

Highlights

Three and nine months ended September 30, 2011 and 2010 (unaudited)

	Three months ended September 30		Nine months ended September 30	
	2011	2010	2011	2010
Operating				
Wells drilled (net wells)				
Oil	2	2	7	8
Natural gas	-	-	-	-
Dry and abandoned	-	1	-	1
Total	2	3	7	9
Success (%)	100%	67%	100%	89%
Undeveloped land holdings (net acres)	46,163	39,665	46,163	39,665
Average daily production				
Crude oil (bbl per day)	1,356	626	1,226	469
Natural gas (Mcf per day)	376	422	339	420
Barrels of oil equivalent (boe per day, 6:1)	1,418	696	1,282	539
Crude oil production (%)	96%	90%	96%	87%
Average sales prices				
Crude oil (\$ per bbl)	\$ 63.07	\$ 58.50	\$ 65.57	\$ 60.48
Natural gas (\$ per Mcf)	\$ 2.44	\$ 3.17	\$ 3.63	\$ 3.87
Barrels of oil equivalent (\$ per boe, 6:1)	\$ 60.86	\$ 54.54	\$ 63.66	\$ 55.65
Operating netback (\$ per boe)				
Petroleum and natural gas revenue	\$ 60.86	\$ 54.54	\$ 63.66	\$ 55.65
Royalties	\$ 12.24	\$ 14.60	\$ 14.69	\$ 14.29
Production & operating expenses	\$ 33.81	\$ 15.57	\$ 32.14	\$ 17.62
Operating netback ⁽¹⁾	\$ 14.81	\$ 24.37	\$ 16.83	\$ 23.74
Financial (000's except per share amounts)				
Oil and natural gas revenue	\$ 7,940	\$ 3,492	\$ 22,282	\$ 8,188
Funds flow from operating activities ⁽²⁾	\$ 820	\$ 824	\$ 2,411	\$ 1,189
Loss and comprehensive loss	\$ (905)	\$ (25)	\$ (2,483)	\$ (1,133)
Per share – basic and diluted	\$ (0.02)	\$ -	\$ (0.06)	\$ (0.04)
Weighted average shares outstanding	43,130	34,368	41,183	31,121
Shares outstanding	43,234	34,368	43,234	34,368
Capital expenditures ⁽³⁾	\$ 5,799	\$ 2,527	\$ 29,530	\$ 7,106
Working capital (net debt) ⁽⁴⁾	\$ (17,294)	\$ 1,043	\$ (17,294)	\$ 1,043
Shareholder's equity	\$ 35,650	\$ 23,105	\$ 35,650	\$ 23,105

(1) Operating netback is a non-IFRS measure and is the net of petroleum and natural gas revenue, royalties, and production and operating expenses.

(2) Funds flow from operating activities is a non-IFRS measure that represents loss and comprehensive loss before non-cash items such as depletion, depreciation, and amortization, accretion expense, share-based compensation, deferred tax and decommissioning liability. Per share amounts are calculated using weighted average shares outstanding consistent with the calculation of net loss per share. Funds flow from operating activities is a key measure as it demonstrates the Company's ability to generate the funds necessary to achieve future growth through capital investment. This table also contains other industry benchmarks and terms, such as working capital (calculated as current assets less current liabilities) and operating netbacks (calculated on a per unit basis as production sales less royalties, transportation and operating costs), which are not recognized measures under IFRS. Management believes these are useful supplemental measures of, firstly, the total net position of current assets and current liabilities of the Company and secondly, the profitability relative to commodity prices. Other entities may calculate these figures differently than Palliser.

(3) Capital expenditures exclude decommissioning liability costs and capitalized share-based compensation.

(4) Working capital (net debt) is a non-IFRS measure representing the total bank loan, accounts payable and accrued liabilities, less accounts receivable, deposits and prepaid expenses.



Report to Shareholders

Palliser Oil & Gas Corporation (“Palliser” or the “Company”) is pleased to report to shareholders the Company’s activities in the third quarter of 2011. Palliser achieved record quarterly production levels during the third quarter of 2011, representing ten consecutive quarters of production growth.

Production during the quarter averaged 1,418 boe/d, an increase of 104% from 696 boe/d in the third quarter of 2010, while production in the third quarter was 16% higher than the second quarter of 2011 average of 1,225 boe/d.

Reflecting on the last quarter, our firm belief is that the steepest part of the High Volume Lift (“HVL”) learning curve is behind us and the Company is entering into a new phase of development. With the completion of new wells and the start up of new salt water disposal (“SWD”) facilities, we are seeing production increases of up to 400% from individual wells tied into the SWD facilities at Lloydminster and Manitou and we expect similar results at Edam. The production increases witnessed at Lloydminster and Manitou have confirmed our expectations that increased salt water disposal capacity would allow us to pump the wells at higher rates, resulting in increased oil production. We also expect that operating costs, which averaged \$32.14 per boe in the nine month period ended September 30, 2011, will be reduced to approximately \$29.00 per boe in the fourth quarter of 2011, primarily due to the reduction of salt water trucking and disposal costs in several of the Company’s core areas. The full impact of the forecasted production increases and operating cost reductions are expected to be realized in the first quarter of 2012, once all of the new salt water disposal facilities are optimized and production from the new wells and the shut-in wells have ramped up. The Company has a number of similar HVL opportunities in our prospect inventory for future growth and we see significant scope to expand our heavy oil operations and take advantage of the proprietary knowledge base we have been developing at Palliser over the last three years.

OPERATIONS & OUTLOOK

Palliser continues to focus on its heavy oil prospects in the greater Lloydminster area. The Company’s capital program

for the first nine months of 2011 amounted to \$29.5 million, including the Manitou property acquisition which was completed in February. Capital spending activity was focused on drilling new wells, reactivating old wells and implementing SWD infrastructure. As previously reported, the SWD facility at Lloydminster was operational at the end of the second quarter, while at Manitou, the Company completed the majority of the expansion and modifications on the existing SWD and battery facilities. At the end of the third quarter, Palliser also started construction of its SWD facilities in the Edam area. As budgeted, two (2.0 net) wells were drilled and one (1.0 net) well was re-entered in the third quarter (100% success), with all wells being completed for heavy oil production. For the nine month period ended September 30, 2011, the Company has drilled seven (7.0 net) wells, re-entered one (1.0 net) well, and reactivated seven (7.0 net) wells, resulting in 15 (15.0 net) heavy oil wells (100% success). During the fourth quarter, Palliser will complete the balance of the fall drilling and reactivation program involving a total of twelve (12.0 net) wells, with all wells forecasted to be on production in December. The capital budget is weighted heavily towards the second half of the year, coinciding with the start up of the Company’s SWD facilities. During 2011, Palliser has more than doubled its heavy oil acreage and amassed numerous high quality prospects for future growth.

Palliser’s SWD facilities at Lloydminster and Manitou have allowed the Company to restart shut in wells and continue to expand production in both of these projects. Results at Lloydminster and Manitou give an indication of the impact that these new facilities can have in a short time frame. At Manitou, additional pipeline and pump installations were completed in October, which significantly increased total disposal capacity, allowing further optimization of production and restarting shut-in wells. Increased disposal capacity plus the drilling of one new well saw production at Manitou increase 77% from 231 bbl/d in the second quarter to 410 bbl/d in the third quarter. Similarly at Lloydminster, completion of the SWD facilities plus drilling of one well enabled the company to ramp up production by 301% from 74 bbl/d in the second quarter, to 297 bbl/d in the third quarter. Starting in the fourth quarter, we expect to realize similar gains



at Edam, where new SWD facilities are currently in the final construction stages. Production at Edam has been reduced from 798 bbl/d in the second quarter to 560 bbl/d in the third quarter, primarily as a result of struggling to keep high water cut wells optimized and shutting in an additional three wells, in anticipation of the imminent start up of the SWD facilities. While a component of this production loss is decline, we are forecasting to see significant production increases with implementation of the SWD facilities which will enable us to ramp up production by optimizing existing wells, reactivate eight shut in wells, and bring on stream our six new fourth quarter wells.

