

MANAGEMENT'S DISCUSSION AND ANALYSIS

November 6, 2006

The following is Management's Discussion and Analysis ("MD&A") of Iteration Energy Ltd. (the "Company" or "Iteration") operating and financial results as at and for the three and nine month periods ended September 30, 2006 as well as information and estimates concerning the Company's future outlook based on currently available information. This discussion should be read in conjunction with Iteration's unaudited consolidated financial statements as at and for the three and nine months ended September 30, 2006 and the audited consolidated financial statements as at and for the year ended December 31, 2005, together with accompanying notes. Readers should also refer to Iteration's 2005 Annual Information Form and Management's Discussion and Analysis for the year ended December 31, 2005. All financial information is reported in Canadian dollars, unless noted otherwise, and in accordance with Canadian generally accepted accounting principles ("GAAP").

Certain amounts in prior periods have been reclassified to enable comparison with the current period's presentation.

Natural gas is converted to crude oil equivalent at a ratio of six thousand cubic feet to one barrel. Boe's may be misleading, particularly if used in isolation. A boe conversion ratio of 6 mcf: 1 bbl is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.

Additional information about Iteration Energy Ltd. filed with Canadian securities commissions, including periodic quarterly and annual reports and the Annual Information Form (AIF), is available on-line at www.iterationenergy.com and at www.sedar.com.

ITERATION OVERVIEW

Iteration is a Canadian oil and gas company with focus areas in Northeast British Columbia/Northwest Alberta and in East Central Alberta. The most significant currently producing properties are Boundary Lake, Bernadet and Rigel in Northeast British Columbia and Wild River and Atmore in Alberta.

The Company strives to operate its properties whenever possible and to maintain high working interests. Iteration believes this high level of operatorship can translate to controlling costs, timing of capital outlays and projects as well as providing competitive advantages for future opportunities.

Acquisition of East Central Alberta Assets

Pursuant to a purchase and sale agreement dated June 6, 2006, on June 27, 2006 the Company purchased certain petroleum and natural gas properties and related assets in east central Alberta ("East Central Alberta Assets") from an unrelated oil and gas company. The gross purchase price was \$42,325,000, subject to adjustments. The adjusted purchase price was \$42,048,000. The Company assumed an asset retirement obligation of \$2,510,000 associated with this acquisition. The acquisition was initially funded by bank debt. The Company commenced reporting production from this acquisition July 1, 2006.

Issuance of 6,200,000 Subscription Receipts

Pursuant to a short form prospectus dated June 22, 2006, the Company issued 6,200,000 subscription receipts for gross proceeds of \$25,110,000 on June 28, 2006. The subscription receipts were converted into common shares after the closing of the acquisition of the East Central Alberta Assets. The East Central Alberta Asset acquisition closed on June 27, 2006. The net proceeds of the offering were applied to reduce bank debt of the Company incurred in connection with the acquisition of the East Central Alberta Assets.

Acquisition of Iteration Energy Inc.

On March 21, 2005, the Company purchased all of the issued and outstanding shares of Iteration Energy Inc. in exchange for the issuance of 5,750,000 common shares of Iteration and 5,000,000 warrants. The 5,750,000 shares of Iteration are subject to an escrow agreement and are being released as to a third of the issued shares on each of March 20, 2006, 2007 and 2008, respectively. The performance warrants have a term of 42 months and an exercise price of \$2.90 per share. The warrants vested on May 7, 2005. In

conjunction with this acquisition, the Company granted 4,610,000 stock options with an exercise price of \$2.90 to the employees of Iteration Energy Inc. that joined Iteration. The stock options vest over a three-year period and expire after five years.

Divestiture of Lavoy Area Assets

Pursuant to two asset sale agreements dated March 21, 2005, the Company sold its Lavoy area assets to two unrelated third parties for cash consideration totaling \$85.0 million, with an effective date of January 1, 2005. The net proceeds received from the asset sale were \$80.8 million after adjustments for operating results and capital expenditures between the effective date and the closing date of March 24, 2005.

