

WesternZagros Resources Ltd.**Q3 2010**

Third Quarter Interim Report
for the period ended September 30, 2010

Message to Shareholders

WesternZagros Resources Ltd. (TSX-V – WZR) ("WesternZagros" or "the Company") provides its results for the period ended September 30, 2010, key highlights, and activities to date.

On October 14, 2010, the Company safely and successfully completed well control operations at the Kurdamir-1 well, which is WesternZagros' second exploration well in the Kurdistan Region of Iraq ("Kurdistan"). The open hole in the well has been plugged and cemented up to the depth of approximately 2,500 metres, and no further drilling is planned for Kurdamir-1 at this time.

With the well control operations complete, WesternZagros is performing two series of cased hole tests of the Lower Oligocene formation in the Kurdamir-1 well. The Company is pleased with the results of its first cased hole test, which was completed in a zone between 2,365 and 2,415 metres. This test achieved a maximum flow rate, after acidization, of 18.3 million cubic feet per day of gas and a maximum yield of 86 barrels of high quality, 62 degrees API natural gas liquids (condensate), per million cubic feet of gas. No formation water was recovered during the testing. In addition, a mixture of light crude oil and condensate was recovered during the test prior to acidizing the formation. After acidizing the well, the Company interprets that the high gas flow rates and pressures prevented further oil flow. The second cased hole test is currently being performed in a zone between 2,455 and 2,470 metres to confirm the presence of the potential oil leg below the discovered gas and condensate in the Oligocene formation.

At the Kurdamir-1 well, WesternZagros encountered a number of zones of interest in addition to the Oligocene formation, with significant oil shows in the Upper Aaliji, Shiranish and Kometan formations. WesternZagros will not be testing these additional formations in Kurdamir-1 due to wellbore conditions, however further exploration of these zones remains a prime goal. WesternZagros and its co-venturers, the Kurdistan Regional Government ("KRG") and Talisman Block K44 B.V. ("Talisman"), are investigating drilling another well at Kurdamir to obtain a thorough and definitive evaluation of the potential of the structure. This well - Kurdamir-2 - is planned to be spudded after drilling the third exploration well required under the Production Sharing Contract ("PSC") that WesternZagros holds with the KRG.

WesternZagros has identified two locations, Mil Qasim and Qulijan, as potential drilling opportunities and is currently preparing to drill Mil Qasim to meet the third well commitment. The Company plans to complete site construction, well planning and the ordering of the necessary long lead items in the fourth quarter of 2010 and the first quarter of 2011, and anticipates spudding the Mil Qasim well early in the second quarter of 2011.

The Company has also revisited the results of Sarqala-1, the first well it drilled in Kurdistan, and completed a revised analysis of the oil shows in the Miocene Jeribe reservoir encountered in that well. Once the cased hole tests are completed at Kurdamir-1, and prior to moving operations to Mil Qasim, WesternZagros plans to re-enter Sarqala-1 to drill a short sidetrack to test the Jeribe.

Meanwhile, WesternZagros is actively involved in discussions with the KRG and Talisman regarding the optimum way to conduct future activities on the PSC lands. These discussions have focused on determining the timing of the third exploration commitment well; the timing for Kurdamir-2; the operator for drilling Kurdamir-2; and addressing the co-venturers' commercial concerns. The current PSC may be restructured as a result of these discussions.

“We are pursuing a win-win solution that meets the individual objectives of the government and the contractor parties,” said Simon Hatfield, WesternZagros’ Chief Executive Officer. “For WesternZagros, we are seeking flexibility on the timing for drilling our next well, to allow us to incorporate lessons learned and maximize the potential for success. We are encouraged by our recent test results at Kurdamir-1, where we have made a large gas and condensate discovery and encountered 700 metres of oil shows in deeper reservoirs. We are excited by the various opportunities ahead of us, including pursuing further exploration activities at Sarqala, where we have also encountered oil shows, Mil Qasim and Kurdamir-2.”

WesternZagros’ highlights and activities for the third quarter of 2010 to November 18, 2010 include the following:

Operations

- During the drilling of a sidetrack at the Kurdamir-1 well in the second quarter of 2010, WesternZagros encountered a high pressure hydrogen sulphide (H₂S) bearing, hydrocarbon zone. The well was shut in on April 25, 2010 while attempting to stabilize this zone. WesternZagros commenced well control operations on May 15, 2010, after the drill string parted.
- The upper 450 metre portion of the parted drill string was recovered in early July 2010. The hydraulic workover rig, known as a snubbing unit, that had been in use was subsequently removed and well control operations resumed using conventional drilling. A further 1,655 metres of drill string was recovered in early August 2010, with approximately 800 metres remaining in the well bore.
- WesternZagros safely and successfully completed well control operations at the Kurdamir-1 well on October 14, 2010. The open hole was plugged and cemented up to approximately 2,500 metres. No further drilling is planned for the Kurdamir-1 well at this time.
- Cased hole tests of the Lower Oligocene commenced at the Kurdamir-1 well on October 16, 2010. The first cased hole test was completed at depths between 2,365 and 2,415 metres. The test achieved a maximum flow rate, after acidization, of 18.3 million cubic feet per day of gas and a maximum yield of 86 barrels of high quality, 62 degrees API natural gas liquids (condensate), per million cubic feet of gas. No formation water was recovered during the testing. In addition, a mixture of light crude oil and condensate was recovered during the test prior to acidizing the formation. After acidizing the well, the Company interprets that the high gas flow rates and pressures prevented further oil flow. The second cased hole test is currently being performed in a zone between 2,455 and 2,470 metres to confirm the presence of the potential oil leg below the discovered gas in the Oligocene formation.
- The gross costs for Kurdamir-1 as of September 30, 2010 were approximately \$121 million (\$73 million net to WesternZagros). These gross costs include approximately \$66 million of incremental costs associated with well control and sidetrack activities (\$40 million net to WesternZagros). The Company is pursuing reimbursement of a significant portion of these costs under an insurance claim. WesternZagros, as operator, has notified the KRG of a force majeure event under the terms of the PSC related to the well control and subsequent sidetracking operations associated with Kurdamir-1. Under the terms of the PSC, when a force majeure event occurs, the time resulting from any such delay and the time necessary to repair any damage resulting from the delay will be added to any time period provided under the PSC, including the first exploration sub-period.

Exploration

- WesternZagros advanced its analysis of the Sarqala-1 re-entry opportunity. The analysis suggests strong oil potential in the Miocene Jeribe Formation, possibly analogous to the nearby Qamar-1 well, which flowed 2,200 barrels of oil per day from this formation.

- WesternZagros completed a basin modelling study that indicates oil was expelled from the late Cretaceous and early Tertiary source rocks during the time hydrocarbon traps were forming. As such, this study confirms the potential for oil discoveries within the Production Sharing Contract Area.
- WesternZagros is re-evaluating the hydrocarbon potential beneath the Kalar thrust as part of its overall prospective resource re-assessment of its PSC lands. WesternZagros also continues to compile seismic data and information from wells on the exploration blocks adjacent to its Production Sharing Contract Area. WesternZagros is integrating this new information, along with the reprocessed seismic data on its Production Sharing Contract Area, into its seismic interpretations to further define and update its prospects and lead inventory.

Financial

- As at September 30, 2010, WesternZagros had \$50.5 million in working capital.
- WesternZagros' share of capital expenditures for the nine months ended September 30, 2010 associated with its PSC activities and other capitalized costs was \$49.8 million, prior to insurance recoveries. Year-to-date expenditures for 2010 include \$46.2 million of drilling-related costs; \$0.7 million of geological and geosciences related work; \$1.9 million of supervision and local office costs; \$0.3 million of PSC-related costs; and \$0.7 million of corporate-related expenditures. As at September 30, 2010, the Company has recorded estimated insurance recoveries of \$37.0 million, net of deductibles, related to the year-to-date well recovery costs incurred at Kurdamir-1.

Insurance

- WesternZagros initiated an insurance claim in the first quarter of 2010 related to well control operations at Kurdamir-1, commencing when Kurdamir-1 was drilled into a high pressure formation in the Gulneri seal and continuing with the well control operations related to a subsequent additional high pressure zone in the Aaliji seal. The Company received initial confirmation of coverage for the claim from the insurers during the second quarter of 2010. The claim continued through the third quarter of 2010, including well recovery costs incurred until October 14, 2010, when the Company began completion and testing of a portion of the Kurdamir-1 well.
- As at September 30, 2010, WesternZagros had received \$15.7 million in insurance proceeds from the insurers. The Company estimated an additional receivable of \$21.3 million for interim claimable costs as at September 30, 2010. These costs, under the terms of the insurance policy, are subject to review and approval by the adjuster as appointed by the insurers. The Company continues to submit interim insurance claims as allowable costs are incurred and paid. Subsequent to September 30, 2010, the Company received \$1.2 million in insurance proceeds and has received approval for a further payment of \$6.3 million.
- The Company's maximum limit for the current insurance claim is \$45 million, of which approximately \$38.2 million has been incurred up to October 14, 2010, when the completion and testing of a portion of the well began. This leaves approximately \$6.8 million available for Kurdamir-2.

Political

It was announced on November 12, 2010, that an agreement had been reached to form a new federal government with Nouri Al-Maliki and Jalal Talabani reappointed to their respective posts as Prime Minister and President. Mr. Maliki has until December 12, 2010 in order to establish a cabinet.

- **Corporate Social Responsibility**
- During the first nine months of 2010, WesternZagros and its co-venturers **continued to focus on three key** corporate social responsibility initiatives in the Garmian region of Kurdistan - water supply, education and health care. Activities during the third quarter of 2010 included:
 - Procuring extensive local water tanker services;

- Providing low cost methods of obtaining water through extensive earthworks projects for over 40 villages;
- Implementing a partnership project with Mercy Corp, an international NGO, and the local government to improve water access to two rural villages;
- Training the community to maintain the biosand water filter project that was completed in partnership with the Kurdistan Village Reconstruction Association, a local NGO;
- Supporting the Garmian Sports Directorate's Youth Activity Festival, a seven day event attended by 1,400 children through the donation of uniforms, trophies, medals and equipment. Children learned and played various sports including football, volleyball, bicycling and basketball;
- Partnering with Project Cure, an NGO committed to donating medical equipment. The equipment included beds, examination tables, crutches, wheelchairs and IV stands. This equipment was distributed to three local clinics and one hospital in the Kalar-Bawanoor Block.

Summary of Exploration Activities Completed and Exploration Opportunities Being Pursued

Kurdamir-1

- WesternZagros began drilling the Kurdamir-1 well in May 2009, announced a large Oligocene gas and condensate discovery in November 2009, and reached a total depth of 4,077 metres in January 2010 where it encountered a high pressure formation which resulted in a well control incident. Well control operations were concluded on October 14, 2010. A cased hole test of the Lower Oligocene formation conducted in late October and November 2010 resulted in high gas flow rates and high quality condensate, and also confirmed the potential of an Oligocene oil leg in the Kurdamir structure. Technical analysis of the oil shows encountered in the well also supports the presence of oil prone reservoirs in the Upper Aaliji, Shiranish and Kometan formations. The Company is planning a second well in the Kurdamir structure to further evaluate its potential. This second well will likely take place after the Company drills its third exploration commitment well.