During the third quarter, the Company experienced further delays to the SWD projects at Edam, due to some unexpected operational issues encountered in two of the SWD re-entry wellbores. The continued time delay of the Edam SWD projects further reduced production in the third quarter and into the fourth quarter, as it generally takes a full quarter to fully realize production gains on both new drills and new reactivations. We have built this into our current year end forecast, expecting that the full impact of these added production volumes will not be realized until the first quarter of 2012.

As the timing of the SWD, drilling and re-activation projects was further delayed, Palliser decided to change the scope of the new salt water disposal facilities in Edam, Manitou and Lloydminster, in order to make these facilities to be as effective as possible. All of the SWD facilities have been expanded to take trucked volumes and inject at higher pressures, which will enable the Company to maximize capacity at each facility. The Palliser SWD facilities will all be revenue centers as we have started charging fees to third parties who need to dispose their salt water production. New SWD facilities and future expansions have been fast tracked as the Company already holds future SWD and flow line approvals for efficient and timely expansion. The change of scope of these projects has resulted in cost increases for the overall salt water disposal facility program from the original \$4.0 million capital budget to the current estimate of \$7.7 million. Accordingly, Palliser has deferred several drilling and re-activation projects

until 2012. For 2011, the drilling and reactivation program has been reduced from the previous total of 37 operations to the current total of 27 operations. The Company expects that expanding the scope of the SWD facilities will have a greater impact on 2011 production and operating costs than drilling and reactivating wells late in the year.

As a result of the changes in scope and timing of the current year capital program, Palliser has revised 2011 average production guidance to 1,300 – 1,400 boe/d and exit production to 1,800 – 2,050 boe/d. This capital program is forecasted to generate significant year over year production growth.

In the third quarter, Palliser's credit facilities were expanded to \$28 million and the Company initiated a hedging program to reduce cash flow risk due to the current commodity price volatility. In September, the Company entered into fixed priced swaps for 700 bbl/d of heavy oil at \$74.67/bbl for the fourth quarter of 2011 and \$74.21/bbl for the first half of 2012. Palliser recently entered into another fixed priced swap for 200 bbl/d of heavy oil at \$83.10/bbl for the first quarter of 2012. These prices are for production sold into the Western Canadian Select ("WCS") stream and include the heavy oil differential to West Texas Intermediate (WTI).

Year end net debt, currently forecasted to total \$27 million, is expected to be reduced through the first half of 2012, with cash flow from forecasted increased production that is expected to benefit from a reduction in operating costs on a per boe basis.

Palliser expects to issue average and exit production guidance for 2012 in early January.

On behalf of the Board of Directors,

"Signed"

Kevin Gibson
President and Chief Executive Officer

November 9, 2011



Management's Discussion & Analysis

FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2011 and 2010

The following discussion and analysis (“MD&A”) is a review of operations and current financial position for Palliser Oil & Gas Corporation (“Palliser” or the “Company”) for the three and nine months ended September 30, 2011 and 2010. This MD&A should be read in conjunction with the audited financial statements and notes thereto for the year ended December 31, 2010 and the unaudited financial statements and notes thereto for the three months ended March 31, 2011 & nine months ended September 30, 2011. The MD&A is based on information available as of November 9, 2011.

The following information is based on financial statements prepared by management in accordance with International Financial Reporting Standards.

BOE CONVERSIONS

Production volumes are commonly expressed on a barrel of equivalent (“BOE”) basis whereby natural gas volumes are converted at a ratio of six thousand cubic feet to one barrel of oil. The intention is to convert oil and natural gas measurement units into one basis for improved analysis of results and comparisons with other industry participants. The term BOE may be misleading, particularly if used in isolation. The conversion ratio is based on an energy equivalent method and does not represent an economic value equivalency at the wellhead.

NON-IFRS MEASUREMENTS

The Company evaluates its performance using several criteria, including funds flow from operating activities and funds flow from operating activities per share. Funds flow from operating activities is a non-IFRS measure that represents net loss before depletion, depreciation and accretion, share-based compensation and future income tax. Per share amounts are calculated using weighted average shares outstanding consistent with the calculation of net loss per share. Funds flow from operating activities is a key measure as it demonstrates the Company's ability to generate the funds necessary to achieve future growth through capital investment.

A reconciliation of cash flow from operating activities to funds flow from operating activities is as follows:

	Three months ended September 30		Nine months ended September 30	
	2011	2010	2011	2010
Cash flow from operating activities	\$ 2,563	\$ 937	\$ 2,970	\$ 980
Add (deduct):				
Asset retirement expenditures				
Changes in non-cash working capital	\$ (1,743)	\$ (110)	\$ (559)	\$ 208
Funds flow from operating activities	\$ 820	\$ 827	\$ 2,411	\$ 1,188

The Company also assesses its performance utilizing operating netback. Operating netback represents the profit margin associated with the production and sale of petroleum and natural gas, and is calculated as production revenue less royalties, and production and operating expenses, on a barrel of oil equivalent basis.

These non-IFRS measures are not standardized and therefore may not be comparable to similar measures utilized by other entities.



FORWARD-LOOKING STATEMENTS

The information contained herein contains forward-looking statements and assumptions, such as those relating to the results of operations and financial condition, capital spending, financing sources, production rates and funds flow from operations. By their nature, forward-looking statements are subject to numerous risks and uncertainties, some of which are beyond Palliser's control, including the impact of general economic conditions, industry conditions, volatility of commodity prices, currency fluctuations, imprecision of reserve estimates, environmental risks, changes in environmental tax and royalty legislation, competition from other industry participants, and ability to access sufficient capital from internal and external sources. Readers are cautioned that the assumptions used in the preparation of such information, although considered reasonable at the time of preparation, may prove to be imprecise and, as such, undue reliance should not be placed on forward-looking statements. Palliser's actual results, performance or achievement could differ materially from those expressed in, or implied by, these forward-looking statements. Palliser disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law.

DRILLING ACTIVITY AND CAPITAL EXPENDITURES

The following tables summarize capital expenditures, drilling results and undeveloped land positions for the three months and nine months ended September 30, 2011 and 2010:

Capital expenditures

	Three months ended September 30		Nine months ended September 30	
	2011	2010	2011	2010
Land acquisition	\$ 221	\$ 31	\$ 1,572	\$ 796
Geological & geophysical	\$ 104	\$ 243	\$ 104	\$ 490
Drilling & completions	\$ 3,458	\$ 1,401	\$ 7,600	\$ 3,671
Drilling tax credits	\$ (12)	\$ -	\$ (21)	\$ -
Equipping and facilities	\$ 1,800	\$ 893	\$ 5,439	\$ 2,044
Property acquisitions	\$ 7	\$ 61	\$ 14,309	\$ 77
Capitalized overhead and other	\$ 205	\$ 141	\$ 480	\$ 514
Office equipment and furniture	\$ 16	\$ 1	\$ 47	\$ 5
Total cash capital expenditures	\$ 5,799	\$ 2,771	\$ 29,530	\$ 7,597
Asset retirement costs	\$ 109	\$ 273	\$ 1,531	\$ 554
Capitalized share-based compensation	\$ 70	\$ 24	\$ 93	\$ 34
Total capital expenditures	\$ 5,978	\$ 3,068	\$ 31,154	\$ 8,185



Drilling Results (gross and net)

	Three months ended September 30		Nine months ended September 30	
	2011	2010	2011	2010
Crude oil	2	2	7	8
Natural gas	-	-	-	-
Salt water disposal	-	1	-	1
Dry and abandoned	-	-	-	-
Total	2	3	7	9
Success (%)	100%	67%	100%	89%

Undeveloped land

September 30	2011	2010
Gross acres	55,025	49,570
Net acres	46,163	39,665

Total capital expenditures of \$5.8 million for the third quarter of 2011 were 100% focused on the Company's greater Lloydminster core area. During the third quarter the Company drilled two heavy oil wells and completed one heavy oil well re-entry. These wells were brought on production in the fourth quarter.

