

## **CYGAM ENERGY INC. (Formerly known as SHEER ENERGY INC.)**

### **MANAGEMENT'S DISCUSSION AND ANALYSIS SIX MONTHS ENDED JUNE 30, 2006**

This Management's Discussion and Analysis (MD&A) is a review of operations, current financial position and outlook for Cygam Energy Inc. (Cygam or the Company) and should be read in conjunction with the unaudited interim consolidated financial statements for the three and six months ended June 30, 2006. This MD&A is dated as of August 11, 2006.

The unaudited interim consolidated financial statements have been prepared by management and approved by Cygam's Audit Committee on behalf of the Board of Directors. These statements are based on certain estimates and assumptions and involve risks and uncertainties. Actual results may differ materially. Refer to the Business Risks section of this MD&A for additional information related to identified risks, estimates and uncertainties.

All financial information is reported in Canadian dollars and is in accordance with Canadian generally accepted accounting principles (GAAP) unless otherwise noted. Natural gas has been converted into barrels of oil equivalent (boe) at 6:1. The abbreviation boe, boe per day and mboe disclosed in this MD&A may be misleading, particularly if used in isolation. A boe conversion ratio of 6 mcf: 1 boe is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.

#### **Cautionary Statement regarding Forward-Looking Information**

Certain statements contained in this MD&A including statements which contain words such as "anticipate", "could", "should", "expect", "seek", "may", "intend", "likely", "will", "believe" and similar expressions, statements relating to matters that are not historical facts, and statements of our beliefs, intentions and expectations about development, results and events which will or may occur in the future, constitute "forward-looking information" within the meaning of applicable Canadian securities legislation and are based on certain assumptions and analysis made by us derived from our experience and perceptions. Forward-looking information in this MD&A includes, but is not limited to: statements relating to "reserves" and "resources" as they involve the implied assessment, based on certain estimates and assumptions that the resources and reserves described can be profitably produced in the future; expected cash provided by continuing operations; future capital expenditures, including the amount and nature thereof; oil and natural gas prices and demand; expansion and other development trends of the oil and natural gas industry; business strategy and outlook; expansion and growth of our business and operations; the maintenance of existing government, supplier and partner relationships; supply channels; accounting policies; balance sheet financial instruments; credit risks; and other such matters.

All such forward-looking information is based on certain assumptions and analyses made by us in light of our experience and perception of historical trends, current conditions and expected future developments, as well as other factors we believe are appropriate in the circumstances. The risks, uncertainties, and assumptions are difficult to predict and may affect operations, including, without limitation: the risks associated with foreign operations; foreign exchange fluctuations; commodity prices; equipment and labour shortages and inflationary costs; general economic conditions; industry conditions; changes in applicable environmental, taxation and other laws and regulations as well as how such laws and regulations are interpreted and enforced; the ability of oil and natural gas companies to raise capital; the effect of weather conditions on operations and facilities; the existence of operating risks; volatility of oil and natural gas prices; oil and natural gas product supply and demand; risks inherent in the ability to generate sufficient cash flow from operations to meet current and future obligations; increased competition; stock market volatility; opportunities available to or

pursued by us and other factors, many of which are beyond our control. The foregoing factors are not exhaustive and are further discussed herein under the heading "Business Risks and Uncertainties".

Actual results, performance or achievements could differ materially from those expressed in, or implied by, this forward-looking information and, accordingly, no assurance can be given that any of the events anticipated by the forward-looking information will transpire or occur, or if any of them do so, what benefits will be derived therefrom. Except as required by law, Cygam Energy Inc. disclaims any intention or obligation to update or revise any forward-looking information, whether as a result of new information, future events or otherwise.

The forward-looking information contained herein is expressly qualified by this cautionary statement.

## **REVERSE TAKE-OVER**

Effective October 11, 2005, Cygam (formerly Sheer Energy Inc.) completed a reverse take-over (the "RTO Transaction") involving the acquisition of all the issued and outstanding shares of Rigo Oil Company Limited ("ROCL"), Vega Oil S.p.A. ("Vega"), whereby the shareholders of ROCL acquired control of Cygam. The RTO Transaction resulted in change of control of Cygam, including the resignation and subsequent appointment of certain new directors and officers.

