ORCA EXPLORATION GROUP INC.

2012 Q3 Interim Report

ORCA EXPLORATION GROUP INC.

is an international public company engaged in hydrocarbon exploration, development and supply of gas in Tanzania and oil appraisal and gas exploration in Italy. Orca Exploration trades on the TSXV under the trading symbols ORC.B and ORC.A.

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GLOSSARY

mcf	Thousands of standard cubic feet	*1P*	Proven reserves
MMcf	Millions of standard cubic feet	*2P*	Proven and probable reserves
Bcf	Billions of standard cubic feet	*3P*	Proven, probable and possible reserves
Tcf	Trillions of standard cubic feet	*Kwh*	Kilowatt hour
MMcfd	Millions of standard cubic feet per day	*MW*	Megawatt
MMbtu	Millions of British thermal units	*US$*	US dollars
HHV	High heat value	*CDN$*	Canadian dollars
LHV	Low heat value	*bar*	Fifteen pounds pressure per square inch

FINANCIAL AND OPERATING HIGHLIGHTS

	THREE MONTHS ENDED OR AS AT			NINE MONTHS ENDED OR AS AT		
	30 Sep 2012	30 Sep 2011	Change	**30 Sep 2012**	30 Sep 2011	Change
Financial *(US$'000 except where otherwise stated)*						
Revenue	**22,425**	10,457	114%	**56,545**	28,393	99%
Profit before taxation	**6,310**	1,289	389%	**25,136**	6,660	277%
Operating netback *(US$/mcf)*	**3.14**	1.78	76%	**2.75**	1.88	46%
Cash and cash equivalents	**23,289**	42,632	(45%)	**23,289**	42,632	(45%)
Working capital	**37,730**	58,369	(35%)	**37,730**	58,369	(35%)
Shareholders' equity	**120,204**	101,563	18%	**120,204**	101,563	18%
Earnings per share - basic *(US$)*	**0.04**	0.00	n/a	**0.37**	0.08	363%
Earnings per share - diluted *(US$)*	**0.04**	0.00	n/a	**0.36**	0.08	350%
Funds flow from operating activities	**14,379**	5,323	170%	**34,250**	13,562	153%
Funds per share from operating activities - basic *(US$)*	**0.42**	0.15	193%	**0.99**	0.39	154%
Funds per share from operating activities - diluted *(US$)*	**0.41**	0.15	186%	**0.97**	0.38	155%
Net cash flows from operating activities	**9,088**	(2,457)	n/a	**21,430**	3,181	574%
Net cash flows per share from operating activities - basic *(US$)*	**0.26**	(0.07)	n/a	**0.62**	0.09	578%
Net cash flows per share from operating activities - diluted *(US$)*	**0.26**	(0.07)	n/a	**0.61**	0.09	581%
Outstanding Shares *('000)*						
Class A shares	**1,751**	1,751	0%	**1,751**	1,751	0%
Class B shares	**32,743**	32,939	(1%)	**32,743**	32,939	(1%)
Options	**2,172**	2,807	(23%)	**2,172**	2,807	(23%)
Operating						
Additional Gas sold *(MMcf)* - industrial	**1,022**	719	42%	**2,686**	1,957	37%
Additional Gas sold *(MMcf)* - power	**4,270**	4,442	(4%)	**12,415**	10,201	22%
Additional Gas sold *(MMcfd)* - industrial	**11.1**	7.8	42%	**9.8**	7.2	36%
Additional Gas sold *(MMcfd)* - power	**46.4**	48.3	(4%)	**45.3**	37.4	21%
Additional Gas sold *(MMcfd)* - total	**57.5**	56.1	2%	**55.1**	44.6	24%
Average price per mcf *(US$)* - industrial	**9.21**	10.47	(12%)	**9.62**	10.10	(5%)
Average price per mcf *(US$)* - power	**3.55**	2.76	28%	**3.03**	2.69	13%

