

TWOCO PETROLEUMS LTD.
CONDENSED INTERIM FINANCIAL STATEMENTS

For the three and nine months ended September 30, 2011 and 2010
(Unaudited – Prepared by Management)

Notice of No Auditor Review of Condensed Interim Financial Statements

In accordance with National Instrument 51-102 released by the Canadian Securities Administrators, the Company discloses that its auditors have not reviewed these unaudited condensed interim financial statements as at and for the three and nine months ended September 30, 2011 and 2010.

TWOCO PETROLEUMS LTD.
CONDENSED INTERIM STATEMENTS OF FINANCIAL POSITION

Unaudited
(Canadian dollars)

	September 30 2011	December 31 2010
Assets		(Note 22)
Current assets		
Cash	\$ 858,332	\$ 2,432,961
Trade and other receivables	881,889	675,100
Prepaid expenses and deposits	142,227	252,175
	1,882,448	3,360,236
Exploration and evaluation assets (Note 6)	3,011,931	3,128,241
Property, plant and equipment (Note 7)	23,806,149	21,395,815
	\$ 28,700,528	\$ 27,884,292
Liabilities and Shareholders' Equity		
Current liabilities		
Bank debt (Note 8)	\$ 18,197,917	\$ 18,291,667
Trade and other payables	1,537,939	2,407,607
Unsecured debentures (Note 10)	–	2,746,791
Flow-through share premium (Note 12(b))	39,780	313,900
	19,775,636	23,759,965
Convertible debentures (Note 9)	3,232,769	–
Decommissioning liability (Note 11)	4,740,567	4,412,261
	27,748,972	28,172,226
Shareholders' (deficit) equity		
Share capital (Note 12)	33,401,764	30,245,270
Warrants (Note 13)	586,041	606,791
Equity component of convertible debentures (Note 9)	175,540	–
Contributed surplus	2,001,714	1,580,324
Deficit	(35,213,503)	(32,720,319)
	951,556	(287,934)
	\$ 28,700,528	\$ 27,884,292
Going concern (Note 1)		
Commitments (Note 19)		
Subsequent event (Note 20)		

See the accompanying notes to these condensed interim financial statements.

TWOCO PETROLEUMS LTD.
CONDENSED INTERIM STATEMENTS OF LOSS AND COMPREHENSIVE LOSS
Unaudited
(Canadian dollars)

	For the three months ended September 30		For the nine months ended September 30	
	2011	2010	2011	2010
				(Note 22)
Revenue				
Oil and other natural gas revenue	\$ 1,434,310	\$ 1,155,924	\$ 4,177,433	\$ 4,378,408
Royalties, net of recoveries	(53,435)	(20,724)	(118,594)	209,491
	1,380,875	1,135,200	4,058,839	4,587,899
Expenses				
Production and operating	692,449	531,806	2,013,627	1,842,709
General and administrative	135,444	306,552	583,857	792,669
Depletion and depreciation	646,415	1,339,050	2,241,737	4,764,645
Stock-based compensation (Note 15)	98,749	500	293,027	1,500
	1,573,057	2,177,908	5,132,248	7,401,523
Loss from operating activities	(192,182)	(1,042,708)	(1,073,409)	(2,813,624)
Finance income	4,723	10,455	14,135	10,544
Finance expense	(438,831)	(625,021)	(1,728,557)	(2,028,595)
Net finance expense (Note 5)	(434,108)	(614,566)	(1,714,422)	(2,018,051)
Loss before income tax	(626,290)	(1,657,274)	(2,787,831)	(4,831,675)
Deferred income tax (provision) recovery	–	(178,500)	294,647	(178,500)
Net loss and comprehensive loss	\$ (626,290)	\$ (1,835,774)	\$ (2,493,184)	\$ (5,010,175)
Net loss per share (Note 16)	(0.01)	(0.07)	\$ (0.04)	\$ (0.26)

See the accompanying notes to these condensed interim financial statements.

TWOCO PETROLEUMS LTD.
CONDENSED INTERIM STATEMENTS OF CHANGES IN EQUITY

Unaudited
(Canadian dollars)

	Number of Shares	Share Capital	Equity Component of Convertible Debentures	Warrants	Contributed Surplus	Deficit	Total Shareholders' Equity (Deficit)
Balance at December 31, 2010 (Note 22)	58,625,108	\$ 30,245,270	\$ –	\$ 606,791	\$ 1,580,324	\$ (32,720,319)	\$ (287,934)
Issuance of common shares, net of share issue costs	13,102,987	3,156,494	–	–	107,613	–	3,264,107
Expiry of warrants	–	–	–	(20,750)	20,750	–	–
Issue of convertible debentures, net of tax effect	–	–	175,540	–	–	–	175,540
Stock-based compensation	–	–	–	–	293,027	–	293,027
Total comprehensive loss	–	–	–	–	–	(2,493,184)	(2,493,184)
Balance at September 30, 2011	71,728,095	\$ 33,401,764	\$ 175,540	\$ 586,041	\$ 2,001,714	\$ (35,213,503)	\$ 951,556

	Number of Shares	Share Capital	Equity Component of Convertible Debentures	Warrants	Contributed Surplus	Deficit	Total Shareholders' Equity
Balance at January 1, 2010 (Note 22)	14,941,406	\$ 21,258,648	\$ –	\$ 20,750	\$ 1,043,960	\$ (12,839,442)	\$ 9,483,916
Issuance of common shares, net of share issue costs	43,683,702	9,023,511	–	464,780	111,237	–	9,599,528
Stock-based compensation	–	–	–	–	1,500	–	1,500
Total comprehensive loss	–	–	–	–	–	(5,010,175)	(5,010,175)
Balance at September 30, 2010	58,625,108	\$ 30,282,159	\$ –	\$ 485,530	\$ 1,156,697	\$ (17,849,617)	\$ 14,074,769

See the accompanying notes to these condensed interim financial statements.

TWOCO PETROLEUMS LTD.
CONDENSED INTERIM STATEMENTS OF CASH FLOWS

Unaudited
(Canadian dollars)

	For the three months ended September 30		For the nine months ended September 30	
	2011	2010	2011	2010
				(Note 22)
Cash flows from operating activities				
Net loss	\$ (626,290)	\$ (1,835,774)	\$ (2,493,184)	\$ (5,010,175)
Add back (deduct) non-cash items:				
Depletion and depreciation	646,415	1,339,050	2,241,737	4,764,645
Stock-based compensation	98,749	500	293,027	1,500
Finance expense	438,831	625,021	1,728,557	1,814,845
Deferred tax provision (recovery)	–	178,500	(294,647)	178,500
Interest paid	(308,909)	(331,258)	(1,059,480)	(1,406,417)
Change in non-cash working capital (Note 17)	(180,851)	62,584	(390,841)	390,705
	67,945	38,623	25,169	733,603
Cash flows from financing activities				
Issuance of common shares, net of costs	(463)	3,978,356	2,739,751	3,978,856
Issue of convertible debentures	–	–	3,000,000	–
Settlement of unsecured debentures	–	–	(2,380,000)	–
(Repayment) advances of bank debt	(31,250)	207,601	(93,750)	6,225
	(31,713)	4,185,957	3,266,001	3,985,081
Cash flows from investing activities				
Exploration and evaluation expenditures	(33,647)	(15,521)	(1,724,322)	(94,660)
Property, plant and equipment expenditures	(1,645,336)	(127,521)	(2,565,809)	(661,399)
Change in non-cash working capital (Note 17)	(981,555)	(10,663)	(575,668)	108,250
	(2,660,538)	(153,705)	(4,865,799)	(647,809)
Change in cash	(2,624,306)	4,070,875	(1,574,629)	4,070,875
Cash, beginning of period	3,482,638	–	2,432,961	–
Cash, end of period	\$ 858,332	\$ 4,070,875	\$ 858,332	\$ 4,070,875

See the accompanying notes to these condensed interim financial statements.