Sarqala-1

- WesternZagros began drilling the Sarqala-1 well in May 2008 and reached a total depth of 4,357 metres before suspending operations in early 2009. While numerous oil and gas shows were encountered, the Company was not able to test the well or penetrate all the reservoir targets. WesternZagros has since completed a promising study of the Miocene Jeribe Formation encountered at Sarqala-1 and is planning to re-enter the well in order to drill a short sidetrack and test this zone late in the fourth quarter of 2010.

About Mil Qasim

- Mil Qasim is an anticline defined from seismic data, the crest of which lies approximately three kilometres from the Sarqala-1 well. Target reservoirs are sandstones of the Upper Fars Formation, which are anticipated to be oil bearing. Testing this prospect will require a well drilled to a proposed total depth of approximately 2,400 metres, penetrating known and much simpler geology than that found at either Sarqala or Kurdamir.

About Qulijan

- Qulijan is an attractive drill-ready prospect within 12 kilometres of the Kurdamir-1 discovery well. It is an anticlinal structure with upside potential dependent on fault seal against the fault that separates it from Kurdamir. The main reservoir is Oligocene, where the Company proved hydrocarbons at the Kurdamir-1 well. It will require a well targeted to a depth of approximately 3,800 metres.

Management's Discussion and Analysis

The following management's discussion and analysis ("MD&A") reviews WesternZagros Resources Ltd.'s ("WesternZagros" or the "Company") financial condition, activities and results of operations for the period ended September 30, 2010. It should be read in conjunction with the unaudited interim consolidated financial statements for the period ended September 30, 2010, the audited consolidated financial statements for the year ended December 31, 2009 and the related notes. The effective date of this MD&A is November 18, 2010.

Forward-Looking Information

This discussion offers management's analysis of the financial and operating results of WesternZagros and contains certain forward-looking statements relating, but not limited, to operational information, future drilling plans and testing programs and the timing associated therewith, estimated Production Sharing Contract ("PSC") commitments, anticipated capital and operating budgets, anticipated insurance recoveries, anticipated working capital and estimated costs. Forward-looking information typically contains statements with words such as "anticipate", "estimate", "expect", "potential", "could", or similar words suggesting future outcomes. The Company cautions readers and prospective investors in the Company's securities to not place undue reliance on forward-looking information as, by its nature, it is based on current expectations regarding future events that involve a number of assumptions, inherent risks and uncertainties, which could cause actual results to differ materially from those anticipated by WesternZagros. Readers are also cautioned that disclosed test rates may not be indicative of ultimate production levels.

Forward looking information is based on management's current expectations and assumptions regarding, among other things, outcomes of future well operations, plans for and results of drilling activity, future capital and other expenditures (including the amount, nature and sources of funding thereof), insurance recoveries, future economic conditions, future currency and exchange rates, continued political stability, timely receipt of any necessary government or regulatory approvals, the Company's continued ability to employ qualified staff and to obtain equipment in a timely and cost efficient manner, the continued participation of the Company's co-venture partners in exploration activities and the timely receipt of insurance proceeds. In addition, budgets are based upon WesternZagros' current plans and anticipated costs, both of which are subject to change based on, among other things, the actual outcomes of well operations and the results of drilling activity, unexpected delays, availability of future financing and changes in market conditions. Although the Company believes the expectations and assumptions reflected in such forward-looking information are reasonable, they may prove to be incorrect. Forward-looking information involves significant known and unknown risks and uncertainties. A number of factors could cause actual results to differ materially from those anticipated by WesternZagros including, but not limited to, risks associated with the oil and gas industry (e.g. operational risks in exploration; inherent uncertainties in interpreting geological data; changes in plans with respect to exploration or capital expenditures; interruptions in operations together with any associated insurance proceedings; denial of any portion of the insurance claims; the uncertainty of estimates and projections in relation to costs and expenses and health, safety and environmental risks), the risk of commodity price and foreign exchange rate fluctuations, the uncertainty associated with negotiating with foreign governments and risk associated with international activity.

Readers are cautioned that the forgoing list of important factors is not exhaustive. The forward-looking statements contained in this MD&A are made as of the date of this MD&A and, except as required by law, WesternZagros does not undertake any obligation to update publicly or to revise any of the included forward-looking statements, whether as a result of new information, future events or otherwise. The forward-looking statements contained in this MD&A are expressly qualified by this cautionary statement. See the Risk Factors section of this MD&A for a further description of these risks and uncertainties facing WesternZagros. Additional information relating to WesternZagros is also available on SEDAR at www.sedar.com, including the Company's material change report dated November 25, 2009, which includes the risks and level of uncertainty associated with the Company's ability to recover resources from the PSC lands.

Overview

WesternZagros is a publicly-traded, Calgary-based, international oil and gas company engaged in acquiring properties and exploring for, developing and producing crude oil and natural gas in Iraq. WesternZagros holds a PSC with the Kurdistan Regional Government ("KRG") which covers a 2,120 square kilometre exploration block (the "Kalar-Bawanoor Block" or "PSC lands") in the Kurdistan Region of Iraq and it is on trend with, and adjacent to, a number of prolific historic oil and gas discoveries. WesternZagros (operator) holds a 40 percent working interest, the KRG holds a 20 percent working interest (carried by WesternZagros) and a wholly-owned subsidiary of Talisman Energy Inc. ("Talisman") holds the remaining 40 percent working interest.

Basis of Presentation

Reporting and Functional Currency

The reporting and functional currency of the Company is the United States ("U.S.") dollar. All references herein to US\$ or to \$ are to United States dollars and references herein to Cdn\$ are to Canadian dollars.

Going Concern Uncertainty

The financial data presented below has been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") on the basis that the Company will continue to operate as a going concern, which implies the realization of assets and the settlement of liabilities and commitments in the normal course of business for the foreseeable future. In assessing whether the going concern assumption is appropriate, management takes into account all available information about the future, which is at least, but is not limited to, twelve months from September 30, 2010.

Since inception and typical with development stage companies, the Company has incurred losses from operations and negative cash flows from operating activities, and has an accumulated deficit at September 30, 2010. During the three months ended September 30, 2010, the Company had expenditures of \$0.5 million, before net change in non-cash working capital, for operating activities and \$20.5 million for oil and gas property expenditures, and an overall increase in non-cash working capital of \$3.0 million. During the nine months ended September 30, 2010, the Company had expenditures of \$2.3 million, before net change in non-cash working capital, for operating activities and \$49.8 million for oil and gas property expenditures, as well as an overall increase in non-cash working capital of \$10.1 million. The Company will require additional funding over time to maintain ongoing exploration programs and property commitments, as well as for administration expenses. This requirement for funding will occur during the fiscal year ending December 31, 2011, with the amount dependent on the level of exploration activities pursued by WesternZagros.

There are material uncertainties that could raise significant doubt about the Company's ability to continue as a going concern, as outlined below:

Kurdamir-1 Operations

The Company has now concluded well control operations at Kurdamir-1 and is testing a portion of the well. However, the Company anticipates it will re-drill the Kurdamir structure subsequent to the drilling of its third PSC commitment well. This re-drill will require additional capital and is dependent on the Company being able to access additional funding.

Insurance Claim Related To Well Control Operations

The Company received confirmation of coverage from its insurers during the second quarter of 2010, which mitigates the uncertainty associated with the additional costs of the well recovery operations at Kurdamir-1. However, any unforeseen delays in payment from the insurers or any change in the determination of insurance coverage could impair the Company's ability to continue funding ongoing activities under the PSC. In addition, the insurance claim provides for coverage of the Company's share of allowable costs up to a maximum of \$45 million (\$75 million gross), of which approximately \$38.2 million, net to WesternZagros, has been incurred up to October 14, 2010.

Continued Participation of the Company's Co-Venturers in the PSC

WesternZagros is currently in active discussions with both Talisman and the Kurdistan Regional Government (“KRG”) on future drilling activities on its PSC lands and the timing thereof. As part of these discussions, the Company may be required to initially, or entirely, fund 100% of the costs associated with the third commitment well if Talisman elects not to participate. If these discussions are not successfully concluded, the Company will rely on the force majeure provision of the PSC to guide the timing of future activities.

Other Uncertainties

In general, the Company’s ability to continue operations and exploration activities as a going concern is dependent upon its ability to obtain additional funding over time. While the Company has been successful in obtaining its required funding in the past, there is no assurance that sufficient funds will be available to the Company in the future. The Company has no assurance that such financing will be available or be available on favourable terms. Factors that could affect the availability of financing include the continued support of its shareholders; the results of its exploration activities; meeting all commitments under the PSC; the resolution of remaining political disputes in Iraq; progress on the Federal Petroleum Law and the ability to export oil and natural gas from the Kurdistan Region of Iraq in accordance with the economic terms under the PSC; the state of the capital markets and the ability of the Company to obtain financing to develop reserves; and the timely receipt of proceeds from the current insurance claim associated with the Kurdamir-1 well control operations.

The consolidated financial statements, and associated disclosures in this MD&A, do not reflect adjustments in the carrying values of assets and liabilities reported, revenue or expenses, nor the balance sheet classification used that would be necessary if the going concern assumption was not appropriate. Such adjustments could be material.

Highlights

WesternZagros is currently exploring for crude oil and natural gas in the Kurdistan Region of Iraq and the Company currently has no reserves or production. WesternZagros’ revenue is comprised entirely of interest earned on cash and cash equivalent balances and short-term investments. WesternZagros’ highlights and activities to November 18, 2010 include the following.

Operations

- During the drilling of a sidetrack at the Kurdamir-1 well in the second quarter of 2010, WesternZagros encountered a high pressure hydrogen sulphide (H₂S) bearing, hydrocarbon zone. The well was shut in on April 25, 2010 while attempting to stabilize this zone. WesternZagros commenced well control operations on May 15, 2010, after the drill string parted.
- The upper 450 metre portion of the parted drill string was recovered in early July 2010. The hydraulic workover rig, known as a snubbing unit, that had been in use was subsequently removed and well control operations resumed using conventional techniques. A further 1,655 metres of drill string was recovered in early August 2010, with approximately 800 metres remaining in the well bore.
- WesternZagros safely and successfully completed well control operations at the Kurdamir-1 well on October 14, 2010. The open hole was plugged and cemented up to a depth of approximately 2,500 metres. No further drilling is planned for the Kurdamir-1 well at this time.
- Cased hole testing of the Lower Oligocene commenced at the Kurdamir-1 well on October 16, 2010. The first cased hole test was completed at depths between 2,365 and 2,415 metres. The test achieved a maximum flow rate, after acidization, of 18.3 million cubic feet per day of gas and a maximum yield of 86 barrels of high quality, 62 degrees API natural gas liquids (condensate), per million cubic feet of gas. No formation water was recovered during the testing. In addition, a mixture of light crude oil and condensate was recovered during the test prior to acidizing the formation. After acidizing the well, the Company interprets that the high gas flow rates and pressures prevented further oil flow. The second cased hole test is currently being performed in a zone between 2,455 and 2,470 metres to confirm the presence of the potential oil leg below the discovered gas and condensate in the Oligocene formation.

- The gross costs for Kurdamir-1 as of September 30, 2010 were approximately \$121 million (\$73 million net to WesternZagros). These gross costs include approximately \$66 million of incremental costs associated with well control and sidetrack activities (\$40 million net to WesternZagros). The Company is pursuing reimbursement of a significant portion of these costs under an insurance claim. WesternZagros, as operator, has notified the KRG of a force majeure event under the terms of the PSC related to the well control and subsequent sidetracking operations associated with Kurdamir-1. Under the terms of the PSC, when a force majeure event occurs, the time resulting from any such delay and the time necessary to repair any damage resulting from the delay will be added to any time period provided under the PSC, including the first exploration sub-period.