FINANCIAL AND OPERATING HIGHLIGHTS

Operational Overview

The quarter ended September 30, 2006 was a period of continued growth for the Company. Production from the East Central Alberta acquisition properties has increased more than 60% through workovers and recompletions since closing on June 27, 2006. The overall Company production increased by 20% to 4,680 boed for the third quarter with a September 30 exit rate of 5,100 boed.

Highlights for the Quarter

The major highlights of the three months ended September 30, 2006 were as follows:

- Drilled 10.6 net gas wells and 2.0 net heavy oil wells with a success rate of 86.3%.
- Increased quarter over quarter production by 20% to 4,680 boed, and quarter over quarter exit rate by 13 % to 5,100 boed.
- There was significant upside creation on the recent acquisition of five properties in East Central Alberta;
 - Workovers and recompletions of the southern two properties increased production by over 60 % to 1160 boed by the quarter end. Total cost for adding approximately 450 boed was about \$1.8 million or \$4,000 per boed. Plans are in place for a workover and recompletion program on the three northern properties this winter.
 - The workovers associated with ramping up this production, together with the high facility maintenance costs, pushed operating costs in the third quarter for the Company up to \$9.57 per boe, a 59% increase from the amount reported for the first half of 2006. They will remain high through the winter as work is done on the northern properties.
- Increased the Company's land base to approximately 300,000 net acres, 177,000 of which are undeveloped.
- Negotiated a significant farm-in deal in northeast British Columbia whereby the Company will earn a 70% interest in 9,500 acres of land for a five well commitment.
- Average netback realized during the quarter was \$21.72 per boe, which resulted in funds flow for the quarter of \$7.7 million (\$0.14 per share).

Financial Highlights

The Lavoy property was disposed of on March 24, 2005. Accordingly, the financial results for the period from January 1 to March 24, 2005 include the results of Lavoy. In order to facilitate an understanding of the Company's operating results on a go forward basis, the Lavoy results have been split out in the following table and the Company's analysis of results in this management discussion and analysis has focused on changes that were not as a result of the Lavoy disposition.

	Three months ended Sept 30,		Nine Months Ended Sept 30,			
	2006	2005	2006	2005	2005	2005
	Total	Total	Total	Excluding Lavoy	Lavoy	Total
Financial						
(\$thousands, except as noted)						
Production revenue before royalties	\$16,888	\$14,231	\$46,600	\$36,947	\$8,380	\$45,327
Funds from operations ⁽²⁾	\$7,676	\$8,782	\$24,637	\$19,372	\$6,023	\$25,395
Per Share (\$) ⁽¹⁾						
- basic	\$0.14	\$0.18	\$0.48	\$0.41	\$0.13	\$0.54
- diluted	\$0.14	\$0.17	\$0.48	\$0.41	\$0.13	\$0.54
Net earnings (loss)	\$(2,370)	\$1,518	\$(1,193)	\$(1,231)	\$779	\$(452)
Per Share (\$) ⁽¹⁾						
- basic	\$(0.04)	\$0.03	\$(0.02)	\$(0.03)	\$0.02	\$(0.01)
- diluted	\$(0.04)	\$0.03	\$(0.02)	\$(0.03)	\$0.02	\$(0.01)
Royalties	\$3,041	\$3,351	\$9,795	\$8,458	\$1,649	\$10,107
Production expense	4,122	987	8,260	3,946	829	4,775
Transportation expense	337	10	883	411	-	411
General and admin	1,270	1,224	2,692	3,936	-	3,936
Depletion	11,352	5,638	28,471	17,943	5,542	23,495
Total assets			\$223,163			\$161,234
Capital expenditures:						
Property acquisition	\$(46)	-	\$51,087			-
Exploration, development and other	\$16,789	\$10,210	\$47,877	\$16,643	\$1,998	\$18,641
Shares outstanding						
Common shares Sept 30			55,129,847			48,828,681
Weighted average – basic	55,129,847	48,823,964	51,689,169			47,158,531
Weighted average – diluted ⁽¹⁾	55,129,847	51,402,963	51,689,169			47,158,531
Warrants Sept 30			5,000,000			5,000,000
Stock options Sept 30			5,389,222			4,881,291

(1) For periods with positive net earnings, per share amounts are based on weighted average basic and diluted common shares outstanding for the period. For periods with a net loss, per share amounts are based on basic common shares outstanding for the period.