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NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS
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(Canadian dollars)

1. REPORTING ENTITY AND GOING CONCERN:

Twoco Petroleum Ltd. (the "Company") was incorporated on September 21, 2000 under the Business Corporations Act (Alberta). The Company's principal business activity is the exploration, production and development of oil and natural gas in Western Canada. The Company's registered address is at 2000, 645 – 7th Avenue SW, Calgary, Alberta, T2P 4G8.

These condensed interim financial statements have been prepared on a going concern basis which contemplates the realization of assets and the payment of liabilities in the ordinary course of business. As at September 30, 2011, the Company had a working capital deficiency of \$17,893,188 (December 31, 2010 – \$20,399,729) and an accumulated deficit of \$35,213,503 (December 31, 2010 – \$32,720,319). During the nine months ended September 30, 2011, the Company incurred a net loss of \$2,493,184 and generated positive cash flow from operating activities before changes in non-cash working capital items.

Management has been working on certain strategic alternatives including, but not limited to, recapitalizing the Company through financing arrangements or merging with other companies. In March 2011, the Company issued convertible debentures for gross proceeds of \$3.4 million (Note 9). In April 2011, the Company completed a private placement equity financing for gross proceeds of \$3 million (Note 12). The Company continues to require the support of its lender (Note 8) and may require additional financing in order to address and resolve the Company's liquidity issues. There is no assurance, however, that additional funding will be available, if and when needed, and as such there is significant doubt about the Company's ability to continue as a going concern. Should the Company be unable to continue as a going concern, it may be unable to realize the carrying value of its assets and to meet its liabilities as they become due. The Company's ability to continue as a going concern is dependent upon its ability to attain profitable operations and generate funds therefrom, its ability to continue to obtain capital financing from investors sufficient to meet current and future obligations, and the continued support of lenders and creditors.

2. BASIS OF PREPARATION:

(a) Statement of compliance:

These condensed interim financial statements have been prepared in accordance with International Accounting Standard 34 Interim Financial Reporting ("IAS 34") as issued by the International Accounting Standards Board.

These condensed interim financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") and interpretations of the International Financial Reporting Interpretations Committee that are expected to be effective as at and for the year ending December 31, 2011, the date of the Company's first annual reporting under IFRS. Accordingly, the accounting policies for the annual period that are relevant to these condensed interim financial statements will be determined only when the first IFRS annual financial statements are prepared for the year ending December 31, 2011

The condensed interim financial statements were authorized for issue by the Board of Directors on November 24, 2011.

(b) Basis of presentation:

The preparation of condensed interim financial statements in conformity with IAS 34 requires

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management to make judgments, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. Actual results may differ from these estimates. These condensed interim financial statements include all of the information required for first-time adoption of IFRS.

The preparation of these condensed interim financial statements resulted in changes to the accounting policies as compared with the most recent annual financial statements prepared under Canadian Generally Accepted Accounting Principles ("GAAP"). The accounting policies referred to in Note 3 have been applied consistently to all periods presented in these condensed interim financial statements. They also have been applied in preparing an opening IFRS statement of financial position as at January 1, 2010 for the purposes of the transition to IFRS, as required by IFRS 1 First Time Adoption of International Financial Reporting Standards ("IFRS 1"). The impact of the transition from GAAP to IFRS is explained in Note 22.

(c) Basis of measurement:

The financial statements have been prepared on the historical cost basis.

(d) Functional and presentation currency:

These financial statements are presented in Canadian dollars, which is the Company's functional currency.

(e) Use of estimates and judgments:

The preparation of financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the year in which the estimates are revised and in any future years affected.

Information about significant areas of estimation uncertainty and critical judgments in applying accounting policies that have the most significant effect on the amounts recognized in the financial statements is included in the following notes:

- Note 4 – determination of fair values
- Note 6 – valuation of exploration and evaluation assets
- Note 7 – valuation of property, plant and equipment
- Note 9 – valuation of convertible debentures
- Note 11 – valuation of decommissioning liability
- Note 13 – valuation of warrants
- Note 15 – measurement of share-based payments

In the process of applying the Company's accounting policies, management has made the following judgments, apart from those involving estimates, which may have the most significant effect on the amounts recognized in the financial statements.

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(i) Exploration and evaluation assets:

Costs incurred to acquire rights to explore for oil and natural gas may be grouped as either exploration and evaluation ("E&E") assets or development and production ("D&P") assets, depending on facts and circumstances.

Costs incurred in respect of properties that are in close proximity to existing or established D&P properties (either of the Company or another industry participant), are classified as D&P properties. In such circumstances, technical feasibility and commercial viability are considered to be established.

Costs incurred in respect of new prospects with no nearby established development past or present are classified as E&E assets.

(ii) Determination of cash generating units:

When the Company establishes technical feasibility and commercial viability of its properties, management will evaluate the oil and gas properties and group them into cash generating units ("CGUs") on the basis of their ability to generate independent cash flows, similar reserve characteristics, geographical location, and shared infrastructure.

(iii) Impairment indicators and calculation of impairment:

At each reporting date, the Company assesses whether or not there are circumstances that indicate a possibility that the carrying values of exploration and evaluation assets and property, plant and equipment are not recoverable, or impaired. Such circumstances include incidents of physical damage, deterioration of commodity prices, changes in the regulatory environment, or a reduction in estimates of proved and probable reserves. When management judges that circumstances clearly indicate impairment, property, plant and equipment are tested for impairment by comparing the carrying values to their recoverable amounts. The recoverable amounts of CGUs are determined based on the higher of value-in-use calculations and fair values less costs to sell. These calculations require the use of estimates and assumptions, including the discount rate applied.

(iv) Decommissioning liability:

Dismantling, decommissioning and site disturbance re-mediation costs will be incurred by the Company at the end of the operating life of some of the Company's facilities and properties. The ultimate decommissioning liability is uncertain and can vary in response to many factors including changes to relevant legal requirements, the emergence of new restoration techniques, experience at other production sites, or changes in the risk-free discount rate. The expected timing and amount of expenditure can also change in response to changes in reserves or changes in laws and regulations or their interpretation. As a result, there could be significant adjustments to the provisions established which would affect future financial results.