Exploration

- WesternZagros advanced its analysis of the Sarqala-1 well re-entry opportunity in order to test the Miocene Jeribe Formation. The analysis suggests strong oil potential, analogous to the same formation in the nearby Qamar-1 well, which flowed 2,200 barrels of oil per day.
- WesternZagros completed a basin modelling study that indicates oil was expelled from the late Cretaceous and early Tertiary source rocks during the time hydrocarbon traps were forming. As such, this study confirms the potential for oil discoveries within the Production Sharing Contract Area.
- WesternZagros is re-evaluating the hydrocarbon potential beneath the Kalar thrust as part of its overall prospective resource re-assessment of its PSC lands. WesternZagros also continues to compile seismic data and information from wells on the exploration blocks adjacent to its Production Sharing Contract Area. WesternZagros is integrating this new information, along with the reprocessed seismic data on its Production Sharing Contract Area, into its seismic interpretations to further define and update its prospects and lead inventory.

Financial

- As at September 30, 2010, WesternZagros had \$50.5 million in working capital.
- WesternZagros' share of capital expenditures for the nine months ended September 30, 2010 associated with its PSC activities and other capitalized costs was \$49.8 million, prior to insurance recoveries. Year-to-date expenditures for 2010 include \$46.2 million of drilling-related costs; \$0.7 million of geological and geosciences related work; \$1.9 million of supervision and local office costs; \$0.3 million of PSC-related costs; and \$0.7 million of corporate-related expenditures. As at September 30, 2010, the Company has recorded estimated insurance recoveries of \$37.0 million, net of deductibles, related to the year-to-date well recovery costs incurred at Kurdamir-1.

Insurance

- WesternZagros initiated an insurance claim in the first quarter of 2010 related to well control operations at Kurdamir-1, which commenced when the well was drilled into a high pressure formation in the Gulneri seal. These operations continued after a subsequent additional high pressure zone was encountered in the Aaliji seal. The Company received initial confirmation of coverage for the claim from the insurers during the second quarter of 2010. The claim continued through the third quarter of 2010, including well recovery costs incurred until October 14, 2010, when the Company began completion and testing of the Lower Oligocene formation.
- As at September 30, 2010, WesternZagros had received \$15.7 million in insurance proceeds from the insurers. The Company estimated an additional receivable of \$21.3 million for interim claimable costs as at September 30, 2010. These costs, under the terms of the insurance policy, are subject to review and approval by the adjuster as appointed by the insurers. The Company continues to submit interim insurance claims as allowable costs are incurred and paid. Subsequent to September 30, 2010, the Company received \$1.2 million in insurance proceeds and has received approval for a further payment of \$6.3 million.
- The Company's maximum limit of coverage for the current insurance claim is \$45 million, of which approximately \$38.2 million has been incurred up to October 14, 2010, when the completion and testing of

the Lower Oligocene formation began. This leaves approximately \$6.8 million available for a future Kurdamir re-drill.

Political

It was announced on November 12, 2010, that an agreement had been reached to form a new federal government with Nouri Al-Maliki and Jalal Talabani reappointed to their respective posts as Prime Minister and President. Mr. Maliki has until December 12, 2010, in order to establish a cabinet.

Corporate Social Responsibility

- During the first nine months of 2010, WesternZagros and its co-venturers continued to focus on three key corporate social responsibility initiatives in the Garmian region of Kurdistan - water supply, education and health care. Activities during the third quarter of 2010 included:
 - Procuring extensive local water tanker services;
 - Providing low cost methods of obtaining water through extensive earthworks projects for over 40 villages;
 - Implementing a partnership project with Mercy Corp, an international NGO, and the local government to improve water access to two rural villages;
 - Training the community to maintain the biosand water filter project that was completed in partnership with the Kurdistan Village Reconstruction Association, a local NGO;
 - Supporting the Garmian Sports Directorate's Youth Activity Festival, a seven-day event attended by 1,400 children, through the donation of uniforms, trophies, medals and equipment. Children learned and played various sports including football, volleyball, bicycling, and basketball;
 - Partnering with Project Cure, an NGO committed to donating medical equipment. The equipment included beds, examination tables, crutches, wheelchairs and IV stands. This equipment was distributed to three local clinics and one hospital in the Kalar-Bawanoor Block.

General and Administrative Expenses

For the three and nine month periods ended September 30, 2010, WesternZagros incurred \$1.2 million and \$4.2 million, respectively, in general and administrative ("G&A") expenses compared to \$2.4 million and \$4.8 million for the comparable periods in the prior year. G&A expenses were lower in 2010 compared to the same periods in 2009 mainly due to reduced corporate activities including legal and consulting activities, but were partially offset by a stronger Canadian dollar in 2010 which impacts a large portion of Company's G&A expenditures. On a year-to-date basis, total G&A expenses were also lower in 2010 due to reduced stock-based compensation expense compared to 2009.

Depreciation, Depletion and Amortization (DD&A)

For the three and nine month periods ended September 30, 2010, WesternZagros had \$0.1 and \$0.4 million, respectively, of depreciation related to certain administrative assets (2009: \$0.2 and \$0.6 million). No depletion is recorded on oil and gas related assets because WesternZagros has yet to determine whether proved reserves are attributable to the PSC lands.

Stock-Based Compensation

The Company recognizes stock-based compensation expense for all stock options granted, with a corresponding increase to contributed surplus. For the three months ended September 30, 2010, WesternZagros had \$0.4 million of stock-based compensation expense included in G&A and \$0.1 million in capitalized G&A, and for the nine months ended September 30, 2010, had \$0.9 million of expense and \$0.7 million in capitalized G&A. In comparison, WesternZagros had \$0.4 million of stock-based compensation expense included in G&A and \$0.5 million in capitalized G&A for the three month period ended September 30, 2009, and had \$1.2 million of expense and \$1.0 million in capitalized G&A for the nine month period ending September 30, 2009.

Foreign Exchange

WesternZagros adopted the U.S. dollar as its measurement and reporting currency because the majority of its expenses are, or will be, directly or indirectly denominated in U.S. dollars, and also to facilitate a more direct comparison to other international crude oil and natural gas exploration and development companies. WesternZagros holds over 90 percent of its cash and cash equivalents and short-term investments in U.S. dollar accounts and U.S. dollar-priced Government of Canada bonds; however, the Company has certain assets and liabilities in currencies other than the U.S. dollar, mainly Canadian dollars. These are converted to U.S. dollars at the end of each period, resulting in foreign exchange gains and losses. The Canadian dollar balances are held for the purpose of funding WesternZagros' Canadian dollar expenditures, which are mainly related to G&A costs for its head office and certain drilling-related services and tangibles procured from Canadian suppliers. In the third quarter of 2010, WesternZagros recorded a foreign exchange gain of \$0.1 million compared to a foreign exchange loss of \$0.04 million in the third quarter of 2009 relating to these conversions. In the nine months ended September 30, 2010, WesternZagros recorded a foreign exchange loss of \$0.1 million compared to a foreign exchange gain of \$0.009 million for the nine months ended September 30, 2009.

Income Taxes

For the three month period ended September 30, 2010, WesternZagros had an income tax recovery of \$0.07 million (2009: \$0.2 million expense), comprised of \$0.11 million of current income tax recovery and reduced by \$0.04 million of future income tax expense. For the nine month period ended September 30, 2010, WesternZagros had an income tax recovery of \$0.9 million (2009: \$0.8 million recovery), made up of \$1.0 million of current income tax recovery and reduced by \$0.1 million of future income tax expense. The current tax recovery relates to the expected recovery of taxes incurred in 2008 on realized foreign exchange gains and losses in WesternZagros' wholly-owned Canadian subsidiary. The tax recovery uses the associated G&A costs incurred by, and related tax pools available in, the Company's subsidiaries. The future income tax expense results from the utilization of share issuance costs in the current year to recover a portion of the current income tax expense. WesternZagros anticipates recovering the majority of the current income tax expense incurred in 2008 as it continues to incur G&A and other expenditures related to its exploration and financing activities.

Subsequent to September 30, 2010, the Company received a tax refund of Cdn\$1.5 million relating to the carry back of certain capital and non-capital losses from 2009 against the realized foreign exchange gains in the 2008 taxation year.

Revenue

WesternZagros' revenue is comprised entirely of interest earned on cash and cash equivalents. Interest of \$0.038 million was earned in the third quarter of 2010 compared to \$0.036 million in the third quarter of 2009. For the nine month period ending September 30, 2010, WesternZagros earned \$0.074 million of interest, compared to \$0.152 million in the nine months ended September 30, 2009. On a year-to-date basis, the decrease in interest income during 2010 is mainly due to the decreased balances of cash and cash equivalents. For the three month period ended September 30, 2010, interest income included interest of \$0.02 million received in relation to a prior year tax refund, which offset the decrease in interest income during the quarter associated with decreased balances of cash and cash equivalents as compared to the same period in 2009.

Net Loss

For the three month period ended September 30, 2010, WesternZagros had a net loss of \$1.1 million compared to a net loss of \$2.7 million in the third quarter of 2009. The decreased net loss was mainly due to lower G&A costs and a greater proportion of support costs allocated to capital projects during the third quarter of 2010 as compared to the same quarter of 2009. For the nine month period ended September 30, 2010, WesternZagros recorded a net loss of \$3.8 million as compared to a \$4.5 million loss in the corresponding period of 2009. This was mainly due to a greater proportion of G&A costs allocated to capital projects as well as lower stock-based compensation expense in 2010 as compared to 2009.

Capital Expenditures

For the three month period ended September 30, 2010, total capital expenditures on the Kalar-Bawanoor Block were \$32.7 million, prior to any insurance recoveries, including \$30.6 million for drilling and related operations; \$0.3 million for geological and geosciences related work (reprocessing and interpretation of seismic data); \$0.3 million for PSC-related activities; and \$1.5 million for supervision and local office costs in support of drilling operations. Included in drilling and related operations during the third quarter of 2010 were \$29.9 million for operations at Kurdamir-1, \$0.3 million for site preparation at Qulijan-1 and \$0.3 million for initial planning costs related to the Mil Qasim-1 prospect.

WesternZagros' share of capital expenditures for the three months ended September 30, 2010 associated with its PSC activities and other capitalized costs was \$20.5 million, prior to any insurance recoveries. Expenditures during the third quarter of 2010, prior to any insurance recoveries, include \$19.0 million of drilling-related costs; \$0.3 million of geological and geosciences related work; \$0.7 million of supervision and local office costs; \$0.3 million for PSC-related expenditures; and \$0.2 million of corporate-related expenditures. By comparison, WesternZagros' share of capital expenditures in the third quarter of 2009 was \$11.5 million, which included \$8.4 million of costs related to Kurdamir-1 and \$1.1 million of supervision and local office costs in support of drilling operations, and \$2.0 million for long-lead items and other tangibles for a subsequent well and consumables for testing operations.