(2) Management uses funds from operations and funds from operations per share (before changes in non-cash working capital and asset retirement expenditures) to analyze operating performance and leverage. Funds from operations and funds per share as presented do not have any standardized meaning prescribed by Canadian GAAP and therefore they may not be comparable with the calculation of similar measures for other entities. Funds from operations as presented is not intended to represent operating cash flow or income from operations for the period nor should it be viewed as an alternative to cash flow from operating activities, net

earnings or other measures of financial performance calculated in accordance with Canadian GAAP. All references to funds from operations and funds per share throughout this MD&A are based on cash flow from operating activities before changes in non-cash working capital and asset retirement expenditures.

Operating Highlights

	Three months ended Sept 30,		Nine months ended Sept 30			
	2006	2005	2006	2005	2005	2005
	Total	Total	Total	Excluding Lavoy	Lavoy	Total
Operating						
Gas Production						
Total natural gas (bcf)	2.4	1.4	6.2	4.3	1.2	5.6
Daily average natural gas (mcf/d)	26,087	15,810	22,873	15,875	4,727	20,602
Average price (\$/mcf)	6.16	9.03	6.61	7.77	6.48	7.48
Oil and Liquids Production						
Total oil and liquids (Mbbbls)	30.6	18.1	89.0	66.4	.8	67.2
Daily average oil and liquids (bbls/d)	332	197	327	243	3	246
Average price oil and liquids (\$/bbl)	65.76	67.40	59.39	55.00	23.47	54.63
Daily Average Production (boed)	4,680	2,830	4,140	2,890	790	3,680
Land						
Undeveloped land holdings			177,200			70,600
Drilling						
Wells drilled (net)						
Gas	10.6	8.0	18.8			10.0
Oil	2.0	-	5.0			-
Dry	2.0	-	3.6			-
Total	14.6	8.0	27.4			10.0
Success rate (%)	86.3	100.0	86.9			100.0

Quarterly Financial Data

(\$ thousands except per share data)

Quarter ended	2006			2005			2004	
	Sept 30	June 30	Mar 31	Dec 31	Sept 30	June 30	Mar 31	Dec 31
Including Lavoy								
Revenues	\$16,888	\$12,394	\$17,317	\$20,719	13,956	\$10,939	\$20,157	\$20,035
Net earnings (loss)	(2,370)	(1,472)	2,649	4,271	1,519	473	(2,443)	(2,955)
Net earnings (loss) per common share – basic and diluted (\$)	(0.04)	(0.03)	0.05	0.09	0.04	0.01	(0.06)	(0.07)

Excluding Lavoy

Revenues	\$16,888	\$12,394	\$17,317	\$20,719	13,956	\$10,939	\$11,777	\$13,371
Net earnings (loss)	(2,370)	(1,472)	2,649	4,271	1,519	473	(3,222)	(1,936)
Net earnings (loss) per common share – basic and diluted (\$)	(0.04)	(0.03)	0.05	0.09	0.04	0.01	(0.06)	(0.04)

OPERATING RESULTS (EXCLUDING LAVOY)**Net Earnings (Loss)**

Iteration's net loss for the three months ended September 30, 2006 was \$2.4 million, as compared to net earnings (after adjusting for Lavoy) of \$1.5 million for the three months ended September 30, 2005. Although production was 65% higher during the quarter, as compared to the prior year, the financial results were impacted by lower realized natural gas prices and also by higher operating costs associated with increasing production on the recent East Central Alberta acquisition and major repairs to compressors at Boundary Lake. Third quarter results also reflect an additional charge of \$439,000 to reduce estimated overhead recoveries recorded in the first half of 2006. Of this amount, \$248,000 related to capital expenditures incurred during the first quarter and \$191,000 related to capital expenditures incurred in the second quarter.