In addition, capital activity included costs of approximately \$2.0 million relating to the drilling and completion of one well, the reactivation of two wells, and facility and flow line costs for three salt water disposal wells in the Edam area. The implementation of the three salt water disposal infrastructure continued into the fourth quarter with the first salt water disposal operational at the end of October and the other two salt water disposal wells planned to be operational in the latter half of November.

For the nine month period ended September 30, 2011, Palliser incurred capital expenditures in the amount of \$29.5 million (excluding asset retirement costs and capitalized share-based compensation) that was 100% focused on the Company's greater Lloydminster core area. Included in capital expenditures for the nine month period ended September 30, 2011 is the acquisition of heavy oil properties adjacent to Palliser's existing Manitou properties in the greater Lloydminster area. The property acquisition that closed on January 26, 2011 was valued at \$14.0 million. The acquisition was financed with the issuance of 3.0 million common shares and \$9.5 million cash. For the nine month period ended September 30, 2011 the Company drilled and cased seven heavy oil wells of which four were drilled in January, one was in March and two in August. The two drilled in August are to be brought on production in the fourth quarter. For the nine month period ended September 30, 2011 the Company reactivated a total of eight heavy oil wells.



Production and Sales

The following table summarizes the Company's average daily production:

	Three months ended September 30		Nine months ended September 30	
	2011	2010	2011	2010
Crude oil production (bbl/d)	1,356	626	1,226	469
Natural gas production (mcf/d)	376	422	339	420
BOE/d (6:1)	1,418	696	1,282	539
% crude oil production	96%	90%	96%	87%

The Company's average daily production for the three months ended September 30, 2011 of 1,418 boe/d is an increase of 104% from 696 boe/d in the third quarter of 2010. The Company's average daily production for the nine months ended September 30, 2011 of 1,282 boe/d is an increase of 138% from 539 boe/d in the prior year comparative period. The increase is due primarily to the heavy oil production additions resulting from the 2010 and 2011 drilling programs, and production acquired from the Manitou property acquisition in the first quarter of 2011. Production average of 1,418 boe/d in the third quarter of 2011 is higher than the production average of 1,200 boe/d and 1,225 in the first and second quarters of 2011 respectively. The Company has successfully achieved ten consecutive quarters of production growth.

The Company's crude oil production weighting was 96% in the third quarter of 2011 compared to 90% in the third quarter of 2010. As the Company's focus and current capital program is allocated 100% to its heavy oil prospects in the greater Lloydminster area, the Company is budgeting to have a crude oil production weighting of approximately 97% in 2011.

The following table summarizes the Company's revenue and average prices realized for its crude oil and natural gas production:

	Three months ended September 30		Nine months ended September 30	
	2011	2010	2011	2010
Crude oil	\$ 7,855	\$ 3,369	\$ 21,946	\$ 7,744
Natural gas	\$ 85	\$ 123	\$ 336	\$ 444
Total petroleum and natural gas sales	\$ 7,940	\$ 3,492	\$ 22,282	\$ 8,188
Crude oil (\$/bbl)	\$ 63.07	\$ 58.50	\$ 65.57	\$ 60.48
Natural gas (\$/mcf)	\$ 2.44	\$ 3.17	\$ 3.63	\$ 3.87
\$/BOE	\$ 60.86	\$ 54.54	\$ 63.66	\$ 55.65

Petroleum and natural gas sales for the three months ended September 30, 2011 were \$7.9 million compared to \$3.5 million in the prior year comparative period. The 126% increase in sales is attributed to an increase of 104% in average quarterly production in 2011 compared to the third quarter of 2010, and an increase of 8% in the average realized commodity price from \$58.49 per boe in the third quarter of 2010 to \$63.07 in the third quarter of 2011.

Petroleum and natural gas sales for the nine months ended September 30, 2011 was \$22.2 million compared to \$8.2 million in the prior year comparative period. The 171% increase in sales is attributed to an increase of 138% in average production for the nine months ended September 30, 2011 compared to the prior year comparative period, and an increase of 14% in the average realized commodity price from \$55.65 per boe to \$63.66.



Royalties

The following table summarizes the Company's royalties:

	Three months ended September 30		Nine months ended September 30	
	2011	2010	2011	2010
Royalties	\$ 1,597	\$ 935	\$ 5,141	\$ 2,102
% of oil and gas sales	20%	27%	23%	26%
\$/BOE	\$ 12.24	\$ 14.60	\$ 14.69	\$ 14.29

The Company's royalty rate as a percentage of sales was 20% for the quarter ended September 30, 2011 as compared to 27% for the comparable period last year. Palliser's average royalty rate averaged 23% for the nine months ended September 30, 2011 compared to 26% in the prior year comparable period. The average royalty rate as a percentage of oil and gas sales in 2011 is lower than the comparative 2010 periods as a result of a growth in the number of oil wells producing at lower average production rates compared to 2010, which attract a lower royalty rate.

Production and Operating Expenses

	Three months ended September 30		Nine months ended September 30	
	2011	2010	2011	2010
Operating expenses	\$ 4,411	\$ 997	\$ 11,249	\$ 2,593
\$/BOE	\$ 33.81	\$ 15.57	\$ 32.14	\$ 17.62

Operating costs for the quarter ended September 30, 2011 were \$4.4 million (\$33.81/boe) as compared to \$1.0 million (\$15.57/boe) in the third quarter of 2010. Operating costs for the nine month period ended September 30, 2011 were \$11.25 million (\$32.14/boe) as compared to \$2.6 million (\$17.62/boe) in the prior year comparative period. Per unit operating costs in both of the 2011 periods are higher than in 2010 primarily due to increased salt water volumes and related trucking and disposal costs.

For the three month period ended September 30, 2011, salt water trucking and disposal costs accounted for \$12.87/boe, or 38% of total operating expenses of \$33.81/boe. For the nine month period ended September 30, 2011, salt water trucking and disposal costs accounted for \$11.22/boe, or 35% of total operating expenses of \$32.14/boe.

The Company is in the process of securing its own salt water disposal facilities which the Company forecasts will result in a reduction in salt water trucking and disposal costs and address future production constraints. The Company is forecasting operating costs on a per boe basis to be reduced in the fourth quarter of 2011 when the Company is forecasted to have its own salt water disposal facilities operational at its largest producing area of Edam. The salt water disposal facilities at Lloydminster along with an expansion of the existing salt water disposal facilities at Manitou Lake that were completed late in the second quarter will also contribute to a reduction in salt water trucking and disposal costs. The forecasted reduction in operating costs on a per boe basis is forecast to continue in 2012.



Operating Netback

(\$ per BOE)

	Three months ended September 30		Nine months ended September 30	
	2011	2010	2011	2010
Sales Price	\$ 60.86	\$ 54.54	\$ 63.66	\$ 55.65
Royalties	\$ (12.24)	\$ (14.60)	\$ (14.69)	\$ (14.29)
Production and operating expenses	\$ (33.81)	\$ (15.57)	\$ (32.14)	\$ (17.62)
	\$ 14.81	\$ 24.37	\$ 16.83	\$ 23.74

General and Administrative ("G&A") Expense

	Three months ended September 30		Nine months ended September 30	
	2011	2010	2011	2010
Gross general and administrative expense	\$ 1,192	\$ 720	\$ 3,246	\$ 2,445
Overhead recovery	\$ -	\$ (84)	\$ (146)	\$ (123)
Capitalized	\$ (205)	\$ (141)	\$ (451)	\$ (514)
Net general and administrative expense	\$ 987	\$ 495	\$ 2,649	\$ 1,808
\$/BOE	\$ 7.57	\$ 7.73	\$ 7.57	\$ 12.29

General and administrative expenses, net of recoveries and capitalized G&A, were \$1.0 million or \$7.57 per boe for the current quarter as compared to \$0.5 million or \$7.73 per boe in the prior year comparative quarter. The Company's net G&A expenses for the third quarter of 2011 are higher than the prior year comparative period mainly due to the Company staffing up for the upcoming winter drilling program and the inclusion of bank financing fees incurred in the third quarter. General and administrative expenses, net of recoveries and capitalized G&A, were \$2.6 million or \$7.57 per boe for the nine month period ended September 30, 2011 as compared to \$1.8 million or \$12.29 per boe in the prior year comparative period. The Company's net G&A expenses for the nine month period ended September 30, 2011 is higher than the prior year comparative period, but have been reduced significantly on a per boe basis.