For the nine month period ended September 30, 2010, total capital expenditures on the Kalar-Bawanoor Block were \$79.5 million, prior to any insurance recoveries, including \$73.9 million for drilling and related operations; \$0.8 million for geological and geosciences related work (reprocessing and interpretation of seismic data); \$0.3 million for PSC-related activities; and \$4.5 million for supervision and local office costs in support of drilling operations. Included in drilling and related operations during the nine months ended September 30, 2010, were \$68.6 million for operations at Kurdamir-1, \$4.8 million for Qulijan-1, \$0.3 million for initial planning costs related to the Mil Qasim-1 prospect, and \$0.2 million for other expenditures.

WesternZagros' share of capital expenditures for the nine months ended September 30, 2010 associated with its PSC activities and other capitalized costs was \$49.8 million, prior to recovery of insurance proceeds, compared to \$43.1 million for the comparable period in 2009. Year-to-date expenditures for 2010 include \$46.2 million of drilling-related costs; \$0.7 million of geological and geosciences related work; \$1.9 million of supervision and local office costs; \$0.3 million of PSC-related costs; and \$0.7 million of corporate-related expenditures.

For the nine month period ended September 30, 2010, the costs for Kurdamir-1 have been credited by approximately \$37.0 million, net to WesternZagros, for estimated claimable costs under the current insurance claim. This amount is net of deductibles.

WesternZagros capitalized \$2.2 million in G&A expenses (2009: \$2.1 million), including \$0.7 million of stock-based compensation costs (2009: \$1.0 million), directly related to exploration activities for the nine months ended September 30, 2010.

As at September 30, 2010, the Company had approximately \$147 million, net to WesternZagros, of recoverable costs available that may ultimately be recovered from future oil and natural gas sales in accordance with the terms of the PSC.

Production Sharing Contract – Summary

Under the terms of its PSC, WesternZagros has a 40 percent working interest and the KRG has a 20 percent interest in the PSC which is carried by WesternZagros. The remaining 40 percent was allocated to Talisman in June 2008 by the KRG. WesternZagros, the KRG and Talisman are collectively the “Contractor Group” under the PSC. WesternZagros is the operator of the PSC lands until the end of the first operating sub-period of the PSC, when a Joint Operating Company may be established if so elected by the Contractor Group.

Production Sharing Contract – Commercial Terms

Under the PSC, the sharing of oil occurs as follows: of the total oil produced, operations oil is available to WesternZagros for use in carrying out its obligations under the PSC; the remaining oil is subject to a 10 percent royalty payable to the KRG (the residual is considered to be “net available oil”). The net available oil is determined on a development by development basis. Up to 45 percent of the net available oil is available for cost recovery, with the remainder as “profit oil.” Expenses eligible for cost recovery include all costs and expenditures incurred by the Contractor Group for exploration, development, production and decommissioning operations, as well as any other costs and expenditures incurred directly or indirectly with these activities. The portion of profit oil available to the Contractor Group is based on a sliding scale from 35 percent to 16 percent, depending on a calculated R-Factor. The R-Factor is established by reference to the ratio of cumulative revenues over cumulative costs. When the ratio is below one, the Contractor Group is entitled to 35 percent of the profit oil. The percentage is then reduced on a linear sliding scale to a minimum of 16 percent at an R-Factor ratio of two or greater.

The production sharing terms for natural gas are the same as the oil production sharing terms except that the net gas available for cost recovery is 55 percent and the profit sharing component percentages and the R-Factor levels are increased. For natural gas, the portion of profit natural gas available for the Contractor Group is based on a sliding scale from 40 percent to 20 percent depending on a calculated R-factor. The R-Factor is established by reference to the ratio of the Contractor Group’s cumulative revenue over cumulative costs. When the R-Factor is below one, the Contractor Group is entitled to 40 percent of the profit oil. The Contractor Group’s percentage is then reduced on a linear scale to a minimum of 20 percent at a ratio of 2.75 or greater.

Production

Pursuant to the terms of the PSC, WesternZagros maintains the right to market its share of oil on the world market. There is an obligation under the PSC to make oil production available to meet regional market demand. The price of such oil is a market-based oil price based on a basket of crudes. The price for natural gas is based on local commercial value and Iraq tariffs. Currently, no markets exist for natural gas within Iraq and there is no infrastructure for export.

Contract Obligations and Commitments

The PSC contemplates two exploration sub-periods of three years and two years, respectively, with two possible one-year extensions. The first exploration sub-period ends December 31, 2010. During the first sub-period, the Contractor Group is required to complete a minimum of 1,150 kilometres of seismic surveying (which has been completed), to drill three exploration wells, and to commit a minimum of \$75 million in the aggregate on these activities. At the end of the first exploration sub-period, WesternZagros and the other parties to the PSC may relinquish the entire contract area (other than any discovery or development areas), continue further exploration operations by entering into the second exploration sub-period, or request a one-year extension for further exploration and appraisal activities prior to deciding to enter into the second exploration sub-period.

The PSC also includes capacity-building support payments, which concluded in April 2009, and annual funding for certain technological, logistical, recruitment and training support during the exploration sub-periods. To meet its remaining commitments for the first exploration sub-period, WesternZagros estimates expenditures of approximately \$15 million to \$25 million, excluding the costs associated with future activities at Kurdamir-1. Additional costs of any testing, if required, would be in addition to these amounts. This represents the Company’s 60 to 100 percent funding requirement and includes the remaining costs associated with drilling one additional

exploration commitment well by the end of the first exploration sub-period, and providing associated supervision and local office support.

WesternZagros, on behalf of the Contractor Group, has applied to the KRG to extend the first exploration sub-period for up to 12 months, i.e. to December 31, 2011, in order to allow sufficient time for drilling the flank of the Kurdamir structure to determine whether the downdip Oligocene Reservoir is oil bearing or gas-condensate bearing. The Company, on behalf of the Contractor Group, has also notified the KRG of a force majeure event under the terms of the PSC. See “Force Majeure” and “Outlook” sections in this MD&A for further information.

WesternZagros is actively involved in discussions with the KRG and Talisman regarding the optimum way to conduct future activities on the PSC lands. These discussions have focused on determining the timing of the third exploration commitment well; the timing for Kurdamir-2; the operator for drilling Kurdamir-2; and addressing the co-venturers’ commercial concerns. The current PSC may be restructured as a result of these discussions.

During the second exploration sub-period, the Contractor Group, or those parties that have elected to participate in further exploration, is required to complete a minimum of 575 kilometres of seismic surveying, drill at least two exploration wells and commit a minimum of \$35 million to these activities. At the end of the second exploration sub-period, WesternZagros, and the other parties to the PSC who have elected to participate in the second exploration sub-period, may relinquish the entire contract area (other than any discovery or development areas) or continue further exploration and appraisal operations into the extension periods subject to the following relinquishment requirements. At the end of the second exploration sub-period, and at the end of each subsequent extension period, the PSC requires WesternZagros, and other parties who have elected to participate, to relinquish 25 percent of the remaining undeveloped area within the PSC lands or the entire contract area (other than any discovery or development areas).

WesternZagros has entered into various exploration-related contracts, including contracts for drilling equipment, services and tangibles. The following table summarizes these contractual obligations as at September 30, 2010.

(\$ 000’s)	For the period ended December 31					Total
	2010	2011	2012	2013	2014+	
Exploration	3,450	500	-	-	-	3,950
Office	127	480	160	-	-	767
Total	3,577	980	160	-	-	4,717

Third Party Obligations and Commitments

In 2003, WesternZagros entered into a consulting service agreement that provides for a three percent right to indirectly participate in the future profits the Company may earn in respect to the PSC, in exchange for consulting services provided since that date. In the determination of profits under this agreement, WesternZagros is entitled to deduct the consultant’s proportional share of all costs associated with acquiring the PSC and the exploration, appraisal, development and production expenditures incurred by the Corporation (“eligible costs”), together with interest on such percentage of eligible costs at LIBOR plus three percent.

Further, in 2004, WesternZagros entered into a consulting service agreement that provides for a two percent right to indirectly participate in the future profits the Corporation may earn in respect to the PSC, in exchange for the provision of consulting services during the period 2004 to 2006. In the determination of profits under this agreement, WesternZagros is entitled to deduct one percent of all eligible costs, together with interest on such percentage of eligible costs at LIBOR plus ten percent. The consultant is required to fund the additional one percent of all eligible costs.

Off Balance Sheet Arrangement

The Company does not presently utilize any off-balance sheet arrangements to enhance its liquidity and capital resource positions, or for any other purpose. During the period ended September 30, 2010, WesternZagros did not enter into any off-balance sheet transactions.

Insurance Claim Update

WesternZagros initiated an insurance claim in the first quarter of 2010 related to the cost of well control operations at Kurdamir-1, including those when Kurdamir-1 was drilled into a high pressure formation in the Gulneri seal and the subsequent high pressure zone encountered in the Lower Aaliji seal in the subsequent sidetrack. The control of well insurance policy covering these claims has a net aggregate limit to WesternZagros of \$45 million, net of a \$0.4 million deductible. Up to October 14, 2010, when the completion and testing of a portion of the Kurdamir-1 well began, the Company had incurred approximately \$38.2 million in costs related to well control operations. This leaves approximately \$6.8 million remaining under the claim available for Kurdamir-2.

As at September 30, 2010, WesternZagros had received \$15.7 million in interim insurance payments. In addition, further total claimable costs of \$21.3 million, net to WesternZagros, have been recorded as a receivable as at September 30, 2010. These costs, under the terms of the insurance policy, are subject to review and approval by the adjuster as appointed by the insurers, and are submitted by WesternZagros as they are incurred and paid. Subsequent to September 30, 2010, insurance proceeds of \$1.2 million were received.

Force Majeure

WesternZagros, on behalf of the Contractor Group, has notified the KRG of a force majeure event under the terms of the PSC related to the well control and subsequent sidetracking operations associated with Kurdamir-1. Under the terms of the PSC, when a force majeure event occurs, the time resulting from any such delay and the time necessary to repair any damage resulting from the delay would be added to any time period provided under the PSC, including the first exploration sub-period. The period of force majeure started on January 22, 2010 and continued until October 14, 2010.

Outlook

In spite of the challenges that WesternZagros encountered while drilling its first two wells in the Kurdistan Region of Iraq, management remains confident about the prospectivity of the region and optimistic about the potential to discover and produce oil. However, the delays encountered at the Kurdamir-1 well due to well control operations resulted in it not being possible to meet the PSC requirements to drill the third commitment well prior to the end of the first exploration sub-period on December 31, 2010 unless this sub-period is extended. The Company has declared that the well control incident experienced in January, 2010, and subsequent well control operations that continued until October, 2010, constitute a force majeure event under the PSC. As such, the PSC allows for a day for day extension for every day of delay resulting from the force majeure event and, accordingly, the sub-period would be extended from December 31, 2010 until September, 2011, in order to allow sufficient time to drill the third commitment well.

WesternZagros has continued to analyze the petroleum prospectivity of the remainder of its PSC lands. WesternZagros has identified two locations, Mil Qasim and Qulijan, as potential drilling opportunities to meet the third well commitment, and is currently preparing to drill Mil Qasim. The Mil Qasim prospect, which is located nearby the first exploration well drilled by WesternZagros at Sarqala-1, is shallower and considerably less complex than other prospects WesternZagros has identified in the Kalar-Bawanoor Block. The Company plans to complete site construction, well planning and the ordering of the necessary long lead items in the fourth quarter of 2010 and the first quarter of 2011, and anticipates spudding the Mil Qasim well early in the second quarter of 2011. The Company has also revisited the results of Sarqala-1, the first well it drilled in Kurdistan, and has revised its analysis of the oil shows in the Miocene Jeribe reservoir encountered in that well. Once the cased hole tests are completed

at Kurdamir-1, and prior to moving operations to Mil Qasim, WesternZagros plans to re-enter Sarqala-1 to drill a short sidetrack to test this zone.