Production

Average daily production for the three months ended September 30, 2006 increased by 1,850 boed as compared to the three months ended September 30, 2005. This 65% increase included production from the acquisition of the East Central Alberta assets, a transaction that closed June 27, 2006. The production increase was further enhanced by the workovers and recompletions work undertaken in East Central Alberta during the quarter, which increased production from these properties from approximately 650 boed at closing in late June 2006 to over 1,150 boed by the end of September 2006.

Daily Production (excluding Lavoy) <i>Average for the period</i>	Three months ended Sept 30,			Nine months ended Sept 30,		
	2006	2005	% Change	2006	2005	% Change
Natural Gas (Mcf/d)	26,087	15,810	65	22,873	15,875	44
Crude oil and natural gas liquids (bbl's/d)	332	197	69	327	243	35
Total (boed)	4,680	2,830	65	4,140	2,890	43

The Company has previously issued production guidance of expected average production of between 4,400 and 4,600 boed for 2006, with an expected exit rate of between 5,400 and 5,800 boed, based on capital expenditures of \$123 million. With the recent reduction in gas prices, the Company has decided to defer a portion of its fourth quarter drilling to 2007 in order to maintain a strong balance sheet. With the reduced drilling program, we now expect to be at the low end of the range listed above with average production for 2006 of approximately 4,400 boed and year end production of approximately 5,400 boed. Capital spending for the year is expected to reduce by \$8 million to \$115 million. Although drilling of some wells has been deferred, the Company is continuing to prepare and license a number of additional drilling locations so that it is in the position to accelerate its drilling plans if warranted by gas prices.

Commodity Prices

Industry Benchmarks <i>Average for the period</i>	Three months ended Sept 30,			Nine months ended Sept 30,		
	2006	2005	% Change	2006	2005	% Change
Natural gas (Alberta Spot)						

Cdn\$/GJ at AECO	5.72	8.37	(37)	6.75	7.30	(8)
Edmonton Light Crude Cdn\$/bbl	71.88	76.64	(6)	67.23	68.02	(1)

Realized Commodity Prices	Three months ended Sept 30,			Nine months ended Sept 30,		
<i>Average for the period</i>	2006	2005	% Change	2006	2005	% Change
Natural Gas (\$/Mcf)	6.16	8.94	(31)	6.61	7.41	(15)
Crude oil and natural gas liquids (\$/bbl's)	65.76	67.26	(2)	59.39	54.64	9
Total (\$/boed)	39.22	54.65	(28)	41.24	45.12	(9)

The realized commodity price for natural gas for the quarter decreased by less than the benchmark due to the impact of the positive heating differential realized on our Boundary Lake production, offset by an increasing pricing differential for British Columbia production. The realized commodity price for the nine months ended September 30th decreased by more than the change in the benchmark pricing due to fluctuations in the pricing differential for British Columbia gas.

The realized commodity price for crude oil and natural gas liquids decreased by less than the change in the benchmark due to a higher percentage of natural gas liquids versus crude oil production. However, as a greater percentage of the Company's oil production will be coming from heavy oil (as a result of our drilling operations in Central Alberta) going forward, we expect the realized price per bbl for crude oil and natural gas liquids to decrease in the future.

Revenue

Production revenue was \$16.9 million for the three months ended September 30, 2006, compared with \$14.2 million for the three months ended September 30, 2005. The production revenue increase was due to higher production in the quarter, which was offset by lower commodity prices realized by the Company during the quarter.