HIGHLIGHTS

- Running at the maximum plant and pipeline capacity, the Company delivered Additional Gas sales volumes averaging 57.5 MMcfd for the quarter, up 6% over Q2 (Q3 2011: 56.1 MMcfd).
- A 23% increase in Industrial Gas sales volumes and a 28% increase in Power Gas prices, together with a higher revenue share from cost recovery combined to deliver record funds from operations before working capital changes of US$14.4 million (US$0.41 per share) for the quarter – a 44% increase over Q2 (US$9.9 million or $0.28 per share) and 170% over Q3 2011 ($5.3 million or $0.15 per share).
- Profit after tax for the quarter was down 75% from Q2 to US$1.3 million or US$0.04 per share (Q2 2012: US$5.2 million or US$0.15) a result of writing off US$7.5 million in costs associated with the La Tosca Italy exploration well.
- Working capital at the end of the quarter of $37.7 million including cash of $23.3 million, down 2% and up 15% respectively over Q2, primarily the result of drilling SS-11 offset by the drawdown of US$6.0 million in a new bank financing and the receipt of some TANESCO payments during the quarter.
- Some progress has been made regarding TANESCO payments – the Company received US$13.2 million from the state utility during the quarter and a further US$9.5 million since the end of the quarter. 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 new production well SS-11 was brought onstream 3 October and is currently producing approximately 38 MMcfd of natural gas.
- The SS-9 well, which was producing approximately 30 MMcfd, was planned to be shut in and used only as spare capacity until SS-12 could be drilled. During the quarter, rising casing annulus pressures resulting from a tubing leak dictated that SS-9 be permanently suspended. With a similar rise in casing annulus pressure, a decision was taken to suspend SS-3 to ensure continued safe operations in the field.
- In August, the Government issued an order to redirect all gas volumes to the state utility until 31 December 2012 to aid in emergency power generation. The Company in collaboration with the Government identified a solution which provided TANESCO with sufficient volumes of gas without compromising the Company's Industrial Gas customers.
- Construction has commenced on the pipeline infrastructure expansion project in Tanzania – the government has stated that the 532km pipeline and its associated facilities are expected to be completed and commissioned in 18 months. The Company is developing a plan with TPDC which would double deliverability to 200MMscfd by the time the infrastructure expansion is complete. Any commitments by the Company to proceed are subject to resolution of TANESCO payments, GNT issues, satisfactory commercial arrangements and financing.
- On 1st November 2012, the Government of Tanzania issued a draft natural gas policy for review and consultation among the various stakeholders. The draft policy contemplates a restructuring of TPDC, strategic participation throughout the upstream, midstream and downstream sectors, ownership and control over gas infrastructure and setting domestic natural gas prices. The Company has been asked to submit its views on the draft policy.
- Drilling of the La Tosca well in the Longastrino exploration block in the Po Valley, Northern Italy commenced on 7 August 2012; the well reached total depth on 27 August and has been plugged and abandoned having encountered gas shows. Orca has earned a 70% working interest and, subject to government approval, operatorship of the block. The Company intends to review the technical and drilling data to determine whether or not to continue exploration on the block.

CHAIRMAN & CEO'S LETTER TO THE SHAREHOLDERS

Orca Exploration is encouraged by many positive accomplishments in Q3 2012. This is good news as we continue to navigate our way through the most challenging year in Orca's history. With the commissioning of our new SS-11 well the Songo Songo field has never been in better operational shape from the perspective of wellbore integrity and reliability. We continue to deliver gas at capacity to hungry markets. We posted record financial results in Q3 and we continue to make tangible progress in recovering past due payments from TANESCO.

We are also encouraged that the Government is delivering on the pipeline infrastructure project. The long awaited expansion of pipeline and facilities capacity has begun and we are working to take the Company to the next level in production. Orca is privileged to be playing a key role in meeting Tanzania's near-to-medium term energy strategy objectives.

However we continue to face substantial uncertainties that still need resolution. It is Orca's highest priority to remove those risks that cast a shadow over our operations in Tanzania. To do this we will continue to work closely with the Government towards a full and fair resolution. During the quarter no real progress was made in concluding and documenting the issues agreed in principle with the Government Negotiating Team ("GNT") in July. At that time we had reached an agreement with the GNT on a number of major points to resolve critical issues. Recognising that resolution of these issues is a major impediment to committing to further field development in Tanzania, Orca has asked the Ministry of Energy and Mines ("MEM") to foster the necessary collaboration to resolve these matters and bring them to a conclusion. Based on the progress made to date on TANESCO payments, Orca continues to believe that MEM has the vision and commitment to facilitate a successful completion of the GNT process.

Resolving uncertainties

TANESCO payments are foremost in the minds of our shareholders and management. We are pleased to report that as a result of close collaboration with MEM and new TANESCO management, progress has been made in reducing TANESCO past due accounts. The Company has received US$22.7 million over the past five months and the arrears have been reduced to US$21.7 million. We continue to work closely with the Government towards a full resolution. The Company received US$13.2 million from the state utility during Q3 and a further US$9.5 million since the end of the quarter. At the end of Q3, the TANESCO receivable stood at US$31.2 million (of which US$26.8 million was in arrears), up 5% from US$29.6 million (US$25.6 million in arrears) at the end of Q2.

A viable state utility is a critical component to delivering Tanzania's industrialization and economic growth strategy going forward. An emergency power plan was established a number of years ago as a result of the lack of infrastructure capacity in Tanzania to move additional natural gas to fire much needed power plants. The plan placed TANESCO in the untenable position of having to purchase both high cost independently generated power and large volumes of high cost liquid fuels to generate power without offsetting increases in power prices. There is a cost of service study ongoing by the Tanzanian regulator, EWURA, the result of which is expected to be recommendations to increase power prices in early 2013. Power prices reflecting the real cost of service in the country, together with a changing fuel mix weighted towards natural gas, are expected to restore the state utility to a viable business model by the time the pipeline expansion is commissioned in 2014.

Draft natural gas policy review

On 1 November 2012, the Government of Tanzania issued a draft natural gas policy for review and consultation with stakeholders. The new policy contemplates a restructuring of Tanzania Petroleum Development Corporation ("TPDC") to participate across the upstream, mid-stream and downstream sectors of the industry through a national oil company and to regulate the industry through a new regulatory body.

The Government's stated objective for mid-stream and downstream sector in the draft policy is to promote the development of facilities for natural gas processing, liquefaction, transportation, storage and distribution to ensure reliability of supply. The draft policy contemplates a restructured TPDC acting as a national aggregator of natural gas, owning and managing natural gas infrastructure.