With continued forecasted production growth, general and administrative expenses on a per boe basis are budgeted to decrease further on a per boe basis through 2011.

The Company capitalizes those general and administrative costs that are directly attributable to exploration activities.

Share-based Compensation

	Three months ended September 30		Nine months ended September 30	
	2011	2010	2011	2010
Share-based compensation	\$ 246	\$ 113	\$ 467	\$ 167
Capitalized expense	\$ (52)	\$ (24)	\$ (93)	\$ (34)
Net share-based compensation	\$ 194	\$ 89	\$ 374	\$ 133



Share-based compensation expense (before and after capitalization) for the three and nine months ended September 30, 2011 is higher than the prior comparable periods as a result of a higher number of share options issued and outstanding in the 2011 periods compared to the 2010 periods and the related share-based compensation recognized on those share options.

Exploration and Evaluation Expenditures

	Three months ended September 30		Nine months ended September 30	
	2011	2010	2011	2010
Exploration and evaluation expenditures	\$ -	\$ 243	\$ 407	\$ 490

The Company in accordance with International Financial Reporting Standards has elected to expense costs incurred primarily related to geological and geophysical evaluation of Company's lands that are undeveloped with no reserves associated with them. Under Canadian GAAP these costs were included within capital expenditures. Exploration and evaluation expenditures consist primarily of geological and geophysical evaluation costs. Exploration and evaluation costs that are incurred on lands that have proved or probable reserves associated with them are capitalized in property, plant and equipment.

Depletion, Depreciation and Amortization ("DD&A")

	Three months ended September 30		Nine months ended September 30	
	2011	2010	2011	2010
Depletion and depreciation	\$ 2,141	\$ 737	\$ 5,476	\$ 2,155
\$/BOE	\$ 16.41	\$ 11.51	\$ 15.65	\$ 14.65

For the three months ended September 30, 2011, the Company incurred \$2.1 million (\$16.41/boe) of DD&A expense versus \$0.7 million (\$11.51/boe) for the third quarter of last year. For the nine months ended September 30, 2011, the Company incurred \$5.5 million (\$15.65/boe) of DD&A expense versus \$2.2 million (\$14.65/boe) for the prior year comparative period. The Company calculated depletion, depreciation and amortization under IFRS using proved plus probable reserve volumes. Per unit depletion rates in the 2011 periods compared to the prior year comparative periods have increased as a result of capital expenditures in 2011 for land, seismic, and salt water disposal infrastructure for which the Company has not recognized any reserve additions in the calculation of depletion expense in 2011.

Other Expenses

	Three months ended September 30		Nine months ended September 30	
	2011	2010	2011	2010
Transaction costs	\$ -	\$ -	\$ 120	\$ -

The Company completed a property acquisition in January 2011. In accordance with IFRS, transaction costs related to the acquisition are expensed where as under Canadian GAAP these costs were included as part of capital expenditures.



Management's Discussion & Analysis

	Three months ended September 30		Nine months ended September 30	
	2011	2010	2011	2010
Interest on bank loan	\$ 125	\$ –	\$ 305	\$ 12
Accretion expense	\$ 42	\$ 25	\$ 125	\$ 47
Finance expense	\$ 167	\$ 25	\$ 430	\$ 59

Interest on bank loan amounted to \$125,000 compared to \$nil in the prior year comparative quarter. Interest expense has increased as a result of an increase in bank debt.

Accretion expense is a non-cash item related to the accretion of the Company's decommissioning liability.

INCOME TAXES

A deferred tax recovery of \$0.2 million was recorded for the three month period ended September 30, 2011 compared to a deferred tax recovery of \$nil million in the prior year comparative quarter. A deferred tax recovery of \$0.7 million was recorded for the nine month period ended September 30, 2011 compared to a deferred tax recovery of \$nil million in the prior year comparative period.

The Company has recorded a deferred tax asset in the amount of \$1.2 million as at September 30, 2011. With the growth in Palliser's reserves the Company forecasts it is likely that the benefit of the Company's tax pools will be fully realized. Palliser has approximately \$57.3 million of tax pools, including \$11.1 million of non-capital loss carry-forwards available for deduction against future taxable income. Non-capital losses do not begin to expire until 2026.

LOSS

For the three months ended September 30, 2011 and 2010, the Company had a loss of \$0.9 million (\$0.02 per share) and a loss of \$0.03 million (\$0.00 per share) respectively. For the nine months ended September 30, 2011 and 2010, the Company had a loss of \$2.5 million (0.06 per share) and a loss of \$1.1 million (0.04 per share)

FUNDS FLOW FROM OPERATING ACTIVITIES

Funds flow from operating activities for the three months ended September 30, 2011 is \$0.8 million or \$0.02/share compared to \$0.8 million or \$0.02/share in the prior year comparative period.

LIQUIDITY AND CAPITAL RESOURCES

As at September 30, 2011, the Company had a total credit facility with a financial institution in the amount of \$28.0 million composed of a \$18.0 million revolving demand loan and a \$10.0 million acquisition and development demand loan. The Company's credit facility is subject to semi-annual review by the bank. The facility is a borrowing base facility that is determined based on, among other things, the Company's current reserve report, results of operations, current and forecasted commodity prices and the current economic environment. The credit facility is secured by a general security agreement covering all assets of the Company. The Company's bank loan does not have a specific maturity date as it is a demand facility. This means that the lender has the ability to demand repayment of all outstanding indebtedness or a portion thereof at any time. If that were to occur the Company would be required to source alternate credit facilities or sell assets to repay the indebtedness. The lender requires that the Company maintain a current ratio (current assets adjusted to include the undrawn credit facility balance) of not less than 1.0:1.0. As at September 30, 2011 the Company was in compliance with all banking



covenants. As at September 30, 2011, the revolving operating demand loan had interest payable at prime plus 1.0% and the acquisition and development demand loan had interest payable at prime plus 1.5%. As at September 30, 2011, the Company was not drawn on the acquisition and development demand loan.

On an ongoing basis the Company reviews its capital expenditures to ensure that funds flow and or access to credit facilities is available to fund these capital expenditures. The Company has the flexibility to adjust capital expenditures based on funds flow to manage debt levels.

SHARE CAPITAL

On January 26, 2011 the Company completed a property acquisition financed with the issuance of 3.0 million common shares and \$9.5 million cash. During the first quarter, 150,000 share options were exercised for proceeds of \$0.1 million. In addition, on March 15, 2011 the Company closed a \$10.0 million special warrants financing for net proceeds of approximately \$9.2 million. The Company issued 5,264,000 special warrants which were exercised for 5,264,000 common shares on March 31, 2011 after the Company received its final receipt for a final prospectus qualifying the distribution of the common shares issuable upon exercise of the special warrants. During the third quarter, 250,000 share options were exercised for proceeds of \$0.05 million.

As at November 9, 2011, the Company had 43,233,648 common shares outstanding, 3,499,500 share options outstanding and 167,166 performance share units outstanding.

OFF-BALANCE SHEET ARRANGEMENTS

The Company does not have any special purpose entities, nor is it a party to any transactions or arrangements that would be excluded from the balance sheet other than its operating leases for office space and equipment.

RELATED PARTY TRANSACTIONS

During the three months ended September 30, 2011 the Company incurred nil related party transactions. During the nine months ended September 30, 2011 the Company incurred \$0.2 million (2010 – \$0.1 million) for legal services from a firm in which a director of the Company is a partner. Of this amount, \$nil million (2010 – \$0.1 million) is included in accounts payable and accrued liabilities.