Production Revenue before Royalties	Three months ended Sept 30,			Nine months ended Sept 30,		
<i>(\$ thousands)</i>	2006	2005	% Change	2006	2005	% Change
Production revenue	16,888	14,231	19	46,600	36,947	26

For the three months ended September 30, 2006 and 2005, natural gas production accounted for 93% of the Company's total production. However, for the three months ended September 30, 2006, natural gas production accounted for 87% of production revenue versus 91% for the three months ended September 30, 2005. The decline in the amount of revenue from natural gas production is a reflection of the weaker commodity prices which were realized in the third quarter. For 2006 budget purposes, based on a conversion ratio of 6 mcf of gas being taken as equivalent to 1 barrel of oil, the Company continues to project that 93% of production will be gas and 5% will be from NGL's. Approximately 2% of production is projected to be from oil.

Royalties

Royalty expense, net of Alberta Royalty Tax Credit, was \$3.0 million for the three months ended September 30, 2006, compared with \$3.3 million for the three months ended September 30, 2005. The relatively little change in royalty expense for the quarter is the result of increased production during the quarter, offset by lower commodity prices for natural gas.

However the decrease in the percentage of royalty expense to production revenue during the quarter is the result of;

- 1) The royalty rates on the East Central Alberta assets acquired in June are in the range of 19%, versus the Company average rate of 22%.
- 2) The royalty rates on the heavy oil wells brought on production during the quarter are 13%.
- 3) One of the oil wells drilled in Boundary Lake was granted exploratory status and, therefore, is exempt from crown royalties for a period of 2 years.

Royalties (\$ thousands except where noted)	Three months ended Sept 30,			Nine months ended Sept 30,		
	2006	2005	% Change	2006	2005	% Change
Royalties	3,041	3,351	(9)	9,795	8,458	16
Per boe (\$/boe)	7.06	12.86	(45)	8.67	10.84	(20)
Percentage of revenue (%)	18	23	(22)	21	23	(9)

For 2006 guidance purposes, the Company projects that royalty rates will decrease slightly compared to 2005 and will be in the range of 20 to 22% of 2006 production revenue.

Production Expenses

Production expenses were \$4.2 million for the three months ended September 30, 2006, compared with \$0.9 million for the three months ended September 30, 2005. While a portion of the increase in expenses was due to the 65 % increase in production during the quarter, the increase was also due to the following:

- 1) A number of major overhauls and repairs were required at the Boundary Lake compressor stations as a result of increased gas production, which increased the gas throughput to levels close to the maximum rated capacity for the plant.
- 2) Operating costs of the East Central Alberta assets were \$9.50 per boe at the time of the acquisition. Considerable extra costs were incurred during the initial phase of ramping up production on the summer access properties. A similar two to three month spike is expected for the 2006-07 winter access period when the Company undertakes similar work on the northern properties. Lower operating costs are expected thereafter.

Production expenses (\$ thousands)	Three months ended Sept 30,			Nine months ended Sept 30,		
	2006	2005	% Change	2006	2005	% Change
Field operating costs	3,987	896	345	7,863	3,795	107
Allocated general and administrative expense	135	91	48	397	151	163
Total production expense	4,122	987	317	8,260	3,946	109

Production expenses per boe (\$ per boe)	Three months ended Sept 30,			Nine months ended Sept 30,		
	2006	2005	% Change	2006	2005	% Change
Field operating costs	9.26	3.44	169	6.96	4.81	45
Allocated general and administrative expense	0.31	0.35	(11)	0.35	0.19	84
Total production expense	9.57	3.79	153	7.31	5.00	46

The Company has given previous guidance of an expected average operating cost of \$6.40 for 2006. With the unusually high costs experienced during the third quarter, and the continuation of efforts being undertaken at East Central Alberta, the Company now expects average costs of \$7.50 per boe for 2006 and the first quarter of 2007. However, after the completion of well servicing procedures at East Central Alberta, operating costs are expected to reduce to closer to the \$6.50 per boe level.

Production expenses reported for the three months ended September 30, 2005 were unusually low reflecting reduced activity of the Company following the corporate restructuring. Production expenses for the year ended December 31, 2005 averaged \$7.84.

Operating Netback

The operating netback (before general and administrative expenses) realized for the three months ended September 30, 2006 was \$21.72/boe versus \$37.96/boe for the three months ended September 30, 2005. The decrease in netback realized was primarily due to softening of natural gas prices with an additional reduction due to higher per barrel production costs, as was more fully discussed above.