The draft policy does not contemplate market driven gas prices, but rather a government role in establishing "an appropriate pricing structure" which can both encourage economic use of the system capacities and as well provide incentives for promoting investment.

The draft policy also contemplates strategic involvement by the Government in the LNG value chain and the promotion of efficient LNG production as well as management of natural gas revenues, local content, community & social responsibilities and issues of transparency and accountability.

The Oil and Gas Association of Tanzania ("OGAT"), of which Orca is a member, has prepared a submission on behalf of industry on the draft policy. A copy of the draft policy is available on the Company's website. It is possible that the final terms of the draft Natural Gas Policy may vary from the initial draft and the Company is monitoring developments closely as the draft policy as originally proposed could have a significant effect on the Company's business operations.

Financial results

To meet constant high demand, Orca continued to operate at maximum plant and pipeline capacity. The Company delivered Additional Gas sales volumes averaging 57.5 MMcfd for the quarter, up 6% over Q2 (Q3 2011: 56.1 MMcfd). A 23% increase in Industrial Gas sales volumes and a 27% increase in Power Gas prices, together with a higher revenue share from cost recovery, combined to deliver record funds from operations before working capital changes of US$14.4 million (US$0.41 per share) for the quarter. This represents a 44% increase over Q2 (US$9.9 million or US$0.28 per share) and 170% over Q3 2011 (US$5.3 million or US$0.15 per share). Management currently expects the Songo Songo Production Sharing Agreement ("PSA") cost pools to be fully recovered by year end. If the cost pools had been fully recovered at the beginning of the quarter, funds from operations for the quarter would have been approximately US$8.0 million (US$0.23 per share), a result of the higher revenue interest of TPDC in the PSA after cost recovery. Profit after tax for the quarter was down 75% to US$1.3 million or US$0.04 per share over Q2 (Q2 2012: US$5.2 million or US$0.15 per share) as a result of writing off US$7.5 million in costs associated with the La Tosca Italy exploration well.

Average Power Gas sales prices were up over Q2 to US$3.55/Mcf from US$2.80/Mcf, a result of higher prices provided under the Portfolio Gas Sales Agreement with TANESCO. Weaker liquids fuels prices drove a 9% reduction in Industrial Gas sales prices to US$9.21/Mcf from US$10.14/Mcf in Q2.

The Company remains in a strong financial position with working capital at the end of the quarter of US$37.7 million including cash of US$23.3 million, down 2% and up 15% respectively over Q2 2012. The cost of drilling of the SS-11 well was offset by the drawdown of US$6.0 million in bank financing and the receipt of some TANESCO payments during the quarter.

Bank financing

During the quarter, the Company closed a US$10 million secured bridge loan facility with a Tanzania bank to assist in working capital whilst the TANESCO payment issues are being resolved. The facility has a term of 18 months and is to be repaid in equal installments beginning in March 2013. During the quarter, the Company drew US$6.0 million under the facility. Once the TANESCO payments and GNT issues are resolved, the Company will be in a position to proceed with a reserve-backed facility to finance development. Depending on the time required for resolution of these issues, the Company may secure other financing to support its operations.

Tanzania operations

At the end of the quarter Orca brought the SS-11 production well onstream serving to maintain and strengthen deliverability of the Company's Songo Songo gas production. SS-11 was drilled as a directional well from onshore Songo Songo Island and was completed in May 2012. SS-11 is currently producing approximately 38 million cubic feet per day ("MMcfd") of natural gas through a six-inch diameter Technip Coflexip® pipe laid along the seabed to achieve an efficient natural cooling of the gas stream prior to the plant inlet. The installation involved developing innovative solutions to a number of engineering challenges which were met entirely by local Tanzanian contractors and suppliers who delivered the project on budget and in approximately one-third the time of other solutions. The project achieved some significant milestones in Tanzania, including the first offshore heavy lift achieved in East Africa and the first shallow water application of the technically advanced Coflexip® pipe in East Africa.

SS-11 is an important addition to the production wellbore inventory of Songo Songo. The production equipment originally installed in the SS-9, SS-5, SS-4 and SS-3 wells drilled by TPDC between 1976 and 1983 has reached the end of its useful life. The SS-10 well was drilled by the Company in 2007 and is currently producing approximately 40 MMcfd. With SS-11 now onstream Orca has taken the SS-9 well off production and suspended it as planned. It is anticipated that production from the new SS-11 well can be increased to over 40 MMcfd with a debottlenecking of the gas gathering infrastructure, expected to be completed over the next number of months.

The SS-9 well, which was producing approximately 30 MMcfd, was planned to be shut in and used only as spare capacity until SS-12 could be drilled. During the quarter, rising casing annulus pressures resulting from a tubing leak dictated that SS-9 be permanently suspended. In connection with the SS-9 suspension, the Company assessed the integrity of SS-3 and SS-4, which were producing a total of approximately 18 MMcfd. With a similar rise in casing annulus pressure suggesting a tubing leak, a decision was taken to suspend SS-3 to ensure continued safe operations in the field. 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 be, however, no redundant capacity in the facility or pipeline until additional wells can be drilled in the field and facilities expanded.

Plans to drill an additional development well, SS-12, and an appraisal well at Songo Songo West were placed on hold in mid-2012. Until the outstanding TANESCO receivables have been paid and the re-negotiation of certain terms of the Songo Songo Production Sharing Agreement with the Government and related issues arising from the GNT have been fully resolved, Orca will be unable to proceed with drilling either of these wells.