The related party transactions were in the normal course of operations and were recorded at the exchange amount which is the amount of consideration established and agreed to by the related parties.

FINANCIAL INSTRUMENTS

In September 2011, the Company entered into two derivative financial instruments. Derivative assets and liabilities are subject to both price and currency risks as their fair values are based on assumptions including forward commodity prices. Going forward, the Company may use derivative financial instruments from time to time to hedge its exposure to commodity prices. The mark to market valuations of these contracts is presented in the Company's financial statements. These values are based on forward looking estimates including, but not limited to volatility and commodity prices. To the extent that Palliser enters derivatives to manage commodity price risk, it may be subject to liquidity risk as derivative liabilities become due. While the company has elected not to follow hedge accounting, derivative instruments are not entered for speculative purposes and management closely monitors existing commodity risk exposures. As such, liquidity risk is mitigated since any losses actually realized are offset by increased cash flows realized from the higher commodity price environment.



Derivative Position

	Three months ended September 30		Nine months ended September 30	
	2011	2010	2011	2010
Derivatives				
Current asset	\$ 463	\$ -	\$ 463	\$ -
Non-current asset	\$ -	\$ -	\$ -	\$ -
Current liability	\$ -	\$ -	\$ -	\$ -
Non-current liability	\$ -	\$ -	\$ -	\$ -
Net derivative asset position	\$ 463	\$ -	\$ 463	\$ -

Crude Oil Sales Price Derivatives, Being the Unrealized Gain

Daily barrel ("bbl") Quantity	Remaining term of contract	Fixed price per WCS bbl (CAD) ⁽¹⁾	Fair Market value \$ 000's
700	October 1 to December 31, 2011	\$ 74.67	\$ 125
700	January 1 to June 30, 2012	\$ 74.21	\$ 338
Crude oil fair value position			\$ 463

(1) Western Canadian Select Index pricing

QUARTERLY RESULTS

The following table highlights Palliser's performance for each of the past eight quarters:

(\$000's, except per share amounts)

	Q3/11	Q2/11	Q1/11	Q4/10	Q3/10	Q2/10	Q1/10	Q4/09
Total assets	62,053	57,433	53,156	30,633	27,319	27,781	28,701	19,675
Average daily production - boe/d	1,418	1,225	1,200	929	696	536	382	322
Production revenue	7,940	7,991	6,350	5,016	3,493	2,728	1,968	1,480
Funds flow from operating activities	820	1,435	156	939	1,068	363	77	71
Per share - basic	0.02	0.03	-	0.03	0.03	-	-	-
Cash flow from operating activities	2,563	(59)	461	1,285	1,178	46	235	198
Per share - basic	0.06	-	0.01	0.03	-	-	0.01	0.01
Net loss	(905)	(333)	(1,245)	(432)	(1,096)	(615)	(713)	(651)
Per share - basic	(0.02)	(0.01)	(0.03)	(0.01)	(0.01)	(0.03)	(0.01)	0.03
Working capital (deficiency)	(17,294)	(12,359)	(8,600)	(3,942)	1,043	2,745	5,164	(1,275)
Capital expenditures	5,799	5,196	18,536	5,999	2,771	2,786	1,793	2,368

The quarter's highlights in the table above for Q4 2010 and Q4 2009 are in accordance with Canadian GAAP. The other quarters are in accordance with IFRS.

ADDITIONAL INFORMATION

Additional information relating to Palliser, including Palliser's financial statements can be found on SEDAR at www.sedar.com or on the Company's website at www.palliserogc.com.



Condensed Statement of Financial Position

(unaudited)

<i>(in thousands of Canadian dollars)</i>	Note	September 30 2011	December 31 2010
Assets			
Accounts receivable		\$ 2,618	\$ 2,289
Deposits and prepaid expenses		1,755	87
Financial derivatives	13	463	-
Total current assets		4,836	2,376
Property, plant and equipment	7	50,712	26,435
Exploration and evaluation	8	5,274	3,874
Deferred tax assets		1,233	393
Total non-current assets		57,219	30,702
Total assets		\$ 62,055	\$ 33,078
Liabilities			
Accounts payable and accrued liabilities		\$ 8,311	\$ 5,734
Bank loan	11	13,356	583
Total current liabilities		21,667	6,317
Decommissioning provision		4,738	3,082
Total non-current liabilities		4,738	3,082
Total liabilities		26,405	9,399
Equity			
Share capital	9	42,607	28,616
Contributed surplus		978	515
Deficit		(7,935)	(5,452)
Total equity		35,650	23,679
Total equity and liabilities		\$ 62,055	\$ 33,078

The notes are an integral part of these financial statements.



Condensed Income Statements

(unaudited)

(in thousands of Canadian dollars, except per share amounts)	Note	Three months ended September 30		Nine months ended September 30	
		2011	2010	2011	2010
Oil and natural gas revenue		\$ 7,940	\$ 3,492	\$ 22,282	\$ 8,188
Less: royalties		(1,597)	(935)	(5,141)	(2,102)
Unrealized gain on financial derivatives	13	463	–	463	–
Total oil and natural gas revenue		6,806	2,557	17,604	6,086
Production and operating expenses		4,411	997	11,249	2,593
Exploration and evaluation expenditures		–	243	407	490
Depletion and depreciation		2,141	737	5,476	2,155
General and administrative expenses		987	495	2,649	1,808
Other expenses	4	246	89	546	132
		7,785	2,561	20,327	7,178
Results from operating activities		(979)	(4)	(2,723)	(1,092)
Finance income		–	2	–	6
Finance expense		(167)	(23)	(430)	(82)
Net finance expenses	5	(167)	(21)	(430)	(76)
Loss before income tax		(1,146)	(25)	(3,153)	(1,168)
Income tax expense (reduction):					
Deferred		(241)	–	(670)	(35)
Loss and comprehensive loss for the year		\$ (905)	\$ (25)	\$ (2,483)	\$ (1,133)
Earnings per share:					
Basic & diluted	10	\$ (0.02)	\$ (0.00)	\$ (0.06)	\$ (0.04)

The notes are an integral part of these financial statements.



Condensed Statements of Changes in Equity

(unaudited)

<i>(in thousands of Canadian dollars)</i>	Note	Number of common shares	Share capital	Contributed surplus	Retained earnings	Total equity
Balance at January 1, 2010		21,703,348	\$ 19,118	\$ 283	\$ (4,492)	\$ 14,909
Issue of common shares		12,665,000	10,132	-	-	10,132
Share issue costs, net of tax of \$242		-	(730)	-	-	(730)
Share-based payments		-	-	253	-	253
Options exercised	9	221,537	95	(21)	-	74
Loss for the year		-	-	-	(960)	(960)
Balance at December 31, 2010		34,589,885	28,615	515	(5,452)	23,678
Issue of common shares	9	8,264,000	14,502	-	-	14,502
Share issue costs, net of tax of \$169		-	(690)	-	-	(690)
Share-based payments	12	-	-	518	-	518
Options exercised	9	379,763	180	(55)	-	125
Loss for the period		-	-	-	(2,483)	(2,483)
Balance at September 30, 2011		43,233,648	\$ 42,607	\$ 978	\$ (7,935)	\$ 35,650

The notes are an integral part of these financial statements.



