intention to pay. Subsequent to the end of Q3, the Company has received US\$9.5 million and, as of the date of this report, the arrears total US\$21.7 million. During the year, and as of the date of this report, the Company has received US\$37.4 million from TANESCO, in settlement of the 31 December 2011 arrears and that for the first quarter of 2012.

At the end of Q3 Songas owed the Company US\$17.80 million, whilst the Company owed Songas US\$14.8 million; there is no legal right to offset these amounts.

During Q3, to help alleviate the funding gap caused by the delays in TANESCO payments, the Company put in place a US\$10 million facility with a bank in Tanzania. As at 30 September the Company had drawn down US\$6 million of this facility, incurring financing charges of US\$0.2 million.

Any significant additional capital expenditure in Tanzania remains dependent on TANESCO payments being brought up to date, the satisfactory conclusion of the GNT issues, progress on infrastructure expansion and the subsequent raising of finance. Significant additional capital expenditure will be required to enable the Songo Songo field to produce 200 MMcfd in line with the anticipated infrastructure expansion. There are no guarantees that such additional funding will be available when needed, or will be available on suitable terms, however, management is actively pursuing additional sources of capital as a contingency.

During Q3, as a result of deteriorating hydro power supplies, MEM instructed the Company to temporarily direct all gas supplies to the Power sector. Following extensive discussions agreement was reached on the volumes the Company could supply without jeopardising its ability to meet other commitments.

CONTRACTUAL OBLIGATIONS AND COMMITTED CAPITAL INVESTMENT

Contractual Obligations

Protected Gas

Under the terms of the original gas agreement for the Songo Songo project (“Gas Agreement”), in the event that there is a shortfall/insufficiency in Protected Gas as a consequence of the sale of Additional Gas, then the Company is liable to pay the difference between the price of Protected Gas (US\$0.55/MMbtu) and the price of an alternative feedstock multiplied by the volumes of Protected Gas up to a maximum of the volume of Additional Gas sold (80.3 Bcf as at 30 September 2012). The Company did not have a shortfall during the reporting period does not anticipate a shortfall arising during the licence period.

Operating leases

The Company has two office rental agreements in Dar es Salaam, expiring on 30 November 2012 and 31 October 2013 at an annual rental of US\$122,000 and US\$110,000 per annum respectively. The Company is negotiating an extension to the lease which expires in November 2012.

Capital Commitments

Italy

On 30 May 2010, the Company signed an agreement with Petroceltic International plc (“Petroceltic”) to farm in on Petroceltic’s Central Adriatic B.R268.RG Permit offshore Italy. The farm-in commits the Company to fund 30% of the Elsa-2 appraisal well up to a maximum of US\$11.5 million to earn a 15% working interest in the permit. Thereafter, the Company will fund all future costs relating to the well and the permit in proportion to its participating interest. The Company has also agreed to pay Petroceltic fifteen per cent (15%) of the back costs in relation to the well up to a maximum of US\$0.5 million.

Petroceltic was due to spud the Elsa-2 well prior to 31 October 2010, but the Italian government passed a decree, following the blowout of the Macondo well in the U.S., that prevented the drilling in the Italian seas within five nautical miles of the coastline and within 12 nautical miles around the perimeter of protected Marine Parks. In view of this, Petroceltic suspended the permit until such time as the Ministry of Environment issued a decree of environmental compatibility for the drilling program. During the quarter, Legislative Decree 83/2012 (the “Decree”), published on 26 June 2012 was approved by both houses of the Italian Parliament with no substantial modifications. On 12th August, the Decree became law following publication in the Italian Official Journal. The new law modifies restrictions on offshore oil and gas exploration and production originally introduced by DLGS 128/2010 in August 2010. The well is expected to be drilled following finalisation of an environmental impact study currently expected in the second half of 2013. Orca will not be liable to any costs associated with the drilling of Elsa-2 until a rig contract is signed.

Songo Songo commitments

The total cost of the SS-11 well which came onstream 3 October, including its connection to the gas processing plant, was US\$45 million. Any significant additional capital expenditure in Tanzania remains dependent on TANESCO payments being brought up to date, the satisfactory conclusion of the GNT issues, progress on infrastructure expansion and the subsequent raising of finance. Significant additional capital expenditure will be required to enable the Songo Songo field to produce 200 MMcfd in line with the anticipated infrastructure expansion.