Pipeline construction has commenced

On 8 November, His Excellency Jakaya Kikwete, President of the United Republic of Tanzania, formally commissioned the start of construction of the Mnazi Bay to Dar es Salaam Gas Pipeline Project, which will tie into expanded Songo Songo facilities onshore at Somanga Funga. The Government has stated that the 532km pipeline and its associated facilities are expected to be completed and commissioned in 18 months. This US$1.2 billion infrastructure expansion project is expected to provide Orca with much needed process and pipeline capacity expansion at Songo Songo. The Company had initial technical consultations with the project manager and Songo Songo partner, TPDC, in mid-November. The Company's current objective is to have approximately 200 MMcfd of total gas (approximately 160 MMcfd Additional Gas sales) onstream by the end of 2014 and a field development plan is being prepared for discussion with TPDC. In addition to the outstanding matters of TANESCO payments and GNT issues, the Company has yet to establish any commercial or contractual basis for the processing, transportation or sale of these incremental volumes. All these matters will be required to be resolved prior to our commitment to proceed.

As the Company reported over the past several quarters, power supply is an acute issue for Tanzania aggravated by the lack of rains to fill reservoirs for hydro generation. The Government issued an order in August 2012 to the Company to redirect all gas volumes (including sales to Industrial Gas customers) to TANESCO until 31 December 2012 to aid in emergency power generation. The Company responded immediately and in collaboration with the Government, identified a solution which provided TANESCO with sufficient volumes of gas without compromising the Company's Industrial Gas customers.

Italian operations

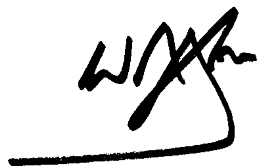
In the Longastrino Block in the Po Valley region of Northern Italy the La Tosca farm-in well was spud on 7 August 2012. It reached total depth of 2,335 metres and was plugged and abandoned in early September having encountered gas shows. The drilling indicated a more limited reservoir sand development than expected from earlier extrapolation of data from nearby wells. The partners concluded that the data did not provide a sufficiently strong economic case to warrant well completion and testing. Total cost of the well to the Company was US$7.5 million, which was written off during the quarter. As a result of the drilling, the Company has earned a 70% working interest and once approved as the new operator, Orca intends to review the technical and drilling data to determine whether to continue exploration on the block.

During the quarter, the Elsa offshore Italy opportunity cleared an important regulatory hurdle. 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 12 August 2012, 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. Petroceltic plc, the operator of the permit has stated that the new legislation removes the existing uncertainty concerning exploration, development and production activities in Italian waters clearing the way for a new application.

Moving forward

Orca remains firmly committed to Tanzania and the development of the country's natural gas resources. In our continued commitment to Tanzania, we are strengthening our in country management team. Shareholders, and in particular those who have been with the Company since its predecessors, will be pleased to know we have appointed David K. Roberts as Orca's Vice President Operations based in Dar es Salaam. From 1999 to 2006 Mr. Roberts was instrumental in managing PanOcean Energy's growth in Gabon from 400 barrels of oil per day ("bpd") to 20,000 bpd.

Against a backdrop of solid operating and financial performance Orca is making tangible progress on the issues that have interrupted the Company's exploration and development program in Tanzania. In the past few months we have demonstrated that Orca and the Government of Tanzania can collaborate successfully in moving towards solutions that are aligned with our common interests. We fully intend to continue on this path and build on this positive working relationship.



W. David Lyons
Chairman & CEO

29 November 2012

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 SPECIFCALLY 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.

ORCA EXPLORATION'S ACTUAL RESULTS, PERFORMANCE OR ACHIEVEMENTS COULD DIFFER MATERIALLY FROM THOSE EXPRESSED IN, OR IMPLIED BY, THESE FORWARD-LOOKING STATEMENTS AND, ACCORDINGLY, NO ASSURANCE CAN BE GIVEN THAT ANY OF THE EVENTS ANTICIPATED BY THE FORWARD-LOOKING STATEMENTS WILL TRANSPIRE OR OCCUR, OR IF ANY OF THEM DO TRANSPIRE OR OCCUR, WHAT BENEFITS ORCA EXPLORATION WILL DERIVE THEREFROM. SUBJECT TO APPLICABLE LAW, ORCA EXPLORATION DISCLAIMS ANY INTENTION OR OBLIGATION TO UPDATE OR REVISE ANY FORWARD-LOOKING STATEMENTS, WHETHER AS A RESULT OF NEW INFORMATION, FUTURE EVENTS OR OTHERWISE. ALL FORWARD-LOOKING STATEMENTS CONTAINED IN THIS DOCUMENT ARE EXPRESSLY QUALIFIED BY THIS CAUTIONARY STATEMENT.

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 CALCUALATED 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 Ubungo, 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
MMcfd	*Bcf*	*%*	*%*
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:

	THREE MONTHS ENDED		NINE MONTHS ENDED	
OPERATING VOLUMES	**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
Total volumes	**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
Total daily sales volume	**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 approximately101 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:

	THREE MONTHS ENDED		NINE MONTHS ENDED	
US$/mcf	**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
Weighted average price	**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:

	THREE MONTHS ENDED		NINE MONTHS ENDED	
Figures in US$'000	**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
Analysed as to:				
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 signficant decrease in Cost Gas until capital spending is resumed.