Condensed Statements of Cash Flows

(unaudited)

(in thousands of Canadian dollars)	Note	Three months ended September 30		Nine months ended September 30	
		2011	2010	2011	2010
Cash flows from operating activities:					
Loss for the year		\$ (905)	\$ (25)	\$ (2,483)	\$ (1,133)
Adjustments for:					
Depletion and depreciation	7	2,141	737	5,476	2,155
Accretion expense	5	42	23	125	70
Unrealized (gain) on financial derivatives	13	(463)	–	(463)	–
Share-based compensation	4	246	89	426	132
Deferred tax recovery		(241)	–	(670)	(35)
Change in non-cash working capital	6	1,743	110	559	(208)
Net cash from (used in) operating activities		2,563	934	2,970	981
Cash flows from investing activities:					
Property, plant and equipment expenditures		(5,799)	(2,527)	(15,553)	(7,106)
Acquisition of Manitou property	7	–	–	(9,478)	–
Change in non-cash working capital	6	955	182	21	172
Net cash from (used in) investing activities		(4,844)	(2,345)	(25,010)	(6,934)
Cash flows from financing activities:					
Proceeds from issue of share capital	9	–	–	10,002	10,132
Repayment of loans and borrowings		–	–	–	(925)
Proceeds from loans and borrowings		2,231	–	12,772	–
Proceeds from exercise of share options	9	50	–	125	–
Share issuance costs	9	–	–	(859)	(972)
Change in non-cash working capital	6	–	–	–	115
Net cash from (used in) financing activities		2,281	–	22,040	8,350
Change in cash and cash equivalents		(1,411)	–	2,397	
Cash and cash equivalents beginning of period		–	4,063	–	255
Cash and cash equivalents end of period		\$ –	\$ 2,562	\$ –	\$ 2,562

The notes are an integral part of these financial statements.



Condensed Notes to Financial Statements

For the three and nine months ended September 30, 2011, with comparative figures for 2010
(*tabular amounts are in thousands of Canadian dollars except share and per share information*)

1. Reporting entity:

Palliser Oil & Gas Corporation (“Palliser” or the “Company”) is a publicly traded company incorporated under the laws of Alberta. The Company is engaged in the exploration for and development and production of petroleum and natural gas and conducts some of its activities jointly with others; these financial statements reflect only the Company’s proportionate interest in such activities.

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 and IFRS 1 first-time adoption of International Financial Reporting Standards has been applied. The financial statements were authorized for issue by the Board of Directors on November 9, 2011.

Accordingly, certain information and footnote disclosure normally included in annual financial statements prepared in accordance with IFRS, as issued by the International Accounting Standards Board (“IASB”) have been omitted or condensed. An explanation of how the transition to IFRS has affected the reported financial position, financial performance and cash flows of Palliser is provided in note 14.

(b) Basis of measurement:

The financial statements have been prepared on the historical cost basis except for certain financial assets and liabilities which are measured at fair value.

(c) Functional and presentation currency:

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

(d) Use of estimates and judgements:

The preparation of financial statements in conformity with IFRS requires management to make judgements, 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 judgements in applying accounting policies that have the most significant effect on the amounts recognized in the financial statements are valuation of property, plant and equipment, intangible exploration assets, utilization of tax losses, measurement of share-based payments and decommissioning provisions.

Reserve estimates impact a number of the areas referred to above in particular, the valuation of property, plant and equipment and the calculation of depletion and depreciation.



3. Significant accounting policies:

The accompanying condensed interim financial statements prepared in accordance with IFRS should be read in conjunction with Note 3 to Palliser's condensed interim financial statements for the period ended March 31, 2011 as the accounting policies applied by the Company in these condensed interim financial statements are the same as those disclosed therein except for the following.

Derivative Financial Instruments

The Company has entered into financial derivative contracts in order to manage the exposure to market risks from fluctuations in commodity prices. These instruments are not used for trading or speculative purposes. The Company has not designated its financial derivative contracts as effective accounting hedges and has not applied hedge accounting, even though the Company considers all commodity contracts to be economic hedges. As a result, all financial derivative contracts are classified as fair value through profit and loss and are recorded in the statement of financial position at fair value.

Embedded derivatives are separated from the host contract and accounted for separately if the economic characteristics and risks of the host contract and the embedded derivative are not closely related. A separate instrument with the same terms as the embedded derivative would meet the definition of a derivative and the combined instrument is not measured at fair value through profit or loss. Changes in the fair value of separable embedded derivatives are recognized immediately in net earnings.

4. Other expenses:

	Three months ended September 30		Nine months ended September 30	
	2011	2010	2011	2010
Transaction costs	\$ -	\$ -	\$ 120	\$ -
Share-based compensation expense	246	89	426	132
Total other expenses	\$ 246	\$ 89	\$ 546	\$ 132

5. Finance income and expenses:

	Three months ended September 30		Nine months ended September 30	
	2011	2010	2011	2010
Finance income	\$ -	\$ 2	\$ -	\$ 6
Financial expenses:				
Interest on bank loan	125	-	305	12
Accretion of provision	42	23	125	70
	167	23	430	82
Net finance expenses	\$ 167	\$ 21	\$ 430	\$ 76



6. Supplemented cash flow information:

Changes in non-cash working capital is comprised of:

	Three months ended September 30		Nine months ended September 30	
	2011	2010	2011	2010
Source/(use) of cash:				
Trade and other receivables	\$ 311	\$ (328)	\$ (329)	\$ (525)
Deposit and prepaid expenses	(404)	29	(1,668)	1
Trade and other payables	2,791	591	2,577	603
	\$ 2,698	\$ 292	\$ 580	\$ 79
Related to operating activities	\$ 1,743	\$ (110)	\$ 559	\$ 208
Related to investing activities	\$ 955	\$ (182)	\$ 21	\$ (172)
Related to financing activities	\$ –	\$ –	\$ –	\$ (115)

7. Property, plant and equipment:

	Oil & natural gas interests
Cost or deemed cost:	
Balance at January 1, 2010	\$ 16,382
Additions	13,109
Disposals	(113)
Balance at December 31, 2010	29,378
Acquisitions through business combinations	13,978
Additions	15,776
Balance at September 30, 2011	\$ 59,132
Depletion, depreciation and impairment losses:	
Balance at January 1, 2010	\$ –
Depletion and depreciation for the year	2,943
Balance at December 31, 2010	2,943
Depletion and depreciation for the period	5,477
Balance at September 30, 2011	\$ 8,420

Acquisition of Manitou Property:

On January 26, 2011 the Company acquired certain heavy oil properties located adjacent to Palliser's existing Manitou properties in the greater Lloydminster area. The total consideration for the acquisition is \$13,978 comprised of \$9,478 cash and 3.0 million common shares. Of the \$13,978 in consideration paid, \$15,166 was allocated to property, plant and equipment and \$1,188 to decommissioning provision. \$120 in transaction costs incurred as part of the acquisition were expensed in the first quarter of 2011.



8. Intangible exploration assets:

	E&E assets
Cost:	
Balance at January 1, 2010	\$ 2,375
Additions	1,499
Balance at December 31, 2010	3,874
Additions	1,400
Balance at September 30, 2011	\$ 5,274

9. Share capital:

The Company is authorized to issue an unlimited number of common shares and an unlimited number of first and second preferred shares.

The holders of common shares are entitled to receive dividends as declared by the Company and are entitled to one vote per share.

The Company closed a \$10,002 special warrant financing (\$1.90 per special warrant) on March 15, 2011 for net proceeds of approximately \$9,143. The 5,264,000 special warrants were automatically exercised for 5,264,000 shares on March 31, 2011.

On January 28, 2011 the Company issued 150,000 common shares on a cash exercise of options for proceeds of \$75. The related compensation expense of \$14 was reclassified from contributed surplus to share capital.

On January 26, 2011 the Company issued 3,000,000 common shares at \$1.50 per share as partial consideration to acquire certain petroleum and natural gas properties.

On August 9, 2011 the Company issued 100,000 common shares on a cash exercise of options for proceeds of \$50. The related compensation expense of \$10 was reclassified from contributed surplus to share capital.

During the period between July 1, 2011 and September 30, 2011 the Company issued 129,763 common shares on cashless exercise of 150,000 options and performance share units for proceeds of \$nil. The related compensation expense of \$31 was reclassified from contributed surplus to share capital.



10. Earnings per share:

Basic earnings per share was calculated as follows:

	Three months ended September 30		Nine months ended September 30	
	2011	2010	2011	2010
Profit for the year	\$ (908)	\$ (25)	\$ (2,486)	\$ (1,133)
Weighted average number of common shares (basic) (in thousands of shares):				
Issued common shares beginning of period	43,004	34,368	34,590	21,703
Share options exercised	126	–	177	–
Effects of shares issued	–	–	6,416	9,418
Weighted average number of common shares - basic	43,130	34,368	41,183	31,121

Outstanding options are anti-dilutive as the Company reported a loss in 2011 and 2010.