Operating Netback (\$/boe)	Three months ended Sept 30,			Nine months ended Sept 30,		
	2006	2005	% Change	2006	2005	% Change
Production revenue	39.22	54.65	(28)	41.24	45.12	(9)
Royalties	(7.06)	(12.86)	(45)	(8.67)	(10.84)	(20)
Production costs	(9.57)	(3.79)	153	(7.31)	(5.00)	46
Transportation costs	(0.87)	(0.04)	2075	(0.78)	(0.41)	90
Operating netback	21.72	37.96	(43)	24.48	28.87	(15)

For guidance purposes, net backs for 2006, before general and administration expenses, based on 2006 projected average prices of AECO (spot) \$6.33/GJ for gas, and Edmonton Light of \$60 per barrel for oil, are projected to average \$23.96 per boe. Previously, management had projected an average price for AECO (spot) of \$7.43 per GJ for gas, which resulted in an estimated net back of \$31.20 per boe.

General and Administrative Expenses

General and administrative expenses were \$1.3 million for the three months ended September 30, 2006, compared with \$1.2 million for the three months ended September 30, 2005. During the third quarter, Management revised its estimate of general and administrative expenses associated with the Company's own interests that could be capitalized. As a result, an adjustment of \$439,000 was made in the quarter to reduce estimated recoveries recorded in the first half of 2006, and increased general and administrative expenses. Of this amount \$248,000 related to capital expenditures incurred during the first quarter and \$191,000 related to capital expenditures incurred in during the second quarter. As a result of this entry, general and administrative expense per boe was \$2.94 per boe for the three months ended September 30, 2006 as compared to \$4.70 for the three months ended September 30, 2005. Not including the adjustment for capital overhead recoveries reported in the first half of the year, general administrative expense per boe for the third quarter would have been \$1.96. (For purposes of calculating general and administrative expenses per boe, all general and administrative expenses incurred during the period and total production for the period, including Lavoy production has been used.) The reasons for the decrease were:

- a) Where the Company is operator of a property, it is allowed to invoice partners an overhead recovery based on capital expenditures incurred on a well as well as a monthly overhead recovery for operating the well. With the increase in capital spending, as well as an increase in the number of wells, the portion of general and administrative expenses recovered from partners has increased.
- b) The production for the third quarter has increased 65% from the previous year. The additional personnel required by the Company to maintain this production were all hired earlier in the year. As a result, as production levels ramp up, the rates per boe for general and administrative expenses decreases.

Management is continuing its efforts to streamline general and administrative functions within the organization. Despite the lower general and administrative costs realized during the second and third quarter, management expects significant costs to be incurred during the fourth quarter in performing the processes suggested by National instrument 52-109 as it relates to the documentation and testing of internal financial controls. With the incurrence of these incremental costs, management continues to expect general and administrative expenses will remain under \$2.25 per boe for 2006. As production continues to increase, lower general and administrative expenses per boe are expected for 2007.

General and administrative expenses <i>(\$ thousands except where noted)</i>	Three months ended Sept 30,			Nine months ended Sept 30,		
	2006	2005	% Change	2006	2005	% Change
General and administrative expenses before the following	1,598	2,037	(22)	4,788	5,748	(17)
Overhead recoveries	(107)	(139)	(24)	(309)	(361)	(14)
Adjustment to first quarter capital overhead recovery	248	-	NA	-	-	NA
Adjustment to second quarter capital overhead recovery	191	-	NA	-	-	NA
Allocation to operating expenses	(135)	(202)	(33)	(397)	(146)	172
Capitalized overhead	(525)	(472)	11	(1,390)	(1,305)	7
Net general and administrative expense	1,270	1,224	3	2,692	3,936	(32)
Per boe (\$ / boe)	2.94	4.70	(37)	2.38	3.92	(39)

Stock Based Compensation Expense

As approved by the Company's shareholders, the stock option plan was amended effective April 1, 2004 to provide stock option holders the choice, upon exercise, to receive a cash payment in exchange for surrendering the option. The cash payment is equal to the appreciated value of the stock option, as determined by the difference between the option's exercise price and the Company's closing share price the day prior to electing to exercise the option. In July, 2005, the stock option plan was further amended to cap the total number of options that may be outstanding at 10 % of the issued and outstanding Common Shares at that time.