	THREE MONTHS ENDED		NINE MONTHS ENDED	
Figures in US$'000	**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:

	THREE MONTHS ENDED		NINE MONTHS ENDED	
Figures in US$'000	**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:

	THREE MONTHS ENDED		NINE MONTHS ENDED	
Amounts in US$/mcf	**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:

	THREE MONTHS ENDED		NINE MONTHS ENDED	
Figures in US$'000	**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:

	THREE MONTHS ENDED		NINE MONTHS ENDED	
Figures in US$'000	**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:

	THREE MONTHS ENDED		NINE MONTHS ENDED	
Figures in US$'000	**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).

	THREE MONTHS ENDED		NINE MONTHS ENDED	
Figures in US$'000	**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:

	THREE MONTHS ENDED		NINE MONTHS ENDED	
Figures in US$'000	**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

	AS AT	
Number of shares ('000)	**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:

(Figures in US$'000 except where otherwise stated)	**2012**			2011				2010
	Q3	Q2	Q1	Q4	Q3	Q2	Q1	Q4
FINANCIAL								
Revenue	**22,425**	16,915	17,207	17,500	10,457	8,296	9,640	10,557
Profit/(loss) after taxation	**1,266**	5,167	6,392	5,267	(54)	383	2,390	1,885
Operating netback *(US$/mcf)*	**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 *(US$)*	**0.04**	0.15	0.19	0.15	0.00	0.01	0.07	0.05
Profit/(loss) per share – diluted *(US$)*	**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 *(MMcf)*	**1,022**	829	835	786	719	688	550	687
Additional Gas sold – power *(MMcf)*	**4,270**	4,172	3,973	4,521	4,442	2,965	2,794	2,926
Average price per mcf – industrial *(US$)*	**9.21**	10.14	9.63	9.94	10.47	10.28	9.42	8.67
Average price per mcf – power *(US$)*	**3.55**	2.80	2.72	2.97	2.76	2.64	2.62	2.63

CONDENSED CONSOLIDATED INTERIM STATEMENT OF COMPREHENSIVE INCOME/(LOSS) (unaudited)

(Figures in US$'000 except per share amounts)	NOTE	THREE MONTHS ENDED **30 Sep 2012**	THREE MONTHS ENDED 30 Sep 2011	NINE MONTHS ENDED **30 Sep 2012**	NINE MONTHS ENDED 30 Sep 2011
REVENUE		**22,425**	10,457	**56,545**	28,393
Cost of sales					
Production and distribution expenses		**(1,497)**	(1,800)	**(4,624)**	(4,009)
Depletion expense		**(2,324)**	(2,647)	**(6,279)**	(5,957)
		18,604	6,010	**45,642**	18,427
General and administrative expenses		**(4,391)**	(4,399)	**(12,322)**	(10,736)
Exploration asset impairment	3	**(7,496)**	–	**(7,496)**	–
Net finance costs		**(407)**	(322)	**(689)**	(1,031)
Profit before taxation		**6,310**	1,289	**25,135**	6,660
Taxation	2	**(5,044)**	(1,343)	**(12,310)**	(3,941)
Profit/(loss) after taxation and comprehensive income		**1,266**	(54)	**12,825**	2,719
EARNINGS/(LOSS) PER SHARE					
Basic *(US$)*		**0.04**	(0.00)	**0.37**	0.08
Diluted *(US$)*		**0.04**	(0.00)	**0.36**	0.08

See accompanying notes to the condensed consolidated interim financial statements.

CONDENSED CONSOLIDATED INTERIM STATEMENT OF FINANCIAL POSITION (unaudited)

(Figures in US$'000)	NOTE	AS AT **30 Sep 2012**	 31 Dec 2011
ASSETS			
Current assets			
Cash and cash equivalents		**23,289**	34,680
Trade and other receivables		**62,285**	40,348
Taxation receivable		**15,078**	5,880
Prepayments		**499**	302
		101,151	81,210
Non-current assets			
Exploration and evaluation assets	*3*	**5,451**	2,921
Property, plant and equipment	*4*	**103,383**	67,713
		108,834	70,634
Total assets		**209,985**	151,844
EQUITY AND LIABILITIES			
Current liabilities			
Trade and other payables		**50,753**	22,801
Bank loan	*7*	**5,800**	–
Taxation payable		**6,867**	2,403
		63,420	25,204
Non-current liabilities			
Deferred income taxes	*2*	**19,285**	15,194
Deferred additional profits tax	*2*	**7,076**	4,787
		26,361	19,981
Total liabilities		**89,781**	45,185
EQUITY			
Capital stock	*6*	**84,610**	84,610
Contributed surplus		**6,988**	6,268
Accumulated income		**28,606**	15,781
		120,204	106,659
Total equity and liabilities		**209,985**	151,844

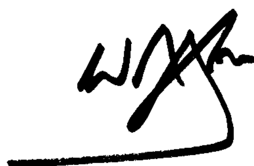
See accompanying notes to the condensed consolidated interim financial statements.

Future operations (Note 1 (d))

Contractual obligations and committed capital investment and contingencies (Note 9)

The condensed consolidated interim financial statements were approved by the Board of Directors on 29 November 2012.