11. Bank loan:

The Company has a revolving operating demand loan of \$18.0 million and an acquisition and development demand loan of \$10.0 million for a total credit facility of \$28.0 million. Advances under the credit facility are payable in full on demand of the lender. Advances under the revolving operating demand loan are available by way of prime rate loans with an interest rate of 1.0% over the lender's prime lending rate. Advances under the acquisition and development demand loan are available by way of prime rate loans with an interest rate of 1.5% over the lender's prime lending rate. The credit facility is secured by a general assignment over the Company's assets.

12. Share-based payments:

Share Options:

The Company has an option plan that entitles officers, directors, employees and certain consultants to purchase shares in the Company. Options are granted at the market price of the shares at the date of grant, have a five year term and vest over three years.

The number and weighted average exercise prices of share options are as follows:

	2011		2010	
	Number of options	Weighted average exercise price	Number of options	Weighted average exercise price
Outstanding at January 1	2,456,500	\$ 0.95	2,226,500	\$ 1.03
Forfeited during the period	(25,000)	0.81	(225,000)	1.35
Exercised during the period	(400,000)	0.50	–	–
Granted during the period	1,468,000	1.38	1,060,000	0.81
Outstanding at September 30, 2011	3,499,500	\$ 1.18	3,061,500	\$ 0.93
Exercisable at September 30, 2011	1,264,833	\$ 1.11	1,461,000	\$ 0.87



Details on the outstanding share options are as follows:

Exercise Price	Number of Options	Weighted average exercise price	Weighted average contractual life (years)
\$0.50	160,000	\$0.50	0.28
\$0.81	925,000	\$0.81	3.71
\$0.94	45,000	\$0.94	4.88
\$0.97	30,000	\$0.97	4.99
\$1.35	2,209,500	\$1.35	3.60
\$1.88	130,000	\$1.88	4.54
	3,499,500	\$1.18	3.44

Performance Share Units:

The Company has a performance share unit plan for its executive officers, which, including share options outstanding under the Company's share option plan, provides for the issuance of up to 10% of the issued and outstanding common shares from treasury at the date of grant. The number of performance share units, which are convertible to shares, is determined by the board of directors. The units vest according to performance targets over a period not to exceed three years from the end of the year the units are granted. Vesting is dependent upon meeting certain corporate performance targets as set and measured by the compensation committee of the board of directors. The units expire three years from the end of the year in which the grant was made. During the year ended December 31, 2010, the Company granted 105,000 performance share units with an expiry date of June 30, 2013. During the year ended December 31, 2010, 15,000 performance share units were forfeited. During the nine month period ended September 30, 2011, the Company granted 110,500 performance share units with an expiry date of June 30, 2014. During the nine month period ended September 30, 2011, 33,335 performance share units were exercised. As at September 30, 2011, 167,166 performance share units are outstanding of which 6,667 performance share units are vested.

Deferred Share Units:

The Company has a cash-settled deferred share unit ("DSU") plan as the form of compensation for the non-employee board of directors. For the nine months ended September 30, 2011, 58,238 DSU's (year ended December 31, 2010, 69,451 DSU's) were granted, with a fair value of \$66 (December 31, 2010 - \$60) included in general and administration expense. As at September 30, 2011, 218,095 (December 31, 2010, 159,857) DSU's are vested and outstanding and \$222 (December 31, 2010 - \$232) is included in accounts payable and accrued liabilities.

Share-based compensation cost of \$426 (2010 - \$132) relating to share options and performance share units was expensed during 2011. In addition, share-based compensation expense of \$93 (2010 - \$10) was capitalized during 2011.



13. Financial Risk Management

(a) Overview

The Company's activities expose it to a variety of financial risks that arise as a result of exploration, development, production and financing activities such as:

- credit risk;
- liquidity risk; and
- market risk.

This note presents information about the Company's exposure to each of the above risks, the Company's objectives, policies and processes for measuring and managing risk.

The Board of Directors oversees managements' establishments and execution of the Company's risk management framework. Management has implemented and monitors compliance with risk management policies. The Company's risk management policies are established to identify and analyze the risks faced by the Company, to set appropriate risk limits and controls, and to monitor risks and adherence to market conditions and the Company's activities.

(b) Credit Risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Company's receivables from oil and natural gas marketers.

Accounts receivable

All of the Company's operations are conducted in Canada. The Company's exposure to credit risk is influenced mainly by the individual characteristics of each customer.

Receivables from oil and natural gas marketers are normally collected on the 25th day of the month following production. The Company's policy to mitigate credit risk associated with these balances is to establish marketing relationships with a number of large purchasers. The Company historically has not experienced any collection issues with its oil and natural gas marketers.

Oil and natural gas marketing companies	\$ 2,621
Other	\$ (3)
Total accounts receivable	\$ 2,618

At September 30, 2011, of \$2.6 million in accounts receivable, 100 percent was current. Palliser had no material accounts receivable deemed uncollectible.

(c) Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses and risking the damage to the Company's reputation. The Company's financial liabilities consist of accounts payable and accrued liabilities and bank debt.



Typically the Company ensures that it has sufficient cash on demand to meet expected operational expenses for a normal period, including the servicing of financial obligations; this excludes the potential impact of extreme circumstances that cannot reasonably be predicted, such as natural disasters. To achieve this objective, the Company prepares annual capital expenditure budgets, which are regularly monitored and updated as considered necessary. Further, the Company utilizes authorizations for expenditures on both operated and non-operated projects to further manage capital expenditures. The Company also attempts to match its payment cycle with collection of oil and natural gas revenue on the 25th of each month.

The Company maintains a \$28.0 million credit facility to provide capital when needed, of which \$14.6 million was available at Sept 30, 2011. Palliser anticipates it will continue to have adequate liquidity to fund its financial liabilities through its future funds from operations and available bank debt. The Company had no defaults or breaches on its bank debt or any financial liabilities as at September 30, 2011.

(d) Market Risk

Market risk is the risk that changes in market prices, such as commodity prices, foreign exchange rates and interest rates will affect the Company's income or the value of the financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimizing the return.

The Company may use financial derivative contracts to manage market risks. All such transactions are conducted within the risk management tolerances that are viewed by the Board of Directors.

Currency Risk

Currency risk is the risk that the fair value of future cash flows will fluctuate as a result of changes in foreign exchange rates. Prices for oil are determined in global markets and generally denominated in United States dollars. The Company does not sell or transact in any foreign currency; however, the United States dollar influences the price of petroleum and natural gas sold in Canada.

Interest Rate Risk

Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in market interest rates. The interest charged on outstanding bank loan fluctuates with the interest rates posted by the lenders. The Company is exposed to interest rate risk and has not entered into any mitigating interest rate hedges or swaps. With regards to interest rate risk, a change of 1 percent in the effective interest rate would impact net income by approximately \$0.1 million annually, based on average debt outstanding during the period.

Commodity Price Risk

Commodity price risk is the risk that the fair value of future cash flows will fluctuate as a result of changes in commodity prices. Commodity prices for oil and natural gas are impacted by not only the relationship between the Canadian and United States dollar but also world economic events dictate the levels of supply and demand. It is the Company's policy to economically hedge some oil and natural gas sales through the use of financial derivative contracts.



Notes to Consolidated Financial Statements

As at September 30, 2011, the Company had fixed pricing applicable to future production through the following contracts:

Crude Oil Sales Price Derivatives, being the unrealized gain			
Daily barrel ("bbl") Quantity	Remaining term of contract	Fixed price per WCS bbl (CAD) ⁽¹⁾	Fair Market value \$ 000's
700	October 1 to December 31, 2011	\$74.67	\$ 125
700	January 1 to June 30, 2012	\$74.21	\$ 338
Crude oil fair value position			\$ 463

(1) Western Canadian Select Index pricing.