(v) Income taxes:

The Company recognizes deferred income tax assets to the extent that it is probable that taxable profit will be available to allow the benefit of that deferred income tax asset to be utilized. Assessing the recoverability of deferred income tax assets requires the Company to make significant estimates related to expectations of future taxable income. Estimates of future taxable income are based on forecast cash flows from operations and the application of existing tax laws. To the extent that future cash flows and taxable income differ significantly from

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estimates, the ability of the Company to realize the deferred income tax assets recorded at the reporting date could be impacted. Additionally, future changes in tax laws in the jurisdictions in which the Company operates could limit the ability of the Company to obtain tax deductions in future periods.

(vi) Contingencies:

By their nature, contingencies will only be resolved when one or more future events occur or fail to occur. The assessment of contingencies inherently involves the exercise of significant judgment and estimates of the outcome of future events.

3. SIGNIFICANT ACCOUNTING POLICIES:

The accounting policies followed in these unaudited condensed interim financial statements are the same as those applied in the Company's unaudited condensed interim financial statements for the period ended March 31, 2011. The Company has consistently applied the same accounting policies throughout all periods presented, as if these policies had always been in effect.

(a) New standards and interpretations adopted:

Accounting standards effective for periods beginning on or after January 1, 2011 have been adopted as part of the transition to IFRS.

(b) New standards and interpretations not yet adopted:

As of January 1, 2013, the Company will be required to adopt IFRS 9, "Financial Instruments", as the first phase of the IASB's project to replace IAS 39, "Financial Instruments: Recognition and Measurement". The new standard replaces the current multiple classification and measurement models for financial assets and liabilities with a single model that has only two classification categories: amortized cost and fair value. The adoption of this standard should not have a material impact on the Company's financial statements.

In May 2011, the IASB issued the following standards which have not yet been adopted by the Company: IFRS 10 Consolidated Financial Statements (IFRS 10), IFRS 11 Joint Arrangements (IFRS 11), IFRS 12 Disclosure of Interests in Other Entities (IFRS 12), IAS 27 Separate Financial Statements (IAS 27), IFRS 13 Fair Value Measurement (IFRS 13) and amended IAS 28 Investments in Associates and Joint Ventures (IAS 28). Each of the new standards is effective for annual periods beginning on or after January 1, 2013 with early adoption permitted. The Company has not yet begun the process of assessing the impact that the new and amended standards will have on its financial statements or whether to early adopt any of the new requirements.

4. DETERMINATION OF FAIR VALUES:

A number of the Company's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes based on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

(a) Property, plant and equipment and E&E assets:

Estimates of recoverable quantities of proved and probable reserves include judgmental

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assumptions regarding commodity prices, exchange rates, discount rates and production and transportation costs for future cash flows. It also requires interpretation of complex geological and geophysical models in order to make an assessment of the size, shape, depth and quality of reservoirs, and their anticipated recoveries. The economic, geological and technical factors used to estimate reserves may change from period to period. Changes in reported reserves can impact asset carrying values, the provision for decommissioning liabilities and the recognition of deferred tax assets, due to changes in expected future cash flows. Reserve estimates are prepared in accordance with the Canadian Oil and Gas Evaluation Handbook and are reviewed by third party reservoir engineers.

The Company makes judgments in determining its CGUs and evaluates the geography, geology, production profile and infrastructure of its assets in making such determinations, which are based on estimates of reserves. Based on this assessment, the Company's CGUs are generally composed of significant development areas. The Company reviews the composition of its CGUs at each reporting date to assess whether any changes are required in light of new facts and circumstances. The amounts recorded for depletion and depreciation of property and equipment, the provision for decommissioning liabilities, and the valuation of property and equipment are based on estimates of proved and probable reserves, production rates, future petroleum and natural gas prices, future costs and the remaining lives and period of future benefit of the related assets. Amounts recorded from joint venture partners are based on the Company's interpretation of underlying agreements and may be subject to joint approval. The Company has recorded balances due from its joint venture partners based on costs incurred and its interpretation of allowable expenditures. Any adjustment required as a result of joint venture audits are recorded in the period of settlement with joint venture partners.

(b) Trade and other receivables, deposits, bank debt and trade and other payables:

The fair value of trade and other receivables, deposits, bank debt and trade and other payables is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date. At September 30, 2011 and December 31, 2010, the fair value of these balances approximated their carrying value due to their short term to maturity.

(c) Convertible debentures:

The fair value of the convertible debentures is based on the discounted present value of future cash flows. The carrying value includes the debt and equity portion of the convertible debentures and excludes the deferred income tax impact of the debentures charged against the equity portion.

(d) Stock options and warrants:

The fair values of stock options and warrants are measured using a Black-Scholes option pricing model. Measurement inputs include share price on measurement date, exercise price of the instrument, expected forfeiture rate (based on historic forfeitures), expected volatility (based on weighted average historic volatility adjusted for changes expected due to publicly available information), weighted average expected life of the instruments (based on historical experience and general option holder behaviour), expected dividends, and the risk-free interest rate (based on government bonds).

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The Black-Scholes pricing model calculations for the nine months ended September 30, 2011 and the year ended December 31, 2010 were based on the following significant assumptions:

	September 30, 2011	December 31, 2010
Risk-free interest rate	1.7%	1.26% – 2.41%
Expected forfeitures	0%	0%
Expected volatility	111%	50% – 135%
Expected life	1.5 years	2 – 5 years
Dividends	nil	nil

(e) Fair value measurement information:

The carrying value of cash, trade and other receivables, deposits, bank debt and trade and other payables included in the statement of financial position approximate fair value due to the short term nature of those instruments.

The reported amount for convertible debentures is based on a Level 2 fair value measurement.

Level 1 fair value measurements are based on unadjusted quoted market prices.

Level 2 fair value measurements are based on valuation models and techniques where the significant inputs are derived from quoted indices.

Level 3 fair value measurements are based on unobservable information.

5. FINANCE INCOME AND EXPENSES:

	Three months ended September 30		Nine months ended September 30	
	2011	2010	2011	2010
Finance income:				
Interest income on bank deposit accounts	\$ 4,723	\$ 10,455	\$ 14,135	\$ 10,544
Finance expenses:				
Interest on bank debt	308,909	304,652	1,317,769	942,643
Interest on debentures	68,559	287,071	251,421	986,773
Accretion of debentures	33,592	2,593	69,413	7,781
Income Tax Act Part XII.6 interest	–	–	7,278	–
Accretion of decommissioning liability	27,771	30,705	82,676	91,398
	<u>438,831</u>	<u>625,021</u>	<u>1,728,557</u>	<u>2,028,595</u>
Net finance expense	\$ (434,108)	\$ (614,566)	\$ (1,714,422)	\$ (2,018,051)

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6. EXPLORATION AND EVALUATION ASSETS:

As at January 1, 2010	\$	6,127,494
Expenditures		113,959
Undeveloped land expiries		<u>(3,113,212)</u>
As at December 31, 2010		3,128,241
Expenditures		1,724,322
Transfers to development and production assets		(1,635,586)
Undeveloped land expiries		<u>(205,046)</u>
As at September 30, 2011	\$	<u>3,011,931</u>

Undeveloped land expiries are included in depletion and depreciation expense in the statement of loss.