WesternZagros estimates its share of expenditures for the remainder of 2010 to be between \$16 million and \$18 million after insurance proceeds. This range includes \$8.2 million of costs for the continued completions and testing operations at Kurdamir-1, of which \$1.2 million is estimated to be recoverable from insurance, leaving a net cost to the Company of \$7.0 million. The remainder of the costs include approximately \$0.5 million for the preparation of Mil Qasim and \$5.8 million to initiate operations to re-enter Sarqala, with the balance associated with various other support costs.

With the objective of maximizing its options and flexibility to increase the likelihood of success, WesternZagros' priorities for the remainder of 2010 are as follows:

- Conclude testing at Kurdamir-1 to confirm the presence of the potential oil leg below the discovered natural gas and condensate in the Oligocene formation;
- Based on a promising study that WesternZagros conducted of the Miocene Jeribe Formation, re-enter the Sarqala-1 well in order to test this zone in the first quarter of 2011;
- Conclude PSC discussions with the KRG and Talisman in a manner that gives the Company flexibility around the timing of the third commitment well and provides for an orderly progression of drilling and other exploration activities to maximize the efficient use of capital; and
- The Company continues to evaluate the commercial potential of the natural gas and condensate discovered at Kurdamir-1. This evaluation has identified a potential local market for natural gas, including local cement plants, and the potential for an export market

Liquidity and Capital Resources

WesternZagros is currently exploring for crude oil and natural gas in the Kurdistan Region of Iraq and currently has no reserves, production or operational cash flows. WesternZagros' revenue is comprised entirely of interest earned on cash and cash equivalent balances. WesternZagros invests its cash and cash equivalents with major Canadian financial institutions with investment grade credit ratings and in Government of Canada instruments. This is in accordance with an Investment Policy approved by the Board of Directors. WesternZagros had no outstanding bank debt or other interest-bearing indebtedness as at September 30, 2010.

At September 30, 2010, WesternZagros had \$50.5 million in working capital. Management currently expects to use this balance to fund future capital expenditures as described in the "Outlook" section. WesternZagros is considering the proper timing to access further financial resources, including assessing the following factors:

- The conclusion of discussions with both the KRG and Talisman as it relates to the PSC and associated timing of work commitments;
- Continued reimbursement of costs under the insurance claim;
- Continued participation of the Company's co-venturers in the PSC activities;
- Capital and operating budgets, including the budget for commencing drilling activities on the third exploration commitment well;
- The completion of the recent federal election process in Iraq and the formation of a new federal government;
- The promulgation of the new Federal Petroleum Law of Iraq and the ability to export oil and natural gas from the Kurdistan Region of Iraq in accordance with the economic terms under the PSC; and

- The current conditions in the financial markets, including the potential for further market instability.

Given the potential for further market instability, ongoing PSC discussions and the continued delays in concluding the Federal Petroleum Law of Iraq, WesternZagros will seek to maintain financial flexibility and will monitor and assess its financing requirements and its ability to access additional financing as its exploration activities progress. With the successful resolution of PSC discussions and the re-entry of Sarqala-1, WesternZagros anticipates that it may require additional funding to complete the drilling of Mil Qasim (the third exploration commitment well). WesternZagros will also require additional financial resources over time to complete any appraisal programs, to potentially drill Kurdamir-2 and to ultimately fund any future development program that is warranted by discoveries at Kurdamir-1 or subsequent wells.

Future global economic events and conditions may result in further volatility in the financial markets which, in turn, could negatively impact WesternZagros' ability to access equity or debt markets over time. In addition, the results of the Company's exploration activities or any prolonged delay in the export of oil from the Kurdistan Region of Iraq in accordance with the economic terms under the PSC could negatively impact the future ability to access equity or debt markets. Any inability to access the equity or debt markets for sufficient capital, at acceptable terms and within required timeframes, could have a material adverse effect on WesternZagros' financial condition, results of operations and prospects.

Outstanding Share Data

As at September 30, 2010, there were 207,464,320 shares issued and outstanding. The number of common shares reserved for issuance pursuant to options granted will not exceed 10 percent of the issued and outstanding common shares. For the nine month period ended September 30, 2010, 85,000 stock options were granted to employees and 1,610,000 forfeited by employees bringing the total stock options outstanding as of September 30, 2010 to 11,482,334.

Supplemental Quarterly Information

The following tables summarize the key financial information on a quarterly basis for the periods indicated.

(\$ thousands, unless otherwise indicated)	Sept 30	June 30	March 31	Dec 31
	2010	2010	2010	2009
Revenue	38	17	19	32
Net Loss	1,098	1,720	1,006	1,035
Net Loss per Share (US\$/share)				
(Basic and Fully Diluted)	0.005	0.008	0.005	0.005
Capital Expenditures	20,455	16,041	13,334	11,250
Total Assets	234,555	236,006	235,977	241,077
Total Long-term Liabilities	228	207	178	175
Dividend (US\$ per share)	Nil	Nil	Nil	Nil

(\$ thousands, unless otherwise indicated)	Sept 30	June 30	March 31	Dec 31
	2009	2009	2009	2008
Revenue	36	35	81	495
Net Loss	2,712	1,404	340	6,653
Net Loss per Share (US\$/share)				

(Basic and Fully Diluted)	0.013	0.006	0.002	0.030
Capital Expenditures	11,456	14,796	16,854	20,339
Total Assets	241,600	241,171	239,288	243,697
Total Long-term Liabilities	171	197	71	69
<u>Dividend (US\$ per Share)</u>	<u>Nil</u>	<u>Nil</u>	<u>Nil</u>	<u>Nil</u>

Risk Factors

The risks factors that could influence actual results have not changed since the 2009 Annual Report and Annual Information Form including the risk that WesternZagros' ability to access the equity or debt markets in the future may be affected by further drilling challenges and related increases to exploration well costs. The financial market instability seen in the first nine months of 2010 may impact WesternZagros' ability, and that of other exploration and development companies, to access equity or debt markets at all or with acceptable terms. The inability to access the equity or debt markets for sufficient capital, at acceptable terms and within required time frames, could have a material adverse effect on WesternZagros' financial condition, results of operations and prospects.

An investment in WesternZagros should be considered highly speculative due to the nature of its activities, the present stage of its development, the need for continued participation of the Company's co-venturers in the PSC activities and its need for additional financing in the future for any acquisition, exploration, development and production of oil and gas reserves beyond current funding levels. WesternZagros' risk factors include, but are not limited to, all the risks normally incidental to the exploration, development and operation of crude oil and natural gas properties and the drilling of crude oil and natural gas wells, including geological risk, encountering unexpected formations or pressures, potential environment damage, blow-outs, fires and spills, all of which could result in personal injuries, loss of life and damage to property of WesternZagros and others; premature declines of reservoirs; environment risks; delay or changes in plans with respect to exploration or development projects or capital expenditures; the ability to attract key personnel; the risk of commodity price and foreign exchange rate fluctuations.

All of WesternZagros' assets are located in the Kurdistan Region of Iraq. As such, WesternZagros is subject to political, economic, and other uncertainties, including, but not limited to, the uncertainty of negotiating with foreign governments, expropriation of property without fair compensation, adverse determinations or rulings by governmental authorities, changes in energy policies or the personnel administering them, nationalization, currency fluctuations and devaluations, disputes between various levels of authorities, arbitrating and enforcing claims against entities that may claim sovereignty, authorities claiming jurisdiction, potential implementation of exchange controls, royalty and government take increases and other risks arising out of foreign governmental sovereignty over the areas in which WesternZagros' operations are conducted, as well as risks of loss due to civil strife, acts of war, guerrilla activities and insurrections. WesternZagros' operations may be adversely affected by changes in government policies and legislation or social instability and other factors which are not within the control of WesternZagros including, among other things, adverse legislation in Iraq and/or the Kurdistan Region, a change in crude oil or natural gas pricing policy, the risks of war, terrorism, abduction, expropriation, nationalization, renegotiation or nullification of existing concessions and contracts, taxation policies, economic sanctions, the imposition of specific drilling obligations and the development and abandonment of fields.

For a complete list of risk factors please refer to Company's Annual Information Form, which is available at www.westernzagros.com or on SEDAR at www.sedar.com.

Future Accounting Pronouncements International Financial Reporting Standards ("IFRS")

In February 2008, the Accounting Standards Board confirmed that all Canadian publicly accountable enterprises will be required to adopt IFRS for interim and annual reporting purposes for fiscal years beginning on or after

January 1, 2011. WesternZagros has performed its preliminary review on the accounting policy choices upon its conversion to IFRS for the fiscal year beginning on January 1, 2011. The implementation of IFRS 6 “Exploration for and Evaluation of Mineral Resources” (“IFRS 6”) has the potential to have the most significance to the Company’s results of operations, financial position and disclosures.

WesternZagros currently utilizes the full cost method for accounting for its exploration activities in the Kurdistan Region of Iraq under Canadian GAAP. Under the full cost method, all costs associated with the acquisition of, exploration for, and the development of crude oil and natural gas, including asset retirement obligations, are capitalized and accumulated within cost centres on a country-by-country basis. Such costs include land acquisition, geological and geophysical activity, drilling and testing of productive and non-productive wells, carrying costs directly related to unproved properties, major development projects and administrative costs directly related to exploration and development activities. As WesternZagros is only currently operating in the Kurdistan Region of Iraq and has only one PSC in that region, it has capitalized all costs associated with those exploration activities, including certain costs incurred prior to entering into the PSC.

Under Canadian GAAP, amounts capitalized under the full cost method are reviewed for impairment whenever events or conditions indicate that their net carrying amount may not be recoverable from estimated future cash flows. If impairment is identified, the assets are written down to the estimated fair market value. The calculation of these future cash flows is dependent on a number of estimates, which include reserves, timing of production, crude oil price, operating cost estimates and foreign exchange rates.

Upon conversion to IFRS, WesternZagros will be required to adopt IFRS 6, which is the standard that deals with accounting for exploration and evaluation (“E&E”) assets in the extractive industries. Typical costs included in the E&E assets are acquisition of rights to explore, topographical, geological, geochemical and geophysical studies, exploratory drilling, trenching, sampling, and activities in relation to evaluating the technical feasibility and commercial viability of extracting mineral resources. Under IFRS 6, costs incurred prior to the legal rights to explore an area being obtained may no longer be capitalized within E&E assets.

IFRS 6 allows either of two alternatives to be chosen as the accounting policy for E&E assets after initial recognition. The first alternative is the “cost model” whereby the item is carried at cost less impairment. The other alternative is the “revaluation model.” The revaluation model requires that, after initial recognition, an asset whose fair value can be reliably measured should be carried at a re-valued amount, being fair value at the date of measurement, less any subsequent accumulated depreciation or accumulated impairment losses. For the purpose of completing an impairment test under IFRS 6, the E&E assets must be allocated to specific cash-generating units (CGUs).