For the three months ended September 30, 2006, a recovery of stock based compensation expense of \$0.2 million was recorded based on the reduction in value of the outstanding stock options as determined using the September 30, 2006 closing share price, as compared to the closing share price at June 30, 2006. Future fluctuations in the stock based compensation expense or recoveries are dependent on the movement of the Company's share price and the number of vested options outstanding. Based on the September 30, 2006 share price of \$3.85, had all 5,389,222 stock options outstanding been vested, stock based compensation expense and a corresponding liability of \$4.4 million would have been recognized. Of this amount, \$2.2 million has been recognized as a current liability, and reported as part of accounts payable, in the September 30, 2006 financial statements.

During the quarter, the Company granted 504,000 “conditional” stock options to employees, none of whom are officers, at an exercise price of \$4.35 per share. The options have a three year vesting period and a term of four years. These options are conditional because the granting of these options has resulted in the number of common shares available to be issued under the stock option plan exceeding the maximum number allowed (currently 10% of issued and outstanding common shares). The conditional nature of these options can only be removed by ratification of the granting of the options to the employees by the shareholders of the Company at the 2007 annual general meeting. In the event that the shareholders do not ratify the Shareholder Proposal with respect to these conditional options, all of the conditional options granted will immediately and automatically terminate without payment.

These conditional options have not been included in the calculation of the effect of dilutive options for purposes of calculating weighted average common shares outstanding as the result would not be dilutive.

Concurrent with the granting of the options, the Board has adopted a stock appreciation rights (“SAR”) plan and granted 504,000 stock appreciation rights to the employees who were granted the conditional options, with the same exercise price, vesting conditions and term as the options. Upon the exercise of each SAR, the employee will be entitled to receive a cash payment equal to the difference between the closing price of the common shares on the date immediately preceding the date of exercise, and the exercise price of \$4.35 per SAR. In the event that the shareholders ratify the Shareholder proposal with respect to the conditional options, all SAR’s granted will immediately and automatically terminate without payment and the options granted will remain in effect.

No obligation has been recorded by the Company either with respect to the conditional options or the SAR’s because as at September 30, 2006, the market value of the common shares of the Company was less than the exercise price of the conditional options and SAR’s.

Interest Expense

Interest expense on current debt (the Company had no long term debt) for the three months ended September 30, 2006 was \$0.5 million as compared to \$0.02 million for the three months ended September 30, 2005. (For purposes of calculating interest expense per boe, Lavoy production for the period January 1 to March 24, 2005 has been included). Interest expense increased as a result of utilizing a portion of its \$50 million credit facility to fund the capital drilling program and the acquisition of the East Central Alberta Assets.

Interest expense (<i>\$ thousands except where noted</i>)	Three months ended Sept 30,			Nine months ended Sept 30,		
	2006	2005	% Change	2006	2005	% Change
Interest expense	471	19	2379	698	607	15
Per boe (\$/boe)	1.09	0.07	1457	0.62	0.60	3

Depletion

Depletion and depreciation expense was \$11.4 million for the three months ended September 30, 2006 compared to \$5.6 million for the three months ended September 30, 2005. The increase in the amount of depletion recorded was due to the magnitude of capital spending undertaken by the Company during the fourth quarter of 2005 and the first three quarters of 2006, combined with higher production during 2006 three and nine month periods as compared to 2005.

Depletion (<i>\$ thousands except where noted</i>)	Three months ended Sept 30,			Nine months ended Sept 30,		
	2006	2005	% Change	2006	2005	% Change
Depletion	11,352	5,638	101	28,471	17,943	59

Per boe (\$/boe)	26.36	21.65	22	25.20	22.17	14
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Capital Expenditures

Exploration and development capital spending for the three months ended September 30, 2006 were \$17.4 million, versus \$10.2 million for the three months ended September 30, 2005.