In accordance with accounting for reverse take-over, the consolidated financial statements of the Company treat ROCL as the acquiring company and therefore all results prior to the acquisition date of October 11, 2005 reflect the operations of ROCL only.

## **EXPLORATION ACTIVITIES**

During the quarter, Cygam's wholly-owned subsidiary, Rigo Oil Company Limited, finalized the acquisition of an additional 62.5% interest in the Jorf Permit in Tunisia from Pioneer Natural Resources, the previous operator. The Company now holds a 100% working interest in the permit and, as the new operator, has successfully requested the extension of the drilling commitment at Jorf to August 6, 2007. Cygam received a considerable amount of seismic data on the Jorf and the adjoining Bazma permit in Tunisia from the Tunisian State Oil Company (ETAP) and previous operators. Such data was sent to the Calgary office where it is currently being interpreted. Selected seismic lines are also being reprocessed to improve quality. It is expected that the Company will complete the preliminary assessment of the Triassic and Permian potential in both permits by the end of the third quarter. Plans for shooting a potential additional seismic program and for drilling locations will be made at that time. As mentioned before, Cygam has already received expressions of interest from other companies willing to participate in exploratory activities in both areas pending a review of the seismic data.

The Company also acquired casing, tubing and related completion equipment which should be sufficient to satisfy the requirements of a well drilled either at Jorf or Bazma.

Additional seismic data on the Sud Tozeur prospecting licence has also been received from ETAP and will be reinterpreted and reprocessed where necessary.

In Italy, Cygam's wholly-owned Italian subsidiary, Vega Oil S.p.A., secured a drilling rig for its 100% owned prospect at Posta Nuova. Drilling is planned for October-November depending on the actual availability of the drilling contractor. Negotiations are currently underway to have all necessary supplies and approvals in place by the end of September.

In Canada, completion of the well drilled at 9-19-50-16W5M in the South Edson Unit, where Cygam has an 8.9688% working interest, occurred in the second quarter. The well is now awaiting tie-in into the Unit through a 1.5 km pipeline and is expected to be on production in the fall. Drilling, completion and routine maintenance operations were also conducted in the Snipe Lake South Unit where the Company has a 0.0763814% working interest.

## FINANCIAL PERFORMANCE

### Selected Financial Information

In accordance with the accounting for reverse takeovers, the results for the three and six months ended June 30, 2005 are for ROCL only, and the results for the three and six months ended June 30, 2006 include the Canadian operations, ROCL and Vega.

|  | Three months ended |                  | Six months ended |                  |
|--|--------------------|------------------|------------------|------------------|
|  | 2006               | 2005             | 2006             | 2005             |
|  | \$                 | \$               | \$               | \$               |
| Oil and gas revenue                      | 124,671            | -                | 295,736          | -                |
| Royalties, net of ARTC                   | (31,007)           | -                | (66,548)         | -                |
| Other revenue                            | 158,887            | 53,920           | 303,470          | 107,523          |
| Total net revenue                        | 252,551            | 53,920           | 532,658          | 107,523          |
| Operating costs                          | 50,404             | -                | 93,078           | -                |
| Depletion, amortization and accretion    | 44,292             | -                | 84,302           | 27               |
| General & administration                 | 295,811            | -                | 540,597          | -                |
| Interest                                 | 1,119              | -                | 2,867            | -                |
| Exchange (gain)/loss                     | 2,484              | (6,989)          | 2,484            | (6,989)          |
| Stock-based compensation expense         | 92,062             | -                | 184,124          | -                |
|  | 486,172            | (6,989)          | 907,452          | (6,962)          |
| Earnings (Loss) before following items   | (233,621)          | (141,173)        | (374,794)        | 114,485          |
| Gain on sale of marketable securities    | -                  | 4,827,555        | -                | 4,827,555        |
| Unrealized loss on marketable securities | (496,988)          | -                | (341,305)        | -                |
| <u>Net earnings (loss)</u>               | <u>(730,609)</u>   | <u>4,888,464</u> | <u>(716,099)</u> | <u>4,942,040</u> |
| Current and future income tax recovery   | 5,000              | -                | 5,000            | -                |
| <u>Net earnings (loss) after tax</u>     | <u>(725,609)</u>   | <u>4,888,464</u> | <u>(711,099)</u> | <u>4,942,040</u> |