Contingencies

Re-rating Agreement

During Q2 2011, the Company signed a Re-rating Agreement with TANESCO and Songas to increase the gas processing capacity to a maximum of 110 MMcfd (the pipeline and pressure requirements at the Ubungo power plant restrict the infrastructure capacity to a maximum of 102 MMcfd). Under the terms of the Re-rating Agreement, the Company effectively pays an additional tariff of US\$0.30/mcf for sales between 70 MMcfd and 90 MMcfd and US\$0.40/mcf for volumes above 90 MMcfd in addition to the tariff of US\$0.59/mcf payable to Songas as set by the energy regulator, EWURA.

Under the terms of this agreement, the Company agreed to indemnify Songas for damage to its facilities caused by the re-rating, up to a maximum of US\$15 million, but only to the extent that this was not already covered by indemnities from TANESCO or Songas' insurance policies. As at 30 September 2012 the Company is not aware of any damage to the facilities that would result in a charge and the indemnity will remain in force until such time as the plant is de-rated. The Re-rating Agreement will expire 31 December 2012. An extension of the Re-Rating Agreement is currently being discussed among MEM, TPDC and Songas.

Access to infrastructure

Ndovu Resources Limited, with support from TPDC and MEM, has indicated that they wish to tie into the gas processing plant on Songo Songo Island and sell up to 10 MMcfd from their Kiliwani North field. Access has not yet been granted and it is not clear when, or if, this will occur.

PSA Negotiations

In February 2012 on the recommendation of MEM, the Government announced that it was establishing a negotiating team, the GNT, to discuss a number of issues raised in parliament in relation to the Company's Songo Songo PSA with TPDC. In Tanzania, government negotiating teams are a common mechanism to negotiate with business. The scope of the GNT was to discuss a number of points that were raised by the Parliamentary Committee for Energy into the workings of the PSA. This included, but is not limited to, TPDC back in rights, profit sharing arrangements, the unbundling of the downstream assets, cost recovery and Orca's management of the upstream operations. After making submissions to the GNT, the Company commenced discussions in April 2012 and further in July 2012. In July 2012, Parliament dissolved the Parliamentary Committee for Energy and Minerals on the grounds of alleged widespread corruption and abuse of power. A Parliamentary team formed to investigate the allegations subsequently cleared Members of Parliament of any wrong doing. During the quarter, an agreement in principle was been reached on a number of major points to resolve the issues. The GNT has completed its mandate, and the responsibility for finalisation, documentation and implementation has moved back to MEM. The agreement in principal contemplated completion this process by the end of 2012. As at the date of this report, a number of issues remain to be fully resolved and documented. The outcome of these negotiations could have a significant impact on the operations of the Company, which cannot be estimated at this time.

Back in

TPDC has indicated that they wish to exercise their right to 'back in' to the field development. The implications and workings of the 'back in' have been discussed with the GNT along with other issues. The issues are not yet fully resolved however, there may be the need for additional reserve and accounting modifications once these discussions are concluded. For the purpose of the reserves certification as at 31 December 2011, it was assumed TPDC will 'back in' for 20% for all future new drilling activities and other developments and this is reflected in the Company's net reserve position.



Unbundling

In connection with the GNT negotiations and the recently announced draft Natural Gas Policy, TPDC and MEM have indicated that they wish Orca to unbundle the downstream distribution business in Tanzania. The methodology for this has been discussed with the GNT along with other issues. The Company anticipates further negotiations will be necessary before this matter is concluded.

Cost recovery

The Company's cost pool in Tanzania was recovered early in Q2 2011 resulting in a reduction in the percentage of net revenue attributable to the Company. During 2012 the level of Cost Gas has increased as a result of significant expenditure on drilling the SS-11 well. TPDC conducted an audit of the historic cost pool and in 2011 disputed approximately US\$34 million of costs that had been allocated to the cost pool from 2002 through to 2009. The Company contends that the disputed costs were appropriately incurred on the Songo Songo project in accordance with the terms of the PSA. This matter was not resolved during discussions with the GNT to date. While the Company remains confident that the final outcome will be satisfactory, it is prepared to utilise the dispute resolution mechanisms outlined in the PSA if necessary. This matter has had no impact on the current quarter.