Director



Director

CONDENSED CONSOLIDATED INTERIM STATEMENT OF CASH FLOWS (unaudited)

(Figures in US$'000)	NOTE	THREE MONTHS ENDED **30 Sep 2012**	THREE MONTHS ENDED 30 Sep 2011	NINE MONTHS ENDED **30 Sep 2012**	NINE MONTHS ENDED 30 Sep 2011
CASH FLOWS FROM OPERATING ACTIVITIES					
Profit after taxation		**1,266**	(54)	**12,825**	2,719
Adjustment for:					
Depletion and depreciation	4	**2,393**	2,741	**6,549**	6,142
Exploration assets impairment	3	**7,496**	–	**7,496**	–
Stock-based compensation		**80**	493	**701**	403
Deferred income taxes		**2,019**	718	**4,091**	1,406
Deferred additional profits tax		**900**	1,158	**2,289**	1,946
Interest income		**(2)**	(1)	**(4)**	(5)
Unrealised foreign exchange loss		**227**	268	**303**	951
		14,379	5,323	**34,250**	13,561
(Increase) in trade and other receivables		**(11,086)**	(8,802)	**(22,577)**	(14,120)
(Increase)/decrease in taxation receivable		**(2,293)**	559	**(9,198)**	(57)
(Increase)/decrease in prepayments		**342**	278	**(197)**	(102)
Increase in trade and other payables		**7,653**	779	**14,688**	4,582
Increase in taxation payable		**93**	(594)	**4,464**	(684)
Net cash flows from operating activities		**9,088**	(2,457)	**21,430**	3,181
CASH FLOWS USED IN INVESTING ACTIVITIES					
Exploration and evaluation expenditures		**(5,469)**	(1,016)	**(10,026)**	(1,554)
Property, plant and equipment expenditures		**(9,564)**	(2,909)	**(42,219)**	(5,320)
Interest received		**2**	1	**4**	5
Proceeds from sale of vehicle		**–**	–	**–**	5
Increase in trade and other payables		**3,413**	152	**13,817**	1,012
Net cash used in investing activities		**(11,618)**	(3,772)	**(38,424)**	(5,852)
CASH FLOWS FROM FINANCING ACTIVITIES					
Bank loan proceeds		**5,800**	–	**5,800**	–
Net cash from financing activities		**5,800**	–	**5,800**	–
Increase in cash and cash equivalents		**3,270**	(6,229)	**(11,194)**	(2,671)
Cash and cash equivalents at the beginning of the period		**20,194**	48,993	**34,680**	45,519
Effect of change in foreign exchange		**(175)**	(132)	**(197)**	(216)
Cash and cash equivalents at the end of the period		**23,289**	42,632	**23,289**	42,632

See accompanying notes to the condensed consolidated interim financial statements.

CONDENSED CONSOLIDATED INTERIM STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY (unaudited)

(US'000)	CAPITAL STOCK	CONTRIBUTED SURPLUS	ACCUMULATED INCOME	TOTAL
Balance as at 1 January 2011	85,100	5,288	7,795	98,183
Stock based compensation	–	661	–	661
Total comprehensive income for the period	–	–	2,719	2,719
Balance as at 30 September 2011	**85,100**	**5,949**	**10,514**	**101,563**

(US'000)	CAPITAL STOCK	CONTRIBUTED SURPLUS	ACCUMULATED INCOME	TOTAL
Note	*6*			
Balance as at 1 January 2012	84,610	6,268	15,781	106,659
Stock based compensation	–	720	–	720
Total comprehensive income for the period	–	–	12,825	12,825
Balance as at 30 September 2012	**84,610**	**6,988**	**28,606**	**120,204**

See accompanying notes to the condensed consolidated interim financial statements.

General Information

Orca Exploration Group Inc ("Orca Exploration " or the "Company") was incorporated on 28 April 2004 under the laws of the British Virgin Islands. The Company is a participant in a gas-to-electricity project in Tanzania and has gas and oil exploration interests in Italy. The condensed consolidated interim financial statements of the Company as at and for the three and nine months ended 30 September 2012 comprise accounts of the Company and all its wholly owned subsidiaries (collectively, the "Company").

1 BASIS OF PREPARATION

(a) Statement of Compliance

These condensed consolidated interim financial statements of the Company, have been prepared in accordance with IAS 34 Interim Financial Reporting and do not include all of the information required for the full annual financial statements prepared in accordance with International Financial Reporting Standards as issued by the IASB. Selected explanatory notes are included to explain events and transactions that are significant to an understanding of the changes in financial position and performance of the Company and should be read in conjunction with the consolidated financial statements and notes thereto in the Company's 2011 annual report. These condensed consolidated interim financial statements were approved by the Board of Directors on 29 November 2012.

(b) Judgements and estimates

The preparation of these condensed consolidated interim financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, income and expenses. Actual results could differ from these estimates.

In preparing these condensed consolidated interim financial statements, the significant judgements made by the management in applying the Company's accounting policies and the key sources of estimation uncertainty were the same as those applied to the consolidated financial statements as at and for the year ended 31 December 2011.

(c) Significant accounting policies

The same accounting policies have been applied in the preparation of these condensed consolidated interim financial statements as those applied by the Company in its consolidated financial statements as at and for the year ended 31 December 2011.