### Oil and Gas Revenue

Oil and gas revenues (net of royalties) for the three months ended June 30, 2006 of \$93,664 represents revenue from the Canadian operations. Production for the quarter was 31.6 barrels of oil equivalent per day (boe/d), comprising approximately 69% natural gas and 31% oil and NGLs, at an average price of \$43.35 per boe. Crown and production royalties (net of ARTC) was \$31,007 or \$10.78 per boe, whilst operating expenses were \$50,404 or \$17.53 per boe.

The oil and gas revenue fell 27% from the previous quarter ended March 31, 2006 due to drop in the price of natural gas received by the Company, combined with reduced production from the Harmattan unit which was shut-in for several days in June to complete a turbine replacement, and reduced volumes from the South Edson and Signalta units.

## **Other Revenue**

Other revenue in the three months ended June 30, 2006 and 2005 includes distributions of \$83,829 (2005 - \$53,920) received from investments in marketable securities, and interest income of \$75,057 (2005 - \$nil) on cash balances invested in short-term fixed income securities.

## **Unrealized Loss on Marketable Securities**

As noted earlier, Cygam's reverse takeover included the acquisition of units of a public entity. At the time of the acquisition, management had designated these units as held for trading with the intent to dispose of these units when funds were required for exploration activities. At June 30, 2006 the units are stated in the financial statements at the lower of cost and fair market value of \$4,726,387 (March 31, 2006 - \$5,223,375) resulting in an unrealized loss of \$496,988 during the quarter.

## **Net Income**

The net loss after tax for the period was \$ 725,609 (2005 – net earnings \$4,888,464). The net loss of \$233,621 before the unrealized loss on marketable securities included the non-cash stock based compensation cost of \$92,062 and \$44,292 for depletion, amortization and accretion.

## **General and Administrative Expenses**

The general and administration expenses for the period ended June 30, 2006 of \$295,811 (2005- \$nil), included \$112,228 paid as consulting fees, of which \$79,509 was paid to directors and officers of Cygam, or to companies whose shareholders are directors and officers of Cygam, \$72,232 incurred in legal, audit and accounting fees, and \$25,949 incurred on shareholder and public company expenses including expenses relating to the annual general meeting held on June 15, 2006.

In the three months ended June 30, 2006, the Company capitalized \$37,160 (2005 - \$28,201) of the general and administrative expenses incurred in Tunisia as these costs were directly related to the acquisition and exploration of oil & gas properties in Tunisia.

## **Stock-based Compensation**

Stock-based compensation for the period was \$92,062. Stock-based compensation represents a non-cash charge resulting from applying fair value method on stock options issued by the Company during the period. Under this method, compensation expense related to this program is recorded in the statement of operations over their respective vesting periods. The amount of compensation cost recognized in the period is based on the fair value the stock options awarded prior to June 30, 2006 and vesting in 2006.

## **Depletion, Amortization and Accretion**

Depletion, Amortization and Accretion (“DA&A”) amounted to \$44,292 (\$15.40 /boe) for the period, largely related to the production from Canadian properties. The cost of unproved properties is excluded from the DA&A calculation and is assessed periodically to ascertain whether impairment has occurred.

## SUMMARY OF QUARTERLY INFORMATION

The following is a summary of selected financial information for the Company for the past six quarters. Quarterly financial information for the two quarters in 2004 is not available as ROCL was a private company and did not prepare quarterly financial statements during that period.