7. PROPERTY, PLANT AND EQUIPMENT:

	Furniture and office equipment	Development and production assets	Total
Cost or deemed cost			
As at January 1, 2010	\$ 207,295	\$ 33,959,200	\$ 34,166,495
Cash expenditures	10,185	2,681,996	2,692,181
Decommissioning revisions	–	(83,892)	(83,892)
As at December 31, 2010	217,480	36,557,304	36,774,784
Cash expenditures	8,702	2,557,107	2,565,809
Transfers from exploration and evaluation assets	–	1,635,586	1,635,586
Decommissioning revisions	–	245,630	245,630
As at September 30, 2011	\$ 226,182	\$ 40,995,627	\$ 41,221,809
Accumulated depletion and depreciation			
As at January 1, 2010	\$ 168,058	\$ –	\$ 168,058
Depletion and depreciation	17,990	15,192,921	15,210,911
As at December 31, 2010	186,048	15,192,921	15,378,969
Depletion and depreciation	11,451	2,025,240	2,036,691
As at September 30, 2011	\$ 197,499	\$ 17,218,161	\$ 17,415,660
Net book value			
As at January 1, 2010	\$ 39,237	\$ 33,959,200	\$ 33,998,437
As at December 31, 2010	\$ 31,432	\$ 21,364,383	\$ 21,395,815
As at September 30, 2011	\$ 28,683	\$ 23,777,466	\$ 23,806,149

The Company included \$25.3 million of future development costs in the depletion calculation for the nine months ended September 30, 2011 (September 30, 2010 – \$1.1 million; December 31, 2010 – \$4.5 million).

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Impairment loss:

During the nine months ended September 30, 2011, due to benchmark forward pricing for natural gas with respect to certain of the Company's CGUs, the Company tested each of its CGUs for impairment. The E&E assets associated with each CGU were also included in this impairment test.

The recoverable amount of each CGU was estimated based on the higher of the value in use and the fair value less costs to sell. The estimate of fair value less costs to sell was determined using a discount rate of 13% percent (December 31, 2010 – 13% percent) and forecasted cash flows, with escalating prices and future development costs, as obtained from the reserve report. The prices used to estimate the fair value less costs to sell are those used by independent industry reservoir engineers.

Based on the assessment at September 30, 2011, the carrying amount of certain CGUs was determined to be \$226,000 (December 31, 2010 – \$11,071,587) lower than their recoverable amounts, and an impairment loss was recognized and included in depletion and depreciation expense in the statement of loss.

8. BANK DEBT:

In March 2011, the Company and its lender (the "Bank") entered into an indicative term sheet (the "Term Sheet") further amending the terms of the Company's \$18,000,000 revolving credit facility. In particular, the Company was required to: (i) complete an equity issuance for a minimum of \$3,000,000 in gross proceeds on or before April 30, 2011 of which not more than \$1,000,000 may consist of common shares of the Company issued on a flow-through basis within the meaning of the Income Tax Act (Canada) (Note 12); and (ii) complete the issuance of a minimum principal amount of \$3,000,000 of unsecured debentures on or before April 1, 2011 (Note 9) and apply the proceeds toward the repayment and cancellation of the unsecured debentures (Note 10). The next review date of the credit facilities was also extended in connection with the Term Sheet to March 31, 2012 but may be changed at any time at the sole discretion of the Bank. On April 5, 2011, the Company and the Bank entered into a formal amending agreement (the "Amending Agreement") based on the terms and conditions set forth in the Term Sheet.

In connection with the entering into of the Amending Agreement, the Company paid the Bank \$50,000 and was required to pay an additional \$350,000 to the Bank no later than April 30, 2011 by way of issuance of 1,296,297 common shares (the "Bank Payment Shares") at a deemed price of \$0.27 per share. The Bank Payment Shares were issued on April 29, 2011 and were subject to a four month hold from the date of issuance.

	September 30 2011	December 31 2010
Revolving facility	\$ 18,000,000	\$ 18,000,000
Non-revolving facility	197,917	291,667
Bank overdraft	—	—
	<u>\$ 18,197,917</u>	<u>\$ 18,291,667</u>

As at September 30, 2011, the maximum availability of the revolving facility was \$18,000,000 (December 31, 2010 – \$18,000,000) at an interest rate of prime plus 3.75% per annum, payable monthly (December 31, 2010 – prime plus 3.75% per annum based on a debt to trailing cash flow covenant).

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The non-revolving facility is due on demand with scheduled principal repayments of \$10,417 per month and bears interest at prime plus 2%, payable monthly. The facilities are secured by a general security agreement providing a security interest in all of the Company's property, assets and undertakings.

In connection with an amending agreement signed in July 2010, the Company paid the Bank \$50,000 and issued 1,500,000 common share purchase warrants to the Bank exercisable at \$0.30 per share until September 2012. The fair value of the warrants was estimated at \$189,383 (\$0.13 per warrant) based on the Black-Scholes pricing model and recorded as a finance expense.

The Company is subject to a working capital covenant of 1 to 1, which the Company was in compliance with at September 30, 2011. For the purposes of the covenant, working capital is defined as (1) current assets plus any undrawn availability under the facilities to (2) current liabilities less amounts drawn under the facilities and principal payable upon maturity of unsecured debentures (Notes 9 and 10).

9. CONVERTIBLE DEBENTURES:

On March 31, 2011, the Company completed a private placement financing of \$3,400,000 principal amount of redeemable, convertible, unsecured debentures ("2011 Convertible Debentures") for which the proceeds were used to repay the unsecured debentures described in Note 10. The 2011 Convertible Debentures bear interest at the rate of 8% per annum, payable commencing June 30, 2011 and quarterly thereafter and mature December 31, 2012 (the "Maturity Date"). The Company has the option to pay interest accrued on the 2011 Convertible Debentures in common shares at a deemed price per common share based on the market price of the common shares at the time of payment of such interest. The 2011 Convertible Debentures are convertible into common shares at the holder's option at any time prior to the Maturity Date at a conversion price equal to \$0.324 per share. The Company has the ability to redeem the 2011 Convertible Debentures in certain circumstances where an offer or business combination is made to acquire the Company's common shares.

The 2011 Convertible Debentures have been classified as debt, net of the fair value of the conversion feature at the date of issue which has been classified as part of shareholders' equity. The debt portion will accrete up to the principal balance at maturity. Accretion and interest are included in finance expense in the statement of loss.