(d) Future operations

The Company generates in excess of 50% of its operating revenue from sales to the power sector companies, Songas Limited ("Songas") and TANESCO. Songas' financial security is heavily reliant on the payment of capacity and energy charges by TANESCO. The state utility 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$17.8 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 2012 the Company had drawn down US$6.0 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 issues associated with the Government Negotiating Team ("GNT"), 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.

2 TAXATION

Under the terms of the Production Sharing Agreement with the Tanzania Petroleum Development Corporation ("TPDC"), the Company is liable to pay income tax at the corporate rate of 30% on profits generated in Tanzania. During the nine months ended 30 September 2012 the Company has paid US$1.4 million. The amount paid is recovered in full from TPDC by adjusting their share of profit gas.

The tax charge is as follows:

	THREE MONTHS ENDED		NINE MONTHS ENDED	
Figures in US$'000	**30 Sep 2012**	30 Sep 2011	**30 Sep 2012**	30 Sep 2011
Current tax	**3,026**	625	**8,221**	2,535
Deferred tax	**2,018**	718	**4,089**	1,406
	5,044	1,343	**12,310**	3,941

TAX RATE RECONCILIATION

	THREE MONTHS ENDED		NINE MONTHS ENDED	
Figures in US$'000	**30 Sep 2012**	30 Sep 2011	**30 Sep 2012**	30 Sep 2011
Profit before taxation	**6,310**	1,289	**25,136**	6,660
Provision for income tax calculated at the statutory rate of 30%	**1,893**	387	**7,541**	1,998
Add/(deduct) the tax effect of non-deductible income tax items:				
Administrative and operating expenses	**610**	591	**1,892**	1,559
Stock- based compensation	**24**	148	**209**	1,121
Financing charge	**–**	23	**29**	7
Exploration assets impairment	**2,248**	–	**2,248**	–
Permanent differences	**269**	194	**391**	256
	5,044	1,343	**12,310**	3,941

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. Accordingly a deferred tax liability has been recognized for the quarter ended 30 September 2012. The deferred income tax liability includes the following temporary differences:

	AS AT	
Figures in US$'000	**30 Sep 2012**	31 Dec 2011
Differences between tax base and carrying value of property, plant and equipment	**15,961**	14,409
Income tax recoverable	**5,580**	2,416
Other liabilities		
Employee bonuses	**(60)**	(145)
TPDC Additional Profit Gas	**(73)**	(50)
Additional profits tax	**(2,123)**	(1,436)
	19,285	15,194

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, 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 license. The effective APT rate of 31.8% (Q3 2011 20%) is then applied to Profit Gas of US$2.6 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$1.9 million for 2012 and 2011 respectively.

3 Exploration and evaluation assets

Figures in US'000	Italy	Tanzania	Total
COSTS			
As at 1 January 2012	911	2,010	2,921
Additions	6,585	3,441	10,026
Impairment	(7,496)	–	(7,496)
As at 30 September 2012	**–**	**5,451**	**5,451**
NET BOOK VALUES			
As at 30 September 2012	–	5,451	5,451
As at 31 December 2011	911	2,010	2,921

TANZANIA

The exploration and evaluation additions of US$3.4 million for the nine months to 30 September, relates to an offshore site survey conducted in preparation for the drilling of the Songo Songo West prospect to evaluate the field, which is pending determination of proven and probable reserves.

ITALY

Pursuant to the terms of the Company's Longastrino Block farm-in in the Po Valley Basin the Company spent US$6.6 million during 2012 related to the drilling of the La Tosca exploration well. The well was unsuccessful and the related accumulated costs of US$7.5 million were impaired in the period ended 30 September 2012.

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

4 Property, plant and equipment

Figures in US$'000	Natural gas properties	Leasehold improvements	Computer equipment	Vehicles	Fixtures & Fittings	Total
COSTS						
As at 1 January 2012	96,014	320	701	249	334	97,618
Additions	42,112	–	36	–	71	42,219
As at 30 September 2012	**138,126**	**320**	**737**	**249**	**405**	**139,837**
DEPLETION/DEPRECIATION						
As at 1 January 2012	28,833	271	520	196	85	29,905
Depletion and depreciation for the period	6,279	20	121	35	94	6,549
As at 30 September 2012	**35,112**	**291**	**641**	**231**	**179**	**36,454**
NET BOOK VALUES						
As at 30 September 2012	**103,014**	**29**	**96**	**18**	**226**	**103,383**
As at 31 December 2011	67,181	49	181	53	249	67,713

The increase in natural gas properties is primarily due to the drilling of a new production well SS-11 in Tanzania and the tie-in of the well to the processing plant - Q3 US$9.7 million and nine months ended 30 September 2012 US$41.4 million. The total cost of the SS-11 well which came on stream 3 October, including its connection to the gas processing plant, was US$45 million.

In determining the depletion charge, it is estimated by the independent reserve engineers that future development costs of US$79.3 million (Q3 2011: US$113.0 million) will be required to bring the total proved reserves to production.

5 **Segment Information**

The Company has one reportable segment which is international exploration, development and production of petroleum and natural gas. The Company currently has producing assets in Tanzania and exploration interests in Italy.