|  | Q2<br>2006 | Q1<br>2006 | Q4<br>2005  | Q3<br>2005 | Q2<br>2005 | Q1<br>2005 |
|--|------------|------------|-------------|------------|------------|------------|
| P&G sales (net of royalties)                       | \$ 93,664  | \$ 135,524 | 210,025     | -          | -          | -          |
| Other revenue                                      | 158,887    | 144,583    | 128,299     | -          | 53,920     | 50,281     |
| Expenses   | 483,688    | 421,280    | 1,179,285   | -          | -          | -          |
| Earnings (loss) before items below                 | (231,137)  | (141,173)  | (840,961)   | -          | 53,920     | 50,281     |
| Gain on sale of marketable securities              | -          | -          | -           | -          | 4,827,555  | -          |
| Unrealized gain (loss) on<br>marketable securities | (496,988)  | 155,683    | (932,308)   | -          | -          | -          |
| Foreign exchange gain (loss)                       | (2,484)    | -          | (58,486)    | 376,860    | 6,989      | -          |
| Net earnings (loss) before income taxes            | (730,609)  | \$ 14,510  | (1,831,755) | 376,860    | 4,888,464  | 50,281     |
| Current and future income tax recovery             | 5,000      | -          | 10,978      | -          | -          | -          |
| Net earnings after tax                             | (725,609)  | \$ 14,510  | (1,820,777) | 376,860    | 4,888,464  | 50,281     |
| Net income (loss) per share                        | (0.01)     | 0.00       | (0.037)     | 0.009      | 0.117      | 0.001      |

## LIQUIDITY AND CAPITAL RESOURCES

The Company had a net working capital balance of \$11,798,055, including a cash balance of \$7,071,699 as at June 30, 2006. Cash balances in excess of planned requirements were invested in short-term fixed income securities generating \$75,057 in interest income for the three months ended June 30, 2006, and the Company continues to receive monthly distribution of \$27,943 from its investment in marketable securities.

The Company's cash balance and additional funds from the liquidation of the marketable securities are expected to be sufficient to fund the planned first phase of the exploration program over the next two years, and to meet Cygam's obligations on a timely basis for the foreseeable future. The Company, through its subsidiaries in Italy and Tunisia, has either entered into agreements or has received expressions of interest from third parties to participate in the exploration program on several of the permits on the basis of "pay 60% to earn 40% interest". The Company will examine each interest on a permit by permit basis to determine the level and amount of participation offered to third parties. The planned capital expenditures program for the next twelve months, net to Cygam, of approximately \$5,000,000 will be primarily funded from the Company's cash and working capital.

## SHARE CAPITAL

The Company is authorized to issue an unlimited number of common shares as well as first preferred non-voting shares. To date, no preferred shares have been issued. The Company's share capital as at June 30, 2006 and as at December 31, 2005 is outlined below:

|   | Shares            | Amount (\$)         |
|---|-------------------|---------------------|
| Outstanding shares at December 31, 2005     | 72,335,640        | \$ 14,291,305       |
| Outstanding shares at March 31, 2006        | 72,335,640        | \$14,291,305        |
| Issued upon exercise of Series "B" warrants | <u>14,000</u>     | <u>12,386</u>       |
| Outstanding shares at June 30, 2006         | <u>72,349,640</u> | <u>\$14,303,681</u> |

Other than the 14,000 shares issued upon the exercise of warrants, no shares were issued during the three months ended June 30, 2006. No stock options were granted or exercised during the three months ended June 30, 2006. The total number of stock options granted as at June 30, 2006 was 5,025,000.

## BUSINESS RISKS AND UNCERTAINTIES

Cygam is in the business of exploring for, developing and producing oil and natural gas. The Company has production operations in Canada, and exploration activities in Italy and Tunisia. Along with the competitive nature of the oil and gas industry, risk exposures, some of which are beyond the control of the Company, can be categorized as operational, political, regulatory, environmental and financial. The long-term commercial success of Cygam depends on its ability to find, acquire, develop and commercially produce oil and natural gas reserves. Oil and natural gas exploration involves a high degree of risk and there is no assurance that expenditures made on future exploration by the Company will result in new discoveries of oil or natural gas in commercial quantities. It is difficult to project the costs of implementing an exploratory drilling program due to the inherent uncertainties of drilling in unknown formations, the costs associated with encountering various drilling conditions and changes in drilling plans and locations as a result of prior exploratory wells or additional seismic data and interpretations thereof.