The fair value of the conversion feature was determined at the time of issue as the difference between the principal value of the 2011 Convertible Debentures and the discounted cash flows assuming a 13% percent rate based on the estimated rate for debt with similar terms at the time. If the debentures are converted to shares, a portion of the value of the conversion feature under shareholders' equity will be reclassified to shareholders' capital along with the conversion price paid.

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The following table sets forth a reconciliation of the convertible debentures for the nine months ended September 30, 2011:

	Principal	Debt Portion	Equity Component
Balance, January 1, 2011	\$ —	\$ —	\$ —
Issued March 31, 2011	3,400,000	3,165,950	234,050
Tax effect of equity component	—	—	(58,510)
Accretion of equity component	—	66,819	—
Balance, September 30, 2011	\$ 3,400,000	\$ 3,232,769	\$ 175,540

The Company received \$3,000,000 of cash proceeds and issued \$400,000 principal amount of 2011 Convertible Debentures as settlement of \$400,000 principal amount of unsecured debentures (Note 10).

10. UNSECURED DEBENTURES:

On March 31, 2009, the Company closed a private placement financing through the issuance of \$8.3 million of 17% unsecured debentures (“Debentures”) and 4,150,000 common share purchase warrants exercisable at \$1.20 per share until March 31, 2011. Finder’s fees and commissions of \$201,112 were netted against the debt portion of the Debentures and amortized over the term of the Debentures to finance expense in the statement of loss.

In September 2010, \$5,520,000 principal amount of Debentures plus \$167,950 of accrued interest thereon were exchanged for 24,730,202 common shares at a price of \$0.23 per share (Note 12(b)). The remaining \$2,780,000 principal amount of Debentures and accrued interest were repaid on their March 31, 2011 maturity date.

	September 30 2011	December 31 2010
Principal	\$ 8,300,000	\$ 8,300,000
Exchanged for common shares	(5,520,000)	(5,520,000)
Repaid on maturity date	(2,380,000)	—
Exchanged for 2011 Convertible Debentures	(400,000)	—
	—	2,780,000
Unamortized equity portion	—	(2,594)
Unamortized finder’s fees and commissions	—	(30,615)
	\$ —	\$ 2,746,791

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11. DECOMMISSIONING LIABILITY:

The following table presents the reconciliation of the carrying amount of the liability associated with the retirement of the Company's petroleum and natural gas assets:

	September 30 2011	December 31 2010
Decommissioning liability, beginning of period	\$ 4,412,261	\$ 4,373,809
Liabilities incurred	86,695	67,254
Revisions	158,935	(151,146)
Accretion	82,676	122,344
Decommissioning liability, end of period	<u>\$ 4,740,567</u>	<u>\$ 4,412,261</u>

The following significant assumptions were used to estimate the Company's decommissioning liability:

Undiscounted cash flows	\$ 5,142,013	\$ 5,097,200
Risk-free rate	1.8%	2.6%
Inflation rate	1.5%	1.5%
Expected timing of cash flows	8.4 years	9.3 years

12. SHARE CAPITAL:

(a) Authorized:

Unlimited number of common shares, without nominal or par value
 Unlimited number of preferred shares, without nominal or par value, none of which have been issued

(b) Issued and outstanding:

	Number of Shares	Amount
Balance, January 1, 2010	14,941,406	\$ 21,258,648
Unit equity financing (i)	3,255,000	632,359
Flow-through unit equity financing, net of \$313,900 premium (i)	15,695,000	3,329,483
Shares issued for services (i)	3,500	810
Shares issued on exchange of Debentures (ii)	24,730,202	5,687,950
Share issue costs, net of \$178,500 of tax benefit	-	(663,980)
Balance, December 31, 2010	58,625,108	30,245,270
Common share equity financing (iii)	10,157,824	2,742,612
Flow-through share equity financing, net of \$39,780 premium (iii)	994,500	268,515
Shares issued for bank financing (iv)	1,296,297	350,000
Shares issued for debenture interest (v)	654,366	136,373
Share issue costs, net of \$77,763 tax effect	-	(341,006)
Balance, September 30, 2011	<u>71,728,095</u>	<u>\$ 33,401,764</u>

(i) On September 3, 2010, the Company completed an equity financing with an agent (the

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“Agent”) of 3,255,000 Units at a price of \$0.23 per Unit for gross proceeds of \$748,650 and 15,695,000 flow-through Units at a price of \$0.25 per Unit for gross proceeds of \$3,923,750. Each Unit was comprised of one common share of the Company and one common share purchase warrant and each flow-through Unit was comprised of one flow-through common share and one-half of one warrant. Each whole warrant is exercisable into one common share at any time up to September 3, 2012, at a price of \$0.30 per share.

At the time of issuance, the fair value of the warrants was estimated to be \$396,658 (\$0.04 per warrant) based on the Black-Scholes fair value pricing model with \$632,359 ascribed to common shares and \$3,643,383 ascribed to flow-through common shares.

The Agent was paid a 7% cash commission and issued 3,500 common shares in conjunction with the equity financing. In addition, the Agent received options to purchase 1,137,000 Units (“Unit options”) at a price of \$0.23 per Unit exercisable at any time up to September 3, 2012. Each Unit was comprised of one common share of the Company and one common share purchase warrant exercisable at \$0.30 per share until September 3, 2012. The fair value of the Unit options was estimated to be \$143,097 based on the Black-Scholes pricing model and has been included in share issue costs.

Of the total proceeds, \$313,900 was determined to be the flow-through share premium at the time of issuance and the balance of proceeds was recorded to share capital. The Company renounced the flow-through tax benefits to investors in February 2011 at which time the flow-through share premium liability was reversed and a deferred income tax recovery for the tax effect of flow-through shares is recognized in the statement of loss. Additional deferred income tax recovery was recognized for the difference between the deferred tax liability and the liability recognized on issuance.

- (ii) On September 3 and 15, 2010, an aggregate of \$5,520,000 principal amount of Debentures (Note 10) plus \$167,950 of accrued interest thereon were exchanged for a total of 24,730,202 common shares at a price of \$0.23 per share.
- (iii) On April 29, 2011, the Company completed a private placement equity financing with an agent (the “Agent”) of 10,157,824 common shares at a price of \$0.27 per common share for gross proceeds of \$2,742,612 and 994,500 flow-through common shares at a price of \$0.31 per flow-through common share for gross proceeds of \$308,295.

Of the total flow-through proceeds, \$39,780 was determined to be the flow-through share premium at the time of issuance and the balance of proceeds was recorded to share capital. The Company will renounce the flow-through tax benefits to investors in February 2012 at which time the flow-through share premium liability will be reversed and a deferred income tax recovery for the tax effect of flow-through shares recognized in the statement of loss.

The Agent was paid a 7% cash commission and received options to purchase 780,662 common shares at a price of \$0.27 per common share until October 29, 2012. The fair value of the options was estimated to be \$107,613 based on the Black-Scholes pricing model and has been included in share issue costs

- (iv) On April 29, 2011, the Company issued 1,296,297 common shares to its lender at a deemed price of \$0.27 per common share as payment of a \$350,000 fee in connection with the Company entering into a commitment letter with its lender further amending the terms of the Company’s \$18,000,000 revolving credit facility (Note 8).