Fair value is determined following a three level hierarchy:

Level 1: Quoted prices in active markets for identical assets and liabilities. The company does not have and financial assets or liabilities that require level 1 inputs.

Level 2: Inputs other than quoted prices included within level 1 that are observable, either directly or indirectly. Such inputs can be corroborated with other observable inputs for substantially the complete term of the contract. Palliser uses level 2 inputs in the determination of the fair value of derivative assets and liabilities.

Level 3: Under this level, fair value is determined using inputs that are not observable. Palliser has no assets or liabilities that use level 3 inputs.

14. Reconciliation of statement of financial position, financial performance and cash flows from Canadian GAAP to IFRS:

These financial statements should be read in conjunction with Note 13 of the condensed interim financial statements for the three months ended March 31, 2011. The accounting policies set out in note 3 of the condensed interim financial statements for the three months ended March 31, 2011 will be applied in preparing the financial statements for the year ended December 31, 2011, the comparative information presented in these financial statements for the year ended December 31, 2010 and in the preparation of an opening IFRS statement of financial position as at January 1, 2010 (the Company's date of transition).



Notes to Consolidated Financial Statements

At the end of the third quarter – September 30, 2010:

	Notes	Canadian GAAP	Effect of transition to IFRS	IFRS
Assets				
Current assets:				
Cash and cash equivalents		\$ 2,653	\$ –	\$ 2,653
Accounts receivable		1,348	–	1,348
Deposits and prepaid expenses		94	–	94
		4,095	–	4,095
Non-current assets:				
Property, plant and equipment		23,225	(1,251)	21,974
Exploration and evaluation		–	3,055	3,055
Deferred tax assets		–	–	–
		23,225	1,804	25,029
		\$ 27,320	\$ 1,804	\$ 29,124
Liabilities and Equity				
Current liabilities:				
Bank loan		\$ –	\$ –	\$ –
Accounts payable		3,052	–	3,052
		3,052	–	3,052
Non-current liabilities:				
Decommissioning provision		1,749	1,218	2,967
		1,749	1,218	2,967
Equity:				
Share capital		28,061	220	28,281
Contributed surplus		450	–	450
Deficit		(5,992)	366	(5,626)
		22,519	586	23,105
		\$ 27,320	\$ 1,804	\$ 29,124



Notes to Consolidated Financial Statements

Statements of Comprehensive Income for the nine months ended September 30, 2010:

	Notes	Canadian GAAP	Effect of transition to IFRS	IFRS
Revenue:				
Oil and natural gas revenue		\$ 8,188	\$ –	\$ 8,188
Less: royalties		(2,102)	–	(2,102)
		6,086	–	6,086
Expenses:				
Production and operating expenses		2,593	–	2,593
Exploration and evaluation expenditures		–	490	490
Depletion and depreciation		3,849	(1,694)	2,155
General and administrative expenses		1,808	–	1,808
Other expenses		132	–	132
		8,382	(1,204)	7,178
Results from operating activities		(2,296)	1,204	(1,092)
Finance income		6	–	6
Finance expenses		(12)	(70)	(82)
Net finance expenses		(6)	(70)	(76)
Profit before tax		(2,302)	1,134	(1,168)
Income tax expense (reduction)		(172)	137	(35)
Profit and comprehensive income for the period		\$ (2,130)	\$ 997	\$ (1,133)



Notes to Consolidated Financial Statements

Reconciliation of statements of Comprehensive Income for the three months ended September 30, 2010:

	Notes	Canadian GAAP	Effect of transition to IFRS	IFRS
Revenue:				
Oil and natural gas revenue		\$ 3,492	\$ –	\$ 3,492
Less: royalties		(935)	–	(935)
		2,557	–	2,557
Expenses:				
Production and operating expenses		997	–	997
Exploration and evaluation expenditures		–	243	243
Depletion, depreciation and amortization		1,411	(674)	737
General and administrative expenses		495	–	495
Other expenses		89	–	89
		2,992	(431)	2,561
Results from operating activities		(435)	431	(4)
Finance income		2	–	2
Finance expenses		–	(23)	(23)
Net finance expenses		2	(23)	(21)
Profit before tax		(433)	408	(25)
Income tax expense (reduction)		–	–	–
Profit and comprehensive income for the period		\$ (433)	\$ 408	\$ (25)



Notes to Consolidated Financial Statements

Statement of changes in equity for the nine months ended September 30, 2010:

	Note	Number of common shares	Share capital	Contributed surplus	Retained earnings	Total equity
Balance at January 1, 2010		21,703,348	\$ 19,118	\$ 283	\$ (4,492)	\$ 14,909
Issue of common shares		12,665,000	10,132	-	-	10,132
Share issue costs, net of tax of \$242		-	(969)	-	-	(969)
Share-based payments		-	-	167	-	167
Options exercised	9	-	-	-	-	-
Profit for the year		-	-	-	(1,134)	(1,134)
Balance at September 30, 2010		34,368,348	\$ 28,281	\$ 450	\$ (5,626)	\$ 23,105

Notes to reconciliations:

(a) IFRS 1 election for full cost oil and gas entities

The Company elected an IFRS 1 exemption whereby the Canadian GAAP full cost pool was measured upon transition to IFRS as follows:

- (i) exploration and evaluation assets were reclassified from the full cost pool to intangible exploration assets at the amount that was recorded under Canadian GAAP; and
- (ii) the remaining full cost pool was allocated to the producing/development assets and components pro rata using reserve values.

This resulted in a \$2,375 increase in exploration and evaluation assets with a corresponding decrease in property, plant and equipment.

(b) Decommissioning obligations:

Under Canadian GAAP asset retirement obligations were discounted at a credit adjusted risk free rate of 8.0 percent. Under IFRS the estimated cash flow to abandon and remediate the wells and facilities has been risk adjusted therefore the provision is discounted at a risk free rate of 3.54 percent. Upon transition to IFRS this resulted in an \$547 increase in the decommissioning obligations with a corresponding increase in deficit.

As a result of the change in the decommissioning obligation accretion expense decreased by \$75 during the year ended December 31, 2010 and decreased by \$62 for the nine month period ended September 30, 2011 under IFRS compared to Canadian GAAP. In addition, under Canadian GAAP accretion of the discount was included in depletion and depreciation. Under IFRS it is included in finance expenses.

(c) 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 Canadian GAAP was based on units of production over proved reserves. In addition depletion was done on the Canadian cost centre under Canadian GAAP. IFRS requires depletion and depreciation to be calculated based on individual components (ie. fields or combinations thereof).

There was no impact of this difference on adoption of IFRS at January 1, 2010. However, this change resulted in a decrease to depletion expense for the year ended December 31, 2010 of \$2,863 and a decrease to depletion expense for the nine month period ended September 30, 2010 of \$1,645.



(d) Flow-through Shares

Under Canadian 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 affect 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 deferred price premium on flow-through shares. When the expenditures are incurred, the related deferred price premium on flow-through shares is reversed and the related tax affect is recorded to the future tax liability. The impact on this change in accounting policy resulted in recording a transitional adjustment to share capital and deficit of \$220. This adjustment reversed previous flow-through renunciation adjustments made through share capital and recorded the related tax affect.

(e) Income tax

Deferred income taxes have been adjusted to reflect the tax effect arising from the differences between IFRS and Canadian GAAP. The application of the IFRS adjustments resulted in a \$137 deferred tax expense adjustment for the nine month period ended September 30, 2010.

15. Subsequent Events

Crude Oil Sales Price Derivative Contract

Subsequent to September 30, 2011 the Company entered into the following crude oil sale price derivative:

Daily barrel (bbl) quantity	Term of Contract	Fixed Price per bbl (WCS) ⁽¹⁾
200	January 1, 2012 to March 31, 2012	\$83.10

(1) Western Canadian Select Index pricing.



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Calgary, Alberta

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2 Reserves Committee

3 Compensation Committee

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President & CEO

Allan Carswell

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Glenn Taylor

Vice President, Production & Operations

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Transfer Agent

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