The process of evaluating prospects and estimating oil and natural gas reserves is complex and subject to uncertainty. Actual operating results, including production performance, may vary from those estimated, possibly materially. Cygam manages these risks by having operational control, where possible, and working interests commensurate with the assessed risk in each project and by hiring qualified professionals, including independent reserves engineers, with appropriate industry experience.

The Company focuses the majority of its activities on exploration in Tunisia and Italy. Some of the Corporation's operations and related assets are located in countries which carry a higher degree of political and economic risk. Cygam's management has considerable expertise operating internationally and has developed solid, long-term relationships within each of the jurisdictions in which it operates. The Company adheres to all governmental and environmental regulations as they apply in each operating jurisdiction. Regulation changes could increase costs of the Company's operations.

Cygam's current production base in Canada is heavily weighted to natural gas which is subject to price fluctuations based on North American natural gas supply and demand conditions. Oil and natural gas are commodities whose prices have fluctuated widely in recent years and are determined based on world demand, supply and other factors, all of which are beyond the control of the Company.

Cygam maintains an insurance program which is consistent with industry practice to provide adequate coverage of drilling, operations, safety and the environment.

#### **RELATED PARTY TRANSACTIONS**

Transactions between the Company and related parties occurred during the year, as disclosed in the notes to the consolidated financial statements. During the three months ended June 30, 2006, the Company paid \$79,509 as consulting fees to related parties. The Company also paid \$9,200 in legal fees to a legal firm in which a director of the Company is a partner. All such transactions were in respect of technical and specialized services rendered in the normal course of business operations and represent consideration established and agreed to by the related parties which is similar to those negotiated with third parties.

#### **CONTRACTUAL OBLIGATIONS AND COMMITMENTS**

In the ordinary course of business, the Company and its subsidiaries may enter into contracts which contain indemnification provisions, such as service agreements, leasing agreements, asset purchase and sale agreements, joint venture agreements, operating agreements, land use agreements, etc. In such contracts, the Company may indemnify counterparties to the contracts if certain events occur. These indemnification provisions vary on an agreement by agreement basis. In some cases, there are no pre-determined amounts or limits included in the indemnification provisions and the occurrence of contingent events that will trigger payment under them is difficult to predict. Therefore, the maximum potential future amount that the Company could be required to pay cannot be estimated.

Rigo Oil Company Tunisia Ltd. (ROCT) was a partner and is now the operator of the Jorf exploration permit, and the operator of the Sud Tozeur prospecting licence. Under the terms of the exploration permit, the operator and its partners are obligated to drill one well to the depth of 2,500 meters within the term of the permit which has now been extended to August 6, 2007. Under the terms of the Sud Tozeur prospecting licence, which expires on February 24, 2007, ROCT is obligated to re-interpret existing seismic data and acquire 50 kilometers of new seismic lines and has an option to convert the licence to a four year exploration permit. In the event that the obligations are not met or the prospecting licence is not converted to an exploration permit, ROCT may be required to pay a penalty.

The Company rents premises in Rome, Italy, and in Tunis, Tunisia, under operating leases that require payments of \$39,380 per annum in each of 2006 and 2007 in Rome and \$59,000 per annum in Tunis.

#### **CRITICAL ACCOUNTING ESTIMATES**

Cygam's significant accounting policies are disclosed in Note 2 to the audited consolidated financial statements for the year ended December 31, 2005. Certain accounting policies require that management make appropriate decisions with respect to the formulation of estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. The following discusses such accounting policies and is included in the MD&A to assist the reader in assessing our critical accounting policies and practices and the likelihood of materially different results being reported. As management, we review estimates regularly.

The emergence of new information and changed circumstances, including accounting standards, may result in actual results or changes to estimated amounts that differ materially from current estimates.

## **Reserves Determination**

The petroleum and natural gas reserves used in determining our depletion rates and the ceiling test are based upon management's best estimates, and are subject to uncertainty. Through the use of geological, geophysical and engineering data, the reservoirs and deposits of petroleum and natural gas are examined to determine quantities available for future production, given existing operating and economic conditions and technology. The evaluation of recoverable reserves is an ongoing process impacted by current production, continuing development activities and changing economic conditions as reflected in crude oil and natural gas prices and costs. Consequently, the reserves are estimates which are subject to variability. We employ the services of independent oil and gas reservoir engineers (Fekete Associates Inc. and Matsalla Consulting (1981) Ltd.) to assist with the reserve evaluation process for the Canadian properties.