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(v) As payment of accrued interest on debentures (Note 9), the Company issued 278,495 common shares at a price of \$0.2435 per common share on June 30, 2011 and 375,871 common shares at a price of \$0.1824 per common share on September 30, 2011. Of the total common shares issued, 577,382 common shares were issued to a company controlled by a director of the Company, representing \$120,329 of interest.

13. WARRANTS:

The following table summarizes information about warrants outstanding:

	Number of Warrants	Amount
Balance, January 1, 2010	4,150,000	\$ 20,750
Issued (Note 8)	1,500,000	189,383
Issued (Note 12 (b)(i))	11,102,500	396,658
Balance, December 31, 2010	16,752,500	606,791
Expired	(4,150,000)	(20,750)
Balance, September 30, 2011	12,602,500	\$ 586,041

Warrants are exercisable at \$0.30 per share and expire in September 2012.

14. UNIT OPTIONS:

At December 31, 2010 and September 30, 2011, the Company had 1,137,000 Unit options outstanding (Note 12(b)(i)). The Unit options are exercisable at \$0.30 per share and expire on September 3, 2012.

15. SHARE-BASED PAYMENTS:

The Company has a stock option plan whereby the Company may grant options to its directors, officers, employees and consultants for up to 10% of the issued and outstanding common shares of the Company. The maximum number of common shares optioned to any one optionee in a twelve month period shall not exceed 5% of the outstanding common shares of the Company at the time of granting or 2% in the case of consultants and employees conducting investor relations activities on behalf of the Company. Options granted under the plan generally have a five-year term and vest as determined by the Board of Directors. The exercise price of each option is determined by the Board of Directors in accordance with applicable stock exchange policies.

On December 31, 2010, the Company granted 3,000,000 stock options exercisable at \$0.35 per share. The options vest 50% on the date of grant and 50% on the first anniversary of the grant date and expire on December 31, 2015. The fair value of the stock options was estimated at \$783,553 (\$0.26 per option) using the Black-Scholes pricing model.

During the three and nine months ended September 30, 2011, the Company recognized \$98,749 and \$293,027, respectively, of stock-based compensation expense in respect of options granted in 2010 (three and nine months ended September 30, 2010 – \$500 and \$1,500, respectively, in respect of options granted in prior years).

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	Number of Options	Weighted- Average Exercise Price
Balance, January 1, 2010	527,000	\$ 4.21
Issued	3,000,000	0.35
Expired	(494,000)	(4.17)
Forfeited	(8,000)	(7.10)
Balance, December 31, 2010	3,025,000	0.38
Issued (note 12(b)(iii))	780,662	0.27
Balance, September 30, 2011	3,805,662	\$ 0.36

The following table summarizes information about stock options outstanding as at September 30, 2011:

Exercise price	Number outstanding	Weighted-average remaining contractual life (years)	Weighted-average exercise price	Number exercisable
\$ 4.46	15,000	0.56	\$ 4.46	15,000
3.50	10,000	1.56	3.50	10,000
0.35	3,000,000	4.25	0.35	1,500,000
0.27	780,662	1.08	0.27	780,662
	3,805,662	3.36	\$ 0.36	2,305,662

16. PER SHARE AMOUNTS:

Basic net loss per share is calculated as follows:

	Three months ended September 30		Nine months ended September 30	
	2011	2010	2011	2010
Loss for the period	\$ (626,290)	\$ (1,835,774)	\$ (2,493,184)	\$ (5,010,175)
Weighted average number of shares – basic:				
Issued common shares at January 1	58,625,108	14,941,406	58,625,108	14,941,406
Effects of shares issued during the period	12,727,116	12,731,073	7,116,151	4,290,325
	71,352,224	27,672,479	65,741,259	19,231,731
Loss per share – basic:	\$ (0.01)	\$ (0.07)	\$ (0.04)	\$ (0.26)

The effect of warrants and options is anti-dilutive in loss periods.

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17. SUPPLEMENTAL CASH FLOW INFORMATION:

	Three months ended September 30		Nine months ended September 30	
	2011	2010	2011	2010
Change in non-cash working capital				
Trade and other receivables	\$ (174,217)	\$ 707,561	\$ (206,789)	\$ 413,012
Prepaid expenses and deposits	6,345	3,773	109,948	387,484
Trade and other payables	(994,534)	(659,413)	(869,668)	(301,541)
	<u>\$ (1,162,406)</u>	<u>\$ 51,921</u>	<u>\$ (966,509)</u>	<u>\$ 498,955</u>
Allocation of change in non-cash working capital:				
Operating activities	(180,851)	62,584	(390,841)	390,705
Financing activities	(981,555)	(10,663)	(575,668)	108,250
	<u>\$ (1,162,406)</u>	<u>\$ 51,921</u>	<u>\$ (966,509)</u>	<u>\$ 498,955</u>

18. RELATED PARTY TRANSACTIONS:

All related party transactions disclosed in these financial statements are in the normal course of business and have been recorded at the exchange amount which is the amount agreed to between the parties based on standard commercial terms. Management of the Company believes the exchange amount is fair and reasonable.

During the three and nine months ended September 30, 2011, the Company was charged nil and \$5,528, respectively (three and nine months ended September 30, 2010 – \$35,124 and \$46,649, respectively) for legal services by a law firm of which a director of the Company is an associate.

During the three and nine months ended September 30, 2011, the Company was charged nil (2010 - \$15,400 and \$49,200, respectively) for consulting services by a corporation of which a former director of the Company is the president and shareholder.

Included in debenture interest for the three and nine months ended September 30, 2011 is \$60,493 and \$120,329 (2010 – nil and \$155,536), respectively, paid to directors, debenture-holders related to directors and to companies controlled by directors.

19. COMMITMENTS

(a) Operating lease:

As at September 30, 2011, the Company was committed under a lease on its office premises with future minimum payments (excluding expected occupancy costs) of \$7,425 per month until July 31, 2011. In April 2011, the Company signed an amendment to the office premises lease for a term of August 1, 2011 to November 30, 2013 for minimum payments (excluding expected occupancy costs) of \$3,712 per month.

The minimum annual lease payments for years ending December 31 are as follows:

2011	\$	11,136
2012		44,544
2013		<u>40,832</u>
	\$	<u>96,512</u>

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(b) Flow-through expenditures:

The Company has until December 31, 2011 to incur \$3,923,750 of qualifying flow-through expenditures related to the equity financing of flow-through common shares issued in September 2010 as disclosed in Note 12(b)(i). As at September 30, 2011, all (December 31, 2010 – \$1,508,126) of the qualifying flow-through expenditures had been incurred.

The Company has until December 31, 2011 to incur \$308,295 of qualifying flow-through expenditures related to the equity financing of flow-through common shares issued in April 2011 as disclosed in Note 12(b)(iii). As at September 30, 2011, none of the qualifying flow-through expenditures had been incurred in respect of the April 2011 flow-through share issuance.