In July 2009, the International Accounting Standards Board (“IASB”) approved additional exemptions that will allow entities to allocate their oil and gas asset balances as determined under full cost accounting to the IFRS categories of exploration and evaluation assets and development and producing properties. Under the exemption, exploration and evaluation assets are measured at the amount determined under an entity’s previous GAAP. This exemption will relieve entities from significant adjustments resulting from retrospective adoption of IFRS. The project team has analyzed the utilization of the previous GAAP full cost accounting and intends to utilize this exemption.

During the third quarter of 2010 the project team prepared draft accounting policies for Audit Committee approval. Based upon the project teams’ initial analysis the transition to IFRS on the opening balance sheet date does not result in a material adjustment to the Company’s property and equipment.

The valuation and expensing of share-based payments will be done using a graded vesting under IFRS whereas under previous GAAP entire stock option issuances were valued as a whole and expensed on a straight line over the expected lives of the options. This results in an accelerated expensing of the share-based payments as the fair value is weighted more heavily toward the periods closer to the date of issuance of the stock options. The adjustment for the change in treatment of share-based payments results in an increase in contributed surplus with a corresponding decrease in retained earnings. The Company also continues to work on calculating adjustments for the first three quarters of 2010.

Presentation and disclosure portions of the each policy will continue to be addressed during the fourth quarter of 2010. The project team continues to work on the implementation phase, which includes determining the specific qualitative and quantitative impacts for each IFRS requirement that is relevant to the Company and anticipates completion of this prior to the issuance of the Company's December 31, 2010 consolidated financial statements. Furthermore, in the last quarter of 2010 the Company will continue to work on the development of processes and systems to ensure that IFRS comparative data is captured, and to position it for reporting under IFRS in 2011.

The Company does not anticipate significant system modifications or significant changes in internal controls upon conversion to IFRS.

INTERIM CONSOLIDATED BALANCE SHEETS
(United States dollars thousands)
(Unaudited)

	September 30, 2010	December 31, 2009
Assets		
Current Assets		
Cash and Cash Equivalents	\$ 30,100	\$ 76,708
Accounts Receivable	10,739	6,880
Insurance Recoveries Receivable (note 4)	21,270	-
Prepaid Expenses	225	183
Income Tax Recoverable	2,155	1,738
Future Income Taxes (note 7)	127	231
	64,616	85,740
Long-term Assets		
Property, Plant and Equipment (note 4)	169,519	154,911
Deposits held in trust (note 5)	420	420
Future Income Taxes (note 7)	-	6
	169,939	155,337
	\$ 234,555	\$ 241,077
Liabilities		
Current Liabilities		
Accounts Payable and Accrued Liabilities	\$ 14,011	\$ 18,297
	14,011	18,297
Long-term Liabilities		
Asset Retirement Obligation (note 6)	186	175
Future Income Taxes (note 7)	42	-
	14,239	18,472
Shareholders' Equity		
Share Capital (note 8)	253,583	253,583
Contributed Surplus (note 10)	10,284	8,749
Deficit	(43,551)	(39,727)
	220,316	222,605
	\$ 234,555	\$ 241,077

Going Concern (note 1)

Commitments and Contingencies (note 14)

See Accompanying Notes to the Interim Consolidated Financial Statements

Approved by the Board of Directors

(Signed) "Fred J. Dymert"
Director

(Signed) "Randall Oliphant"
Director

**INTERIM CONSOLIDATED STATEMENTS OF OPERATIONS,
COMPREHENSIVE LOSS AND DEFICIT**
(United States dollars thousands, except per share amounts)
(Unaudited)

	Three months ended		Nine months ended	
	September 30, 2010	September 30, 2009	September 30, 2010	September 30, 2009
Revenues				
Interest Income	\$ 38	\$ 36	\$ 74	\$ 152
Expenses				
General and Administrative	1,208	2,359	4,202	4,826
Depreciation	132	189	443	566
Accretion on Asset Retirement Obligation	4	3	11	7
Foreign Exchange (Gain) Loss	(140)	44	105	(9)
	1,204	2,595	4,761	5,390
Loss Before Income Taxes	1,166	2,559	4,687	5,238
Income Tax Expense (Recovery) (note 7)	(68)	153	(863)	(782)
Net Loss and Other Comprehensive Loss	1,098	2,712	3,824	4,456
Deficit, Beginning of Period	42,453	35,980	39,727	34,236
Deficit, End of Period	\$ 43,551	\$ 38,692	\$ 43,551	\$ 38,692
Net Loss Per Share				
– Basic and Diluted (note 11)	\$0.005	\$ 0.013	\$ 0.018	\$ 0.022

Going Concern (note 1)

See Accompanying Notes to the Interim Consolidated Financial Statements

INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS
(United States dollars thousands)
(Unaudited)

	Three months ended		Nine months ended	
	September 30, 2010	September 30, 2009	September 30, 2010	September 30, 2009
Cash Provided By (Used In)				
Cash From Operating Activities				
Net Loss	\$ (1,098)	\$ (2,712)	\$ (3,824)	\$ (4,456)
Non-cash Items				
Depreciation	132	189	443	566
Accretion on Asset Retirement Obligation (note 6)	4	3	11	7
Stock-based Compensation	385	401	880	1,193
Future Income Tax Recovery (note 7)	42	181	151	646
	(535)	(1,938)	(2,339)	(2,044)
Decrease (Increase) in Non-Cash Working Capital (note 13)	292	1,615	(273)	(6,108)
	(243)	(323)	(2,612)	(8,152)
Cash From Financing Activities				
None	-	-	-	-
Cash From Investing Activities				
Short-term Investments	-	-	-	39,967
Capital Expenditures	(20,455)	(11,456)	(49,830)	(43,106)
Insurance Recoveries (note 4)	10,284	-	15,664	-
Decrease (Increase) in Non-cash Working Capital (note 13)	(3,255)	2,675	(9,830)	9,483
	(13,426)	(8,781)	(43,996)	6,344
Decrease in Cash and Cash Equivalents				
	(13,669)	(9,104)	(46,608)	(1,808)
Cash and Cash Equivalents at Beginning of Period	43,769	97,312	76,708	90,016
Cash and Cash Equivalents at End of Period	\$ 30,100	\$ 88,208	\$ 30,100	\$ 88,208
Supplemental cash flow information:				
Income Taxes Recovered (Paid)	\$ -	\$ 1,693	\$ 598	\$ (4,669)

Going Concern (note 1)

See Accompanying Notes to the Interim Consolidated Financial Statements

NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS
Three and nine months ended September 30, 2010 and 2009
(Tabular amounts in United States dollars thousands)
(Unaudited)

1. GOING CONCERN UNCERTAINTY AND BASIS OF PRESENTATION

These interim consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles (“GAAP”) on the basis that WesternZagros Resources Ltd. (the “Corporation” or “WesternZagros”) will continue to operate as a going concern, which implies the realization of assets and the settlement of liabilities and commitments in the normal course of business for the foreseeable future.

Since inception and typical with development stage companies, the Corporation has incurred losses from operations and negative cash flows from operating activities, and has an accumulated deficit at September 30, 2010. During the three months ended September 30, 2010, the Corporation had expenditures of \$0.5 million, before net change in non-cash working capital, for operating activities and \$20.5 million for oil and gas property expenditures, as well as an overall increase in non-cash working capital of \$3.0 million. During the nine months ended September 30, 2010, the Corporation had expenditures of \$2.3 million, before net change in non-cash working capital, for operating activities and \$49.8 million for oil and gas property expenditures, as well as an overall increase in non-cash working capital of \$10.1 million. The Corporation will require additional funding over time to maintain ongoing exploration programs and property commitments, as well as for administration expenses. This requirement for funding will occur during the fiscal year ending December 31, 2011, with the amount dependent on the level of exploration activities pursued by the Corporation.

There are material uncertainties that could raise significant doubt about the Corporation’s ability to continue as a going concern, as further outlined below:

Kurdamir-1 Operations:

The Corporation has now concluded the initial well control operations at Kurdamir-1 and is testing a portion of the well. However, the Corporation anticipates it will re-drill the Kurdamir structure subsequent to the drilling of the third Production Sharing Contract (“PSC”) commitment well. This re-drill will require additional capital and is dependent on the Corporation being able to access additional funding.

Insurance Claim Related To Well Control Operations:

The Corporation received confirmation of coverage from the insurers during the second quarter of 2010, which mitigates the uncertainty associated with the additional costs of the well recovery operations at Kurdimar-1. However, any unforeseen delays in payment from the insurers or any change in the determination of insurance coverage could impair the Corporation’s ability to continue funding ongoing activities under the PSC. In addition, the insurance claim provides coverage for the Corporation’s share of allowable costs up to a maximum of \$45 million (\$75 million gross), of which approximately \$37.0 million, net to the Corporation, has been incurred up to September 30, 2010.

Continued Participation of the Company’s Co-Venturers in the PSC:

WesternZagros is currently in active discussions with both Talisman and the Kurdistan Regional Government (“KRG”) on future drilling activities on its PSC Contract Areas and the timing thereof. As part of these discussions, the Corporation may be required to initially, or entirely, fund 100% of the costs associated with the third commitment well if Talisman elects not to participate. If these discussions are not successfully concluded, the Corporation will rely on the force majeure provision of the PSC to guide the timing of future activities, refer to Note 14 - Commitments and Contingencies – for further discussion on force majeure.

Other Uncertainties:

In general, the Corporation's ability to continue operations and exploration activities as a going concern is dependent upon its ability to obtain additional funding over time. While the Corporation has been successful in obtaining its required funding in the past, there is no assurance that sufficient funds will be available to the Corporation in the future. The Corporation has no assurance that such financing will be available or be available on favorable terms. Factors that could affect the availability of financing include the continued support of its shareholders; the results of its exploration activities; meeting all commitments under the PSC; the resolution of remaining political disputes in Iraq; progress on the Federal Petroleum Law and the ability to export oil and natural gas from the Kurdistan Region of Iraq in accordance with the economic terms under the PSC; the state of the capital markets and the ability of the Corporation to obtain financing to develop reserves; and the timely receipt of proceeds from the current insurance claim associated with the Kurdamir-1 well control operations.

These consolidated financial statements do not reflect adjustments in the carrying values of assets and liabilities reported, revenue or expenses, nor the balance sheet classification used that would be necessary if the going concern assumption was not appropriate. Such adjustments could be material.

2. NATURE OF OPERATIONS

WesternZagros Resources Ltd. (the "Corporation") was incorporated on August 22, 2007 under the laws of the Province of Alberta. The Corporation, an international oil and gas company, is engaged in acquiring properties and exploring for, developing and in due course producing crude oil and natural gas in Iraq and is in the developmental stage. Through its subsidiaries, the Corporation's operations are related to its interest in a Production Sharing Contract with the Kurdistan Regional Government ("KRG") in respect of an exploration project area in the Kurdistan Region of Iraq.

3. SIGNIFICANT ACCOUNTING POLICIES

The interim consolidated financial statements are presented in accordance with Canadian generally accepted accounting principles. The interim consolidated financial statements have been prepared following the same accounting policies and methods of computation as the audited consolidated financial statements for the year ended December 31, 2009. These interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements and the notes thereto in the Corporation's annual report for the year ended December 31, 2009.