## **Full Cost Accounting for Oil and Gas Activities**

Cygam uses the full cost method of accounting for exploration and development activities. In accordance with this method of accounting, all costs associated with exploration and development, are capitalized whether successful or not. The aggregate of net capitalized costs and estimated future development costs is amortized using the unit-of-production method based on estimated proved oil and gas reserves before royalties, as determined by qualified independent petroleum evaluation engineers. Accordingly, changes in estimated proved oil and gas reserves and estimated future development costs would result in changes to the depletion rate. Certain costs related to unproved properties and major development projects may be excluded from costs subject to depletion until proved reserves have been determined or their value is impaired. These properties are assessed periodically and any impairment is transferred to the costs subject to depletion.

## **Asset Impairments**

Under full cost accounting, a ceiling test is performed to ensure that unamortized capitalized costs in each cost centre (country) do not exceed their fair value. Impairment is recognized when the carrying value is greater than the undiscounted future cash flows. In the event of impairment, the amount by which the carrying value exceeds the estimated fair value of the long-lived asset is charged to earnings. Fair value is determined using expected future product prices and costs, and amounts are discounted using a risk-free interest rate.

## **Asset Retirement Obligations**

The fair value of the future retirement obligation is discounted to present value and is recorded as an increase to the related property and equipment with the corresponding balance recorded as a future asset retirement obligation. The increased asset value is amortized according to our policies for property and equipment and the future liability is accreted to expense until the future retirement obligation is expected to be settled.

## **Stock-Based Compensation**

The Corporation uses the fair value method for valuing stock option grants. Under this method, compensation cost attributable to all stock options granted is measured at fair value at the grant date, using the Black-Scholes valuation model, and expensed over the vesting period with a corresponding increase to contributed surplus. Upon exercise of options, consideration received together with the amount previously recognized in contributed surplus is recorded as an increase to share capital.

## **Accounting for Derivative Instruments and Hedging Activities**

Cygam has not entered into any hedging arrangements.

### **Income Tax Accounting**

The determination of the Corporation's income and other tax liabilities requires interpretation of complex laws and regulations often involving multiple jurisdictions. All tax filings are subject to audit and potential reassessment after the lapse of considerable time. Accordingly, the actual income tax liability may differ significantly from that estimated and recorded by management.

### **Legal, Environmental Remediation and Other Contingent Matters**

Cygam is required to both determine whether a loss is probable, based on judgment and interpretation of laws and regulations, and determine that the loss reasonably be estimated and included in the Company's financial statements. Management continually monitors known and potential contingent matters and makes appropriate provisions by charges to earnings when warranted by circumstances.

### **Disclosure Controls and Procedures**

Disclosure controls and procedures have been designed to ensure that information required to be disclosed by the Company is accumulated and communicated to the Company's management as appropriate to allow timely decisions regarding required disclosures. The Corporation's Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO") have concluded, based on their evaluation as of the end of the period covered by this MD&A, that the Corporation's disclosure controls and procedures are effective to provide reasonable assurance that material information related to the Company, including its consolidated subsidiaries, is made known to them by others within those entities. It should be noted that while the Company's CEO and CFO believe that the Corporation's disclosure controls and procedures provide a reasonable level of assurance that they are effective, they do not expect that the disclosure controls and procedures or internal control over financial reporting will prevent all errors and fraud. A control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met.

## **OUTLOOK**

As mentioned previously, Cygam intends to focus largely on international oil and natural gas exploration. The Company plans to conduct a two-phase, success based, initial exploration program for the Italian Permits and Tunisian Permits held by Vega and ROCL as well as look for additional exploration and drilling opportunities in both Italy and Tunisia. The first phase would involve seismic acquisition and interpretation plus the drilling, testing and potential completion of one well on each of the permits acquired pursuant to the Transaction. The second phase would involve the drilling, testing and potential completion of additional wells if Cygam determines it is warranted.