	THREE MONTHS ENDED OR AS AT			THREE MONTHS ENDED OR AS AT		
	30 September 2012			30 September 2011		
Figures in US$'000	Tanzania	Italy	Total	Tanzania	Italy	Total
External Revenue	22,425	–	22,425	10,457	–	10,457
Segment Income/(Loss)	8,762	(7,496)	1,266	(54)	–	(54)
Total Assets	209,985	–	209,985	135,707	–	135,707
Total Liabilities	89,781	–	89,781	34,144	–	34,144
Capital additions	10,046	4,987	15,033	3,123	802	3,925
Depletion & depreciation	2,393	–	2,393	2,741	–	2,741
Exploration assets impairment	–	(7,496)	(7,496)	–	–	–

	NINE MONTHS ENDED OR AS AT			NINE MONTHS ENDED OR AS AT		
	30 September 2012			30 September 2011		
Figures in US$'000	Tanzania	Italy	Total	Tanzania	Italy	Total
External Revenue	56,545	–	56,545	28,393	–	28,393
Segment Income/(Loss)	20,321	(7,496)	12,825	2,719	–	2,719
Total Assets	209,985	–	209,985	135,707	–	135,707
Total Liabilities	89,781	–	89,781	34,144	–	34,144
Capital additions	45,660	6,585	52,245	6,072	802	6,874
Depletion & depreciation	6,549	–	6,549	6,147	–	6,147
Exploration assets impairment	–	(7,496)	(7,496)	–	–	–

6 Capital stock

Authorized and Issued Share Capital

Thousands of shares (thousands)	Authorised	Issued	Amount *US$'000*
CLASS A			
As at 1 January 2012 and 30 September 2012	**50,000**	**1,751**	**$ 983**
CLASS B			
As at 1 January 2012 and 30 September 2012	**100,000**	**32,743**	**$ 83,627**
FIRST PREFERENCE			
As at 30 September 2012	**100,000**	**–**	**–**
Total Class A, Class B and First Preference shares As at 30 September 2012	**250,000**	**34,494**	**$ 84,610**

All of the issued capital stock is fully paid.

Stock options

The table below details the outstanding share options and the movements for the period ended 30 September 2012:

STOCK OPTIONS

Thousands of options or CDN$	Options	Exercise Price *(CDN$)*
Outstanding as at 1 January 2012	3,057	1.00 to 13.55
Issued	400	3.18
Expired	(535)	8.00 to 13.55
Forfeited	(750)	4.75 to 13.55
Outstanding as at 30 September 2012	2,172	1.00 to 12.00

The weighted average remaining life and weighted average exercise price of options at 30 September 2012 were as follows:

Exercise Price *(CDN$)*	Number outstanding as at 30 Sep 2012 *('000)*	Weighted Average Remaining Contractual Life *(years)*	Number Exercisable as at 30 Sep 2012 *('000)*	Weighted Average Exercise Price *(CDN$)*
1.00	1,422	1.92	1,422	1.00
3.18	400	5.25	–	3.18
3.60	250	4.01	250	3.60
12.00	100	0.10	100	11.36
	2,172		1,772	

STOCK APPRECIATION RIGHTS

Thousands of stock appreciation rights or CDN$	Options	Exercise Price
Outstanding as at 1 January 2012 (i)/(ii)	405	4.20 to 13.55
Issued (iii)	100	2.70
Expired	(90)	13.55
Outstanding as at 30 September 2012	415	4.20 to 13.55

(i) A total of 300,000 stock appreciation rights were issued in June 2010 with an exercise price of CDN$4.20. These rights have a term of five years and vest in five equal instalments, the first fifth vesting on the anniversary of the grant date. There is no maximum liability associated with these rights.

(ii) A total of 15,000 stock appreciation rights have a term of five years. All of these options vested over a period of three years and are now fully vested. There is no maximum liability associated with these rights.

(iii) A total of 100,000 stock appreciation rights have a term of five years. These rights were granted in August 2012 and will vest over a period of three years. There is no maximum liability associated with these rights.

The Company records a charge to the income statement using the Black-Scholes fair valuation option pricing model every reporting period with a resulting liability being recognised in the statement of financial position. In the valuation of these stock appreciation rights at the reporting date, the following assumptions have been made: a risk free rate of interest of 1.50%, stock volatility of 53% to 70%, 0% dividend yield 0% forfeiture and a closing stock price of CDN$2.80 per share.

As at 30 September 2012, a total accrued liability of US$0.2 million (Q3 2011: US$0.4 million) has been recognised in relation to the stock appreciation rights. The liability having increased by US$0.1 million during the period as a result in an overall increase in the valuation of the stock appreciation rights, a reduction of US$0.2 million having been recorded in Q3 2011.

Shareholders' Equity and Outstanding Share Data

	AS AT	
Number of shares ('000)	**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	**927**	1,176
Weighted average diluted Class A and Class B shares	**35,421**	35,832

7 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 2012 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.

8 Related party transactions

One of the non executive directors is a partner at a law firm. During the quarter, the Company incurred US$50 (Q3 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.

9 Contractual obligations, committed capital investments and contingencies

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, 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 and 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 31 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

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 the Ministry of Energy and Minerals ("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.

Power generation

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.

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 that they 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 extensive 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.

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David W. Ross
Non-Executive Director
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William H. Smith
Non-Executive Director
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Robert S. Wynne
Chief Financial Officer
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Canada

Officers

W. David Lyons
Chairman and
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