4. PROPERTY, PLANT AND EQUIPMENT

As at September 30, 2010	Cost	Accumulated Depletion and Depreciation	Net Book Value
Kurdistan Region Exploration Project	\$ 169,148	\$ -	\$ 169,148
Corporate	1,832	(1,461)	371
	\$ 170,980	\$ (1,461)	\$ 169,519

As at December 31, 2009	Cost	Accumulated Depletion and Depreciation	Net Book Value
Kurdistan Region Exploration Project	\$ 154,244	\$ -	\$ 154,244
Corporate	1,684	(1,017)	667
	\$ 155,928	\$ (1,017)	\$ 154,911

All costs included in the Kurdistan Region Exploration Project are excluded from depletion as they represent costs incurred related to properties in cost centres that are considered to be in the development stage. Currently, there are no proved reserves. All costs, net of any associated revenues, have been capitalized. The Corporation capitalized \$2.2 million of general and administrative costs (September 30, 2009 - \$2.1 million) including \$0.7 million of stock-based compensation (September 30, 2009 – \$1.0 million) directly related to exploration activities for the nine months ended September 30, 2010.

As at September 30, 2010, the Corporation had approximately \$147 million, net to WesternZagros, of recoverable costs available that may be recovered from future oil or natural gas sales in accordance with the terms of the PSC.

For the nine months ended September 30, 2010, the Corporation credited \$37.0 million of insurance recoveries related to the well recovery operations at Kurdamir-1 against the Kurdistan Region Exploration Project, net of a \$0.4 million deductible.

During the nine months ended September 30, 2010, the Corporation has received \$15.7 million of insurance proceeds from the insurers. The Company estimated an additional receivable of \$21.3 million for interim claimable costs as at September 30, 2010, net of an estimate for incurred costs that may not be claimable. These costs, under the terms of the insurance policy, are subject to review and approval by the adjuster as appointed by the insurers and are submitted by WesternZagros as they are incurred and paid. Subsequent to September 30, 2010, \$1.2 million in proceeds was received related to previously approved interim claims.

5. DEPOSITS HELD IN TRUST

The Corporation had deposited in trust certain amounts to be utilized to fund certain expenditures for drilling operations. The deposits bear interest at prevailing market rates. As of September 30, 2010, the Corporation had a \$0.4 million deposit held in trust for a supplier.

6. ASSET RETIREMENT OBLIGATION

The Corporation records the fair value of legal obligations associated with the retirement and reclamation of tangible long-lived assets when incurred. The asset retirement cost, equal to the estimated fair value of the asset retirement obligation, is capitalized as part of the cost of the related long-lived asset. The estimation of this cost is based on engineering estimates using current costs and technology and in accordance with industry practice. The Corporation's share of total undiscounted amount of estimated cash flow required to settle the obligations is \$1.2 million. The asset retirement obligations are calculated based on a weighted-average approach under the assumption that the cash out-flows required to settle the obligations are incurred either two years after inception or 25 years after inception, with the most likely case that the obligations are paid in the years 2033 and 2034. The Corporation used a credit risk adjusted risk-free rate of 10 percent and an inflation factor of 4 percent to calculate the net present value of the future retirement obligation.

The following table presents the reconciliation of the Corporation's asset retirement obligation:

	September 30, 2010	December 31, 2009
Balance, beginning of year	\$ 175	\$ 69
Liabilities incurred	-	95
Accretion expense	11	11
Balance at end of period	\$ 186	\$ 175

7. INCOME TAXES

	Three months ended		Nine months ended	
	September 30, 2010	September 30, 2009	September 30, 2010	September 30, 2009
Current Income Tax Recovery	\$ (111)	\$ (28)	\$ (1,014)	\$ (1,428)
Future Income Tax Expense	43	181	151	646
	\$ (68)	\$ 153	\$ (863)	\$ (782)

Future Income Tax assets are comprised of:

As at	September 30, 2010	December 31, 2009
Current Future Income Tax Asset:		
Non-Capital Loss Carryforwards	\$ -	\$ 27
Share Issue Costs	127	204
	\$ 127	\$ 231

As at	September 30, 2010	December 31, 2009
Long-term Future Income Tax Asset (Liability):		
Share Issue Costs	\$ 310	\$ 387
Book Values in Excess of Tax Values	(169)	(198)
Valuation Allowance	(183)	(183)
	\$ (42)	\$ 6

8. SHARE CAPITAL

a. Authorized

The Corporation is authorized to issue an unlimited number of common and preferred shares. The common shares are without nominal or par value.

b. Common Shares Issued and Outstanding

	Number of Shares	Amount (000's)
Balance as at December 31, 2009 and September 30, 2010	207,464,320	\$ 253,583

9. STOCK OPTIONS AND STOCK-BASED COMPENSATION

Pursuant to the stock option plan, the Board of Directors may grant options to directors, officers, other employees and other service providers. The aggregate number of shares that may be reserved for issuance pursuant to stock options may not exceed 10 per cent of the issued and outstanding common shares on a non-diluted basis of the Corporation at the time of granting. Stock options expire not more than five years from the date of grant, or earlier if the individual ceases to be associated with the Corporation, and vest at the discretion of the Board of Directors.

No new options were granted during the third quarter of 2010, while 1,001,666 options were forfeited. The following table presents the reconciliation of stock options granted as of September 30, 2010:

Nine Month Period Ended	Number of Options	Weighted Average exercise price (\$CAD)
Outstanding, beginning of the year	13,007,334	\$ 1.50
Granted	85,000	0.50
Exercised	-	-
Forfeited	(1,610,000)	1.59
Expired	-	-
Outstanding, end of period	11,482,334	\$ 1.48

The fair value of all options granted have been estimated at the grant date using the Black-Scholes option pricing model and are summarized in the following table:

Nine Month Period Ended	September 30, 2010
Weighted average fair value of stock options granted	\$0.28
Risk Free Interest Rate	2.00%
Expected Life	3 years
Expected Volatility	88%
Dividend Per Share	Nil

10. CONTRIBUTED SURPLUS

The following table presents the reconciliation of Contributed Surplus:

Nine Month Period Ended	September 30, 2010
Balance, beginning of year	\$ 8,749
Stock-based Compensation	1,535
Balance, end of period	\$ 10,284

11. LOSS PER SHARE

The basic weighted average number of common shares outstanding calculated for the three and nine month period ended September 30, 2010 was 207,464,320 (September 30, 2009 - 207,464,320). In computing diluted per share amounts, the Corporation's options totaling 11,482,334 (September 30, 2009 – 12,766,000) have been excluded as anti-dilutive. Accordingly, no additional common shares were added to the basic weighted average shares outstanding to account for dilution.

12. SHAREHOLDER RIGHTS PLAN

On October 18, 2007, the Corporation adopted a shareholder rights plan (the "Plan"). Under the Plan, one right has been issued in respect of each currently issued common share and one right will be issued with each additional common share which is issued. The rights remain attached to the common shares and are not exercisable or separable unless one or more of certain specified events occur. If a person or group acting in concert acquires 20 per cent or more of the common shares of the Corporation, the rights will entitle the holders thereof (other than the acquiring person or group) to purchase common shares at a substantial discount from the then market price. The rights are not triggered by a "Permitted Bid" as defined in the Plan. The Plan will remain in effect until termination of the annual meeting of shareholders in 2013, unless extended by resolution of the shareholders at such meeting.

13. CHANGES IN NON-CASH WORKING CAPITAL

	Three months ended		Nine months ended	
	September 30, 2010	September 30, 2009	September 30, 2010	September 30, 2009
Operating Activities				
Accounts Receivable	\$ 233	\$ (241)	\$ 186	\$ (174)
Prepaid Expenses	170	91	(42)	166
Income Tax Receivable	(111)	1,762	(417)	(1,417)
Accounts Payable and Accrued Liabilities	-	3	-	(4)
Income Tax Payable	-	-	-	(4,679)
	\$ 292	\$ 1,615	\$ (273)	\$ (6,108)
Investing Activities				
Accounts Receivable	\$ (908)	\$ 542	\$ (4,045)	\$ 4,896
Accounts Payable and Accrued Liabilities	(2,347)	2,133	(5,785)	4,587
	\$ (3,255)	\$ 2,675	\$ (9,830)	\$ 9,483

14. COMMITMENTS AND CONTINGENCIES

Commitments

a) Production Sharing Contract

Under the terms of its PSC, the Corporation has a 40 percent working interest and the KRG has a 20 percent interest in the PSC which is carried by the Corporation. The remaining 40 percent was allocated to a wholly-owned subsidiary of Talisman by the KRG as announced on June 23, 2008. The Corporation, the KRG and Talisman are collectively the "Contractor Group" under the PSC. WesternZagros is the operator of the PSC lands until the end of the first operating sub-period of the PSC, when a Joint Operating Company may be established if so elected by the Contractor Group.

The PSC contemplates two exploration sub-periods of three years and two years, respectively, with two possible one-year extensions. The first exploration sub-period ends December 31, 2010. During the first sub-period, the Contractor Group is required to complete a minimum of 1,150 kilometres of seismic surveying (which has been completed), to drill three exploration wells, and to commit a minimum of \$75 million in the aggregate on these activities. At the end of the first exploration sub-period, the Corporation and the other parties to the PSC may relinquish the entire contract area (other than any discovery or development areas), continue further exploration operations by entering into the second exploration sub-period, or request a one-year extension for further exploration and appraisal activities prior to deciding to enter into the second exploration sub-period.

The PSC also includes capacity building support, which concluded in April 2009, and annual funding for certain technological, logistical, recruitment and training support during the exploration sub-periods. To meet its remaining commitments for the first exploration sub-period, the Corporation estimates expenditures of approximately \$15 million to \$25 million, excluding the costs associated with future activities at Kurdamir-1. Additional costs of any testing, if required, would be in addition to these amounts. This represents the Corporation's 60 to 100 percent funding requirement and includes the remaining costs associated with drilling one additional exploration commitment well by the end of the first exploration sub-period, and providing associated supervision and local office support.

WesternZagros, on behalf of the Contractor Group, has applied to the KRG to extend the first exploration sub-period for up to 12 months, i.e. to December 31, 2011, in order to allow sufficient time for drilling the flank of the Kurdamir structure to determine whether the downdip Oligocene Reservoir is oil bearing or gas-condensate bearing. The Corporation, on behalf of the Contractor Group, has also notified the KRG of a force majeure event under the terms of the PSC. See the “Force Majeure” section below for further information.

During the second exploration sub-period, the Contractor Group, or those parties who have elected to participate in further exploration, is required to complete a minimum of 575 kilometres of seismic surveying, drill at least two exploration wells and commit a minimum of \$35 million to these activities. At the end of the second exploration sub-period, the Corporation and the other parties to the PSC who have elected to participate in the second exploration sub-period, may relinquish the entire contract area (other than any discovery or development areas) or continue further exploration and appraisal operations into the extension periods subject to the following relinquishment requirements. At the end of the second exploration sub-period, and at the end of each subsequent extension period, the PSC requires the Corporation, and other parties who have elected to participate, to relinquish 25 percent of the remaining undeveloped area within the PSC lands or the entire contract area (other than any discovery or development areas).