20. SUBSEQUENT EVENT

In October 2011, the Company granted options to purchase 3,500,000 common shares to officers, directors, employees and consultants of the Company with an exercise price of \$0.20 per share. The options expire five years from the date of grant. One-half of the options granted vest at the date of grant and the remaining options vest one year from the date of grant.

21. RECLASSIFICATIONS:

Certain information provided for prior periods has been reclassified to conform to the presentation adopted in 2011.

22. RECONCILIATION FROM GAAP TO IFRS:

The Company's accounting policies under IFRS differ from those followed under previous GAAP as described in Note 3. These accounting policies have been applied for the three and nine months ended September 30, 2011, as well as to the opening statement of financial position on the transition date, January 1, 2010, the comparative information for the three and nine months ended September 30, 2010 and the comparative information for the year ended December 31, 2010.

On transition to IFRS on January 1, 2010, the Company used the IFRS mandatory exception for the retrospective application of certain IFRS whereby hindsight was not used to create or revise estimates and accordingly, the estimates previously made by the Company under GAAP are consistent with their application under IFRS.

The Company applied the following exemptions to full retrospective application of IFRS in accordance with IFRS 1:

- Deemed cost of property, plant and equipment

The Company has elected to apply the exemption under IFRS 1 allowing the measurement of oil and gas assets at the date of transition to IFRS to be determined based on the amounts disclosed under the full cost method of accounting in accordance with GAAP.

- Decommissioning liability

The exemption provided in IFRS 1 from the full retrospective application of IFRS 1 has been applied and the difference between the net book values of the Company's decommissioning liability as measured under IFRS and their net book values under GAAP as of January 1, 2010 has been recognized directly in opening deficit.

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- Share-based payments

The Company has elected not to apply IFRS 2 Share-based Payments to equity instruments granted after November 7, 2002 that had not vested by the transition date.

- Borrowing costs

The Company has applied the borrowing cost exemption in IFRS 1. It has applied the requirement of IAS 23 Borrowing Costs to borrowing costs relating to qualifying assets on a prospective basis from the date of transition to IFRS.

The remaining IFRS 1 exemptions were not applicable or material to the preparation of the Company's Statement of Financial Position at the date of transition on January 1, 2010.

Reconciliations of the Company's conversion to IFRS as at January 1, 2010 and December 31, 2010 and the year then ended are disclosed in the Company's March 31, 2011 condensed interim financial statements.

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(a) Statement of financial position:

At the end of the comparative period under GAAP – September 30, 2010:

	GAAP	Effect of Transition to IFRS	IFRS
Assets			
Current assets			
Cash	\$ 4,070,875	\$ –	\$ 4,070,875
Trade and other receivables	496,909	–	496,909
Prepaid expenses and deposits	236,621	–	236,621
	4,804,405	–	4,804,405
Exploration and evaluation assets (e)	–	4,599,585	4,599,585
Property, plant and equipment (f)	43,640,661	(12,122,901)	31,517,760
	\$ 48,445,066	\$ (7,523,316)	\$ 40,921,750
Liabilities and Shareholders' Equity			
Current liabilities			
Bank debt	\$ 18,322,917	\$ –	\$ 18,322,917
Trade and other payables	1,025,152	–	1,025,152
Current portion of unsecured debentures	2,719,805	–	2,719,805
Flow-through share premium	–	313,900	313,900
	22,067,874	313,900	22,381,774
Decommissioning liability (g)	3,412,212	1,052,995	4,465,207
Deferred tax liability (i)	104,000	(104,000)	–
	25,584,086	1,262,895	26,846,981
Shareholders' equity			
Share capital (h)	29,518,452	763,707	30,282,159
Warrants	485,530	–	485,530
Contributed surplus	1,156,697	–	1,156,697
Shareholders' deficit (c)	(8,299,699)	(9,549,918)	(17,849,617)
	22,860,980	(8,786,211)	14,074,769
	\$ 48,445,066	\$ (7,523,316)	\$ 40,921,750

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(b) Reconciliation of statement of loss and comprehensive loss:

For the comparative interim period under GAAP – three months ended September 30, 2010:

	GAAP	Effect of Transition to IFRS	IFRS
Revenue			
Oil and other natural gas revenue	\$ 1,155,924	\$ –	\$ 1,155,924
Royalties, net of recoveries	(20,724)	–	(20,724)
	1,135,200	–	1,135,200
Expenses			
Production and operating	531,806	–	531,806
General and administrative (f)(i)	292,179	14,373	306,552
Depletion and depreciation (e) and (f)(ii)	2,001,868	(662,818)	1,339,050
Stock-based compensation	500	–	500
	2,826,353	(648,445)	2,177,908
Loss from operating activities	(1,691,153)	648,445	(1,042,708)
Finance income	10,455	–	10,455
Finance expense (g)	(647,580)	22,559	(625,021)
Net finance expense	(637,125)	22,559	(614,566)
Loss before income tax	(2,328,278)	671,004	(1,657,274)
Deferred income tax recovery (i)	583,500	(762,000)	(178,500)
Net loss and comprehensive loss	\$ (1,744,778)	\$ (90,996)	\$ (1,835,774)
Net loss per share	\$ (0.06)	\$ (0.01)	\$ (0.07)

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For the comparative interim period under GAAP – nine months ended September 30, 2010:

	GAAP	Effect of Transition to IFRS	IFRS
Revenue			
Oil and other natural gas revenue	\$ 4,378,408	\$ –	\$ 4,378,408
Royalties, net of recoveries	209,491	–	209,491
	4,587,899	–	4,587,899
Expenses			
Production and operating	1,842,709	–	1,842,709
General and administrative (f)(i)	749,608	43,061	792,669
Depletion and depreciation (e) and (f)(ii)	6,379,543	(1,614,898)	4,764,645
Stock-based compensation	1,500	–	1,500
	8,973,360	(1,571,837)	7,401,523
Loss from operating activities	(4,385,461)	1,571,837	(2,813,624)
Finance income	10,544	–	10,544
Finance expense (g)	(2,096,989)	68,394	(2,028,595)
Net finance expense	(2,086,445)	68,394	(2,018,051)
Loss before income tax	(6,471,906)	1,640,231	(4,831,675)
Deferred income tax recovery (i)	1,682,500	(1,861,000)	(178,500)
Net loss and comprehensive loss	\$ (4,789,406)	\$ (220,769)	\$ (5,010,175)
Net loss per share	\$ (0.25)	\$ (0.01)	\$ (0.26)

(c) Reconciliation of statement of changes in equity:

At the end of the comparative period under GAAP – September 30, 2010:

	Share Capital	Warrants	Contributed Surplus	Deficit	Total Shareholders' Equity
GAAP	\$29,518,452	\$485,530	\$1,156,697	\$(8,299,699)	\$22,860,980
IFRS adjustments					
Date of transition	1,077,607	–	–	(9,329,149)	(8,251,542)
Flow-through share premium	(313,900)	–	–	–	(313,900)
Comprehensive loss (b)	–	–	–	(220,769)	(220,769)
IFRS	\$30,282,159	\$485,530	\$1,156,697	\$(17,849,617)	\$14,074,769

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(d) Reconciliation of statement of cash flows:

For the comparative interim period under GAAP – nine months ended September 30, 2010:

	GAAP	Effect of Transition to IFRS	IFRS
Cash flows from operating activities			
Net loss	\$ (4,789,406)	\$ (220,769)	\$ (5,010,175)
Add back (deduct) non-cash items:			
Depletion and depreciation (e), (f)(ii)	6,379,543	(1,614,898)	4,764,645
Stock based compensation	1,500	–	1,500
Finance expense	1,883,239	(68,394)	1,814,845
Deferred income tax recovery (i)	(1,682,500)	1,861,000	178,500
Interest paid	(1,406,417)	–	(1,406,417)
Change in non-cash working capital	390,705	–	390,705
	776,664	(43,061)	733,603
Cash flows from financing activities			
Share issuance, net of costs	3,978,856	–	3,978,856
Repayment of bank debt	6,225	–	6,225
	3,985,081	–	3,985,081
Cash flows from investing activities			
Exploration and evaluation expenditures (e)	–	(94,660)	(94,660)
Property, plant and equipment expenditures (f)	(799,120)	137,721	(661,399)
Change in non-cash working capital	108,250	–	108,250
	(690,870)	43,061	(647,809)
Change in cash	4,070,875	–	4,070,875
Cash, beginning of period	–	–	–
Cash, end of period	\$ 4,070,875	\$ –	\$ 4,070,875

Notes to reconciliations:

(e) Exploration and evaluation assets:

The Company reclassified the cost of undeveloped land from the full cost pool to E&E assets at the amount that was recorded under GAAP (January 1, 2010 – \$6,127,494; September 30, 2010 – \$4,599,585; December 31, 2010 – \$3,128,241).

The cost of undeveloped land that expired during 2010 was charged as additional depletion and depreciation expense (nine months ended September 30, 2010 – \$1,622,569; year ended December 31, 2010 – \$3,113,212).

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(f) Property, plant and equipment ("PP&E"):

The remaining full cost pool after the reclassification of E&E assets was allocated to D&P asset components on a pro rata basis using reserve values.

	January 1 2010	September 30 2010	December 31 2010
GAAP	\$ 49,221,084	\$ 43,640,661	\$ 32,927,134
IFRS adjustments			
E&E assets (e)	(6,127,494)	(4,599,585)	(3,128,241)
Undeveloped land expiries (e)	–	(1,622,569)	(3,113,212)
Capitalized G&A (f)(i)	–	(43,061)	(57,435)
Impairment loss (f)(ii)	(9,095,153)	(9,095,153)	(9,665,740)
Depletion expense (f)(iii)	–	3,237,467	4,243,702
Decommissioning liability (g)	–	–	189,607
	(15,222,647)	(12,122,901)	(11,531,319)
IFRS	\$ 33,998,437	\$ 31,517,760	\$ 21,395,815

(i) Capitalized general and administrative costs ("G&A"):

Under IFRS, only costs directly attributable to the exploration and evaluation of assets may be capitalized. During 2010, the Company reclassified certain G&A expenses from the full cost pool to the statement of loss (nine months ended September 30, 2010 – \$43,061; year ended December 31, 2010 – \$57,435).

(ii) Impairment:

In accordance with IFRS, impairment tests of PP&E must be performed at the CGU level as opposed to the full cost ceiling test of the entire PP&E balance as required under GAAP. An impairment loss is recognized if the carrying value exceeds the recoverable amount for a CGU. For the Company, the recoverable amount is determined using fair value less costs to sell based on discounted future cash flows of proved plus probable reserves using forecast prices and costs. At the transition date, the Company recognized a total impairment loss of \$9,095,153 on certain of its CGUs with a corresponding charge to opening deficit.

For the year ended December 31, 2010, as a result of continued decreases in natural gas prices and the impact on forecasted natural gas prices used in evaluating the Company's reserves, the Company recognized \$570,587 of additional impairment losses on certain CGUs.

Impairment losses are recognized as additional depletion and depreciation expense and can be reversed in the future if the recoverable amount increases.

(iii) Depletion policy:

Upon transition to IFRS, the Company adopted a policy of depleting oil and natural gas interests on a unit of production basis over proved plus probable reserves. The depletion policy under the previous GAAP was based on units of production over proved reserves. In addition depletion was done on the Canadian cost center under the previous GAAP. IFRS requires depletion and depreciation to be calculated based on individual components such as fields or combinations thereof. As a result of the change in the depletion policy and the

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effects of other adjustments to PP&E, depletion expense under IFRS was reduced (nine months ended September 30, 2010 – \$3,237,467; year ended December 31, 2010 – \$4,243,702).

(g) Decommissioning liabilities:

Under GAAP, increases in the estimated cash flows were discounted using the current credit-adjusted risk-free rate while downward revisions in the estimated cash flows were discounted using the credit-adjusted risk-free rate that existed when the original liability was recognized. Under IFRS, estimated cash flows are discounted using the risk-free rate that exists at the date of the statement of financial position.

At the IFRS transition date, the Company recorded a \$1,121,389 increase to decommissioning liability and opening deficit. Adjustments arising as a result of changes in the risk-free rate in 2010 have been recorded to property plant, and equipment (September 30, 2010 – not significant; December 31, 2010 – \$189,607). The impact of these changes on accretion has been reflected as a change in financing costs (nine months ended September 30, 2010 – \$68,394; year ended December 31, 2010 – \$90,711).

(h) Flow-through shares:

Under GAAP, the accounting treatment for flow-through shares is to record the full amount of the proceeds in share capital. When expenditures are incurred, the related tax effect is recorded to share capital and the future tax liability. Under IFRS, the amount initially recorded in share capital is limited to the amount of common shares that would have been issued on that date and the difference between the actual proceeds and the amount recorded in share capital is set up as a flow-through share premium liability. The flow-through premium is recorded as a liability until the tax benefits are renounced to the investor, at which time a deferred income tax recovery for the tax effect of flow-through shares is recognized in the statement of loss. Additional deferred income tax recovery recognized for the difference between the deferred tax liability and the liability recognized on issuance.

At the IFRS transition date, the Company recorded a \$1,077,607 increase to share capital and opening deficit for the reversal of \$2,452,297 for the cumulative tax effect of flow-through shares issued prior to 2009, net of \$1,374,690 in flow-through share premiums. In 2010, the Company reduced share capital by \$313,900 and recognized a flow-through share premium liability related to flow-through shares issued in September 2010.

(i) Deferred income taxes

Adjustments to deferred income taxes have also been made in regards to other above-noted adjustments that resulted in changes to the temporary difference between tax and accounting values.