Taxation

The Company has received an assessment for additional withholding tax from the Tanzanian Revenue Authority (TRA), which together with interest penalties totals approximately US\$2.0 million. The Company, supported by its professional advisors, believes the assessment to be without merit and has submitted a formal appeal to the Tax Revenue Appeal Board. A date for the hearing has not yet been set.

Related Party Transactions

One of the non executive directors is a partner at a law firm. During the quarter, the Company incurred US\$50 (Q2 2011: US\$38) to this firm for legal services provided, resulting in a total expenditure of US\$246 for the nine months ended 30 September 2012 (2011: US\$113). The transactions with this related party were made at the exchange amount and as at 30 September 2012 US\$246 was payable.

Shareholders' Equity and Outstanding Share Data

<i>Number of shares ('000)</i>	AS AT	
	30 Sep 2012	31 Dec 2011
SHARES OUTSTANDING		
Class A shares	1,751	1,751
Class B shares	32,743	32,747
Class A and Class B shares outstanding	34,494	34,498
WEIGHTED AVERAGE		
Class A and Class B shares	34,494	34,656
Convertible securities		
Stock options	948	1,176
Weighted average diluted Class A and Class B shares	35,442	35,832

Shares outstanding

No new stock options were issued during the quarter.

No stock options were exercised during the quarter.

No Class B shares were purchased under the normal course issuer bid.

As at 28 November 2012, there were a total of 1,751,195 Class A shares and 32,742,515 Class B shares outstanding.



SUMMARY QUARTERLY RESULTS

The following is a summary of the results for the Company for the last eight quarters:

<i>(Figures in US\$'000 except where otherwise stated)</i>	2012			2011				2010
	Q3	Q2	Q1	Q4	Q3	Q2	Q1	Q4
FINANCIAL								
Revenue	22,425	16,915	17,207	17,500	10,457	8,296	9,640	10,557
Profit/(loss) after taxation	1,266	5,167	6,392	5,267	(54)	383	2,390	1,885
Operating netback <i>(US\$/mcf)</i>	3.14	2.56	2.55	2.41	1.78	1.80	2.16	2.28
Working capital	37,730	38,689	47,063	56,006	58,369	57,070	55,759	52,364
Shareholders' equity	120,204	118,938	113,051	106,659	101,563	100,956	100,573	98,183
Profit/(loss) per share – basic <i>(US\$)</i>	0.04	0.15	0.19	0.15	0.00	0.01	0.07	0.05
Profit/(loss) per share – diluted <i>(US\$)</i>	0.04	0.15	0.18	0.15	0.00	0.01	0.07	0.05
CAPITAL EXPENDITURES								
Geological and geophysical and well drilling	14,749	17,732	18,418	10,989	3,463	1,124	899	607
Pipeline and infrastructure	261	563	219	11	421	364	362	383
Power development	22	84	91	22	–	11	4	–
Other equipment	1	86	20	239	41	94	91	45
OPERATING								
Additional Gas sold – industrial <i>(MMcf)</i>	1,022	829	835	786	719	688	550	687
Additional Gas sold – power <i>(MMcf)</i>	4,270	4,172	3,973	4,521	4,442	2,965	2,794	2,926
Average price per mcf – industrial <i>(US\$)</i>	9.21	10.14	9.63	9.94	10.47	10.28	9.42	8.67
Average price per mcf – power <i>(US\$)</i>	3.55	2.80	2.72	2.97	2.76	2.64	2.62	2.63

CORPORATE INFORMATION

Board of Directors

W. David Lyons
Chairman and
Chief Executive Officer

Winchester
United Kingdom

David W. Ross
Non-Executive Director

Calgary
Canada

William H. Smith
Non-Executive Director

Calgary, Alberta
Canada

Robert S. Wynne
Chief Financial Officer

Calgary, Alberta
Canada

Officers

W. David Lyons
Chairman and
Chief Executive Officer

Winchester
United Kingdom

Robert S. Wynne
Chief Financial Officer

Calgary, Alberta
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Chief Operating Officer

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