Force Majeure

The Corporation, on behalf of the Contractor Group, has notified the KRG of a force majeure event under the terms of the PSC related to the well control and subsequent sidetracking operations associated with Kurdamir-1. Under the terms of the PSC, when a force majeure event occurs, the time resulting from any such delay and the time necessary to repair any damage resulting from the delay would be added to any time period provided under the PSC, including the first exploration sub-period. The period of force majeure started on January 22, 2010 and continued until October 14, 2010.

b) Consulting Service Agreements

In 2003 the Corporation entered into a consulting service agreement that provides a three percent right to indirectly participate in the future profits the Corporation may earn in respect to the PSC, in exchange for consulting services provided since that date. In the determination of profits under this agreement, the Corporation is entitled to deduct the consultant's proportional share of all costs associated with acquiring the PSC and the exploration, appraisal, development and production expenditures incurred by the Corporation (“eligible costs”), together with interest on such percentage of eligible costs at LIBOR plus three percent.

Further, in 2004 the Corporation entered into a consulting service agreement that provides a two percent right to indirectly participate in the future profits the Corporation may earn in respect to the PSC, in exchange for the provision of consulting services during the period 2004 to 2006. In determination of profits under this agreement, the Corporation is entitled to deduct one percent of all eligible costs, together with interest on such percentage of eligible costs at LIBOR plus ten percent. The consultant is required to fund the additional one percent of all eligible costs.

c) Other

The Corporation has entered into various exploration-related contracts, including contracts for drilling equipment, services and tangibles. The following table summarizes the commitments the

Corporation has under these exploration-related contracts and other contractual obligations at September 30, 2010:

	For the Years Ending December 31,					Total
	2010	2011	2012	2013	2014+	
Exploration	3,450	500	-	-	-	3,950
Office	127	480	160	-	-	767
	<u>3,577</u>	<u>980</u>	<u>160</u>	<u>-</u>	<u>-</u>	<u>4,717</u>

Contingencies

Litigation

From time to time the Corporation may become involved in legal or administrative proceedings in the normal conduct of business. Amounts involved in such matters are not reasonably estimable due to uncertainty as to the final outcome. The Company's assessment of the likely outcome of these matters is based on its judgment of a number of factors, including precedents and facts specific to the matters. The Corporation does not believe these matters, individually or in aggregate will have a material adverse effect on its consolidated financial position or results of operations.

Regulatory

Oil and gas operations are subject to extensive controls and regulations imposed by various levels of government that may be amended from time to time. The Corporation's operations may require licenses and permits from various governmental authorities in the countries in which it operates. Under the PSC, the KRG is obligated to assist in obtaining all permits and licenses from any government agencies in the Kurdistan Region and from any other government administration in Iraq. There can be no assurance that the Corporation will be able to obtain all necessary licenses and permits that may be required to carry out exploration and development of its projects.

The political and security situation in Iraq is unsettled and volatile. The Kurdistan Region is the only "Region" of Iraq that is constitutionally established pursuant to the Iraq Constitution, which expressly recognizes the Kurdistan Region. The political issues of federalism and the autonomy of the Regions of Iraq are matters about which there are major differences between the various political factions in Iraq. These differences could adversely impact the Corporation's interest in the Kurdistan Region including the ability to export any hydrocarbons as a result of our activities.

15. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Financial instruments of the Corporation consist of cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities. The Corporation's cash and cash equivalents are designated as held-for-trading and are measured at fair value, which approximates carrying value due to the short-term nature of these instruments. The fair value of cash and cash equivalents is classified as Level I fair value measurement. Accounts receivable are designated as loans and receivables and recorded at amortized cost, which approximates fair value due to the short term nature of the instrument. Accounts payable and accrued liabilities are designated as other liabilities and are recorded at amortized cost. The fair value of accounts payable and accrued liabilities approximate their carrying values due to the short term nature of these instruments.

The Corporation is exposed to credit risk, interest rate risk, market risk, liquidity and funding risk. The following is a description of those risks and how the Corporation manages exposure to them:

Credit Risk

Credit risk is the risk of loss associated with counterparty's inability to fulfill its payment obligations. The Corporation is currently exposed to credit risk on its cash and cash equivalents, to the extent that these balances are invested with various institutions. The Board of Directors of the Corporation has approved an Investment Policy to dictate the various types of instruments and institutions that can be invested in and monitors these against this policy on a regular basis. Currently, the Corporation has entered into transactions for cash equivalents with major Canadian financial institutions with investment grade credit ratings, as well as purchases Government of Canada instruments.

Under the terms of the PSC, as described in note 14, the KRG elected a wholly-owned subsidiary of Talisman as the third party participant under the PSC. The Corporation is subject to credit risk associated with Talisman's 40 percent interest in the PSC and its share of related expenditures. As at September 30, 2010, the Corporation had \$10.7 million of receivables outstanding mostly from Talisman under the credit terms defined by the PSC, including penalty provisions for any amount in default.

Market and Interest Rate Risk

Market risk is the risk of loss that may arise from changes in market factors such as interest rate, foreign exchange rates and equity or commodity prices. The Corporation is exposed to interest rate risk to the extent that changes in market interest rates will impact any interest earned on the Corporation's cash and cash equivalent. The Corporation is also exposed to foreign exchange risk, as the majority of costs are anticipated to be incurred in U.S. dollars and the funds it will have available to it may be in other currencies.

The Corporation's Investment Policy dictates the various types of instruments and institutions that can be invested in and monitors these against this policy on a regular basis. The Board of Directors has also approved a Foreign Exchange Policy to dictate the currencies held by the Corporation and the instruments that can be utilized by the Corporation to meet day to day needs. This Foreign Exchange Policy requires the Corporation to hold the majority of its cash and cash equivalents in U.S. dollars and sets out the type and duration of instruments that can be used to meet the Corporation's day to day foreign exchange needs. The Foreign Exchange Policy does allow the Corporation to hold other balances, mainly Canadian dollars, to meet the requirements to fund ongoing general and administrative and other spending requirements in these currencies. Neither policy permits the Corporation to enter into any economic hedging as it relates to interest or foreign exchange risks. As at September 30, 2010, had the U.S. Dollar changed by one percent against the Canadian dollar, with all other variables held constant, the Corporation's foreign exchange gain or loss would have been affected by approximately \$24,000.

The marketability and price of oil and natural gas that may be acquired or discovered by the Corporation is, and will continue to be, affected by numerous factors beyond its control including the impact that the various levels of government may have on the ultimate price received for oil and gas sales. The Corporation's ability to market its oil and natural gas may depend upon its ability to secure transportation. The Corporation may also be affected by deliverability uncertainties related to the proximity of its potential production to pipelines and processing facilities and operational problems affecting such pipelines and facilities as well as potential government regulation relating to price, the export of oil and natural gas and other aspects of the oil and natural gas business.

Both oil and natural gas prices are subject to wide fluctuation. During 2010, both oil and gas prices remained somewhat volatile with West Texas Intermediate ranging from \$68 to \$86 per barrel. WesternZagros originally negotiated the economic terms of its PSC in 2007 in a \$50 per bbl crude oil price environment and any significant and sustained decline in crude oil prices from this price may impact the feasibility of WesternZagros' business plan.

Liquidity and Funding Risks

Liquidity and funding risk is the risk that the Corporation may be unable to generate or obtain sufficient cash or its equivalent in a timely and cost-effective manner to meet its commitments as they come due. As the Corporation is engaged in acquiring properties and exploring for crude oil and natural gas and is in the developmental stage, it currently does not have a revenue source outside of interest on its cash and cash equivalent and short-term investment balances. The Corporation is therefore required to fund its share of all

commitments from existing balances or access additional sources of cash from the equity markets. The Board of Directors reviews the Corporation's cash and cash equivalent balances against the Corporation's commitments and assesses the timing and need for additional equity financing on a regular basis. However, the Corporation's results will impact its ability to access the capital necessary to meet these commitments. There can be no assurance that debt or equity financing will be available or sufficient to meet these requirements or for other corporate purposes or, if debt or equity financing is available, that it will be on terms acceptable to the Corporation. In recent years, the capital markets have seen a period of significant market instability. The Corporation's ability to access the capital markets in the future may be affected by any prolonged period of market instability. The inability of Corporation to access sufficient capital for its operations could have a material adverse effect on the Corporation's financial condition, results of operations and prospects. Additionally, the Corporation currently expects to re-drill the Kurdamir structure in the future after first drilling the third commitment well required under the PSC. The Corporation will have to raise funds in order to be able to complete the re-drill.

16. CAPITAL STRUCTURE

The Corporation's capital consists of shareholder's equity and working capital. The Corporation will adjust its capital structure to manage its drilling program through the issuance of shares and adjustments to capital spending.

The Corporation's objectives when managing its capital structure are to:

- i) Ensure adequate levels of available cash and cash equivalents and short-term investments to meet the Corporation's commitments under the PSC.
- ii) To prudently fund expenditures related to the acquisition of properties, and for exploration, appraisal and development of crude oil and natural gas resources.

The Corporation funds its share of expenditures of all commitments from existing cash and cash equivalent balances received primarily from issuances of shareholders' equity. The Corporation has not entered into any debt financing arrangements at the balance sheet date and is not subject to any externally imposed capital requirements.

The Board of Directors regularly reviews the Corporation's cash and cash equivalents against the Corporation's expenditure commitments and assesses the timing and need for additional equity financing. The Corporation's results will impact its access the capital necessary to meet these expenditure commitments. There can be no assurance that equity financing will be available or sufficient to meet those commitments, or for other corporate purposes, or if equity financing is available, that it will be on terms acceptable to the Corporation. The inability of the Corporation to access sufficient capital for its operations could have a material adverse impact on the Corporation's financial condition, results of operations and prospects. During 2010 the capital markets have continued to see a period of market instability. The Corporation's ability to access the capital markets in the future may be affected by any prolonged period of market instability.

17. CHANGE IN FINANCIAL STATEMENT PRESENTATION

Certain comparative information has been changed in conformity to the current year financial statement presentation.

Corporate Information

<p>Officers</p> <p>M. Simon Hatfield Chief Executive Officer</p> <p>Greg Stevenson Chief Financial Officer</p> <p>Lianne Tysowski Corporate Secretary</p> <p>Directors</p> <p>David Boone President & CEO Barrick Energy Inc. Calgary, Alberta</p> <p>Fred Dymont Chairman WesternZagros Resources Ltd. Calgary, Alberta</p> <p>John Frangos Independent Businessman Calgary, Alberta</p> <p>M. Simon Hatfield Chief Executive Officer WesternZagros Resources Ltd. Calgary, Alberta</p> <p>James Houck President and Chief Executive Officer The Churchill Corporation Calgary, Alberta</p> <p>Randall Oliphant Executive Chairman and Director New Gold Inc. President and Chief Executive Officer Silver Bear Resources Inc. Toronto, Ontario</p> <p>William Wallace Independent Businessman Glenwood Springs, Colorado</p>	<p>Head Office</p> <p>WesternZagros Resources Ltd. Suite 600, 440 – 2nd Ave. S.W. Calgary, Alberta T2P 5E9 Phone: (403) 693-7001 Fax: (403) 233-0174 Website www.westernzagros.com</p> <p>Auditors</p> <p>PricewaterhouseCoopers LLP Calgary, Alberta</p> <p>Resource Evaluators</p> <p>Sproule International Ltd. Calgary, Alberta</p> <p>Legal Counsel</p> <p>Macleod Dixon LLP Calgary, Alberta</p> <p>King & Spalding LLP Houston, Texas</p> <p>Transfer Agent And Registrar</p> <p>Valiant Trust Company Calgary, Alberta</p> <p>Stock Exchange Listing</p> <p>TSX Venture Exchange Common Shares: WZR</p>
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