Cygam's exploration plans for the remainder of 2006 in Italy and Tunisia include:

- (a) **B.R. 268 RG (Miglianico East) Permit.** The Company is currently finalizing the acquisition of approximately 300 kilometers of existing marine seismic from the previous permit operator. The seismic data will be re-interpreted and re-processed in Calgary as soon as received. An additional shallow water seismic survey may be recommended after a complete assessment of the acquired seismic data.
- (b) **Posta Nuova Permit.** Upon final ministerial approval for the permit, expected in early September, Cygam will acquire a surface drilling lease in order to drill a well in October-November. An agreement has been reached with a drilling contractor who will provide a rig for that period; tubulars and completion equipment are being secured.
- (c) **Montalbano Permit.** The Company has had technical meetings with its partners in the permit and committed to purchase and reprocess 80 kilometers of existing seismic lines and the acquisition of approximately 40 kilometers of new lines in 2007.

- (d) **Civitaquana Permit.** The Company has submitted an updated environmental assessment for this permit and expects to receive final ministerial approval in late 2006. Upon receipt of final approval, Cygam will need to purchase and reprocess 100 kilometers of existing seismic data and acquire an additional 60 kilometers of 2D seismic lines.
- (e) **d348 C.R.-VG (Aretusa) Permit .** The Company recently received preliminary ministerial approval for this new exploration permit in the Mediterranean Sea, offshore south-eastern Sicily. The Company has presented a final environmental report, necessary for the formal approval process.
- (f) **Jorf Permit.** The Company is currently re-interpreting and reprocessing all the existing seismic data on the permit. Upon final geological and geophysical assessment of large carbonate reef structures believed to exist on the Jorf block, the Company will consider shooting an additional seismic program and then commit to drill a well. Drilling rig availability is currently being investigated.
- (g) **Bazma Permit.** This concession was officially awarded to ROCL on February 24, 2006. Acquisition of all existing seismic coverage on the permit was finalized and reinterpretation and reprocessing of data has commenced. A well may be drilled on this permit, in lieu of the commitment well on the Jorf permit, in the latter part of 2006 or in early 2007, depending on rig availability.
- (h) **Sud Remada Permit.** The permit operator, Storm Ventures International Inc., is currently reviewing all geological and geophysical data on the OMZ2 well and has also conducted a geochemical sampling on known producing structures and undrilled seismic anomalies on the block. A second Silurian Acacus structure or a large Ordovician structure in the northern portion of the permit may be proposed as part of the ongoing exploration in the permit.
- (i) **Sud Tozeur Permit.** Seismic data on the permit has been received through ETAP and additional data is being requested from a previous operator. Before February 24, 2007, the Company is committed to reinterpret all existing seismic data and to acquire 50 kilometers of new seismic lines. Availability of seismic crews is not a problem in Tunisia at the present time as two companies are interested in shooting the required program. The Company will finalize the exact location of the seismic program in the next few months. In February 2007, the Company will have the option to apply for a four year exploration permit or withdraw from further commitments. It is expected that the Company will convert the prospecting licence into an exploration permit.

As noted earlier, the Company's cash balances are expected to fund only part of the estimated costs of the first phase of the proposed program and to help cover anticipated general and administrative expenses and working capital provided that Cygam can farm out portions of its prospective interests in the Italian and Tunisian Permits. Additional funds will have to be raised to proceed with the second phase and to complete the initial phase if farm-outs cannot be arranged. There is no assurance that farm-outs will be arranged or that such additional funds can be raised on reasonable terms, or at all.

On the Canadian properties, modest production increases are anticipated in the near term due to the resumption of full production at Harmattan combined with production increases at Snipe Lake resulting from infill drilling activities. Additionally, the successful completion and imminent tie-in of a development well in the South Edson unit and the potential drilling of a second development well in the same unit in late 2006 will increase Cygam's Canadian production. Production revenue is expected to continue to benefit from the higher oil prices which are currently being experienced. Natural gas prices are also expected to improve as the winter heating season approaches.