Capital Expenditures (\$ thousands)	Three months ended Sept 30,			Nine months ended Sept 30,		
	2006	2005	% Change	2006	2005	% Change
Acquisition of oil and gas properties	(46)	-	NA	51,087	-	NA
Exploration and development expenditures	16,789	10,210	65	47,877	16,643	188
Total	16,743	10,210	64	98,964	16,643	494

With the current weakness of commodity prices, the Company has reassessed its proposed capital spending program for the balance of 2006 and the first quarter of 2007. As a result of this reassessment, the 2006 projected capital program, inclusive of acquisitions to date, has been decreased from \$123 million to \$115 million. The decrease has been achieved by the following:

- 1) The deferral of drilling of several wells until later in 2007.
- 2) A reduction in the amount of capital allocated to land and seismic acquisitions.
- 3) With the reduction in commodity prices, the costs of providing capital services have started to decrease. With these decreases, the Company has sent out requests for new bids on a number of planned capital programs.

Capital and Liquidity

The capital program will be financed by a combination of cash on hand, cash flow from operations and draws on the Company's \$50 million credit facility which was established with a Canadian Chartered Bank during the second quarter in connection with the acquisition of the East Central Alberta Assets.

For guidance purposes the Company has used projected average prices for 2006 of \$6.33/GJ AECO (spot) for gas and \$60 per bbl for Edmonton Light oil. Based on projected 2006 projects, the impact on the Company's estimated fourth quarter funds flow, reported in previous guidance as \$11 million, of a \$1.00/GJ swing in AECO (spot) is approximately \$3.8 million.

The Company has entered into various operating leases with respect to its premises. The leases expire June 30, 2009 and require the following future minimum lease payments, by calendar year (\$'000's);

2006	\$ 172
2007	687
2008	687
2009	344

Related Party Transactions

For the three months ended September 30, 2006, there were no related party transactions.

Outstanding Common Shares

As at November 3, 2006, there were 55,129,847 common shares, 5,000,000 warrants, 5,376,222 stock options and 478,000 conditional stock options or SARS outstanding.

Critical Accounting Estimates

The Company calculates the asset retirement obligation based on estimates of the date of abandonment, abandonment costs, and inflation. These amounts are then discounted to a present value amount. The estimates used are as follows:

Abandonment and reclamation costs:

Well bore and surface reclamation	\$ 35,000 per well
Pipelines	10,000 per pipeline segment
Roads	15,000 per km
Batteries	15,000 per battery
Compressors	200,000 per compressor

Inflation	2 % per annum
Discount rate	6% per annum

The Company also calculates the ceiling test on reserves based upon estimates of future prices for commodities, production rates, royalty rates, operating costs and inflation rates. Future prices for commodities are based on forward curve amounts. Future production rates, decline rates, royalty rates and operating costs are based on historical amounts. Inflation for commodity prices is 2.5% per annum, and 2% per annum for operating costs.

Outlook for 2006

The initial work to return the Company to active operations and profitability has been completed. The major focus is now on adding new drilling locations and prospective lands in order to grow production through an ongoing exploitation and exploration program. The Company is aggressively pursuing acquisition and farm-in opportunities in its core areas, and will continue to be active at landsales. The planned 2006 capital program of \$115 million is expected to result in a year over year production growth, net of the Lavoy disposition, in excess of 45%, with average production expected to be approximately 4,400 boed. The Company continues to expect year end production to be approximately 5,400 boed.

Directors, Officers and Auditors

Current Officers and Directors of the Company are as follows;

Officers

Brian Illing	President and CEO
Mark Ariss	VP Exploration East
Sean Johnson	CFO
Jane Mactaggart	VP Exploitation
Carmen McKay-Illing	VP Corporate Affairs
Kevin Stromquist	VP Exploration West

Directors

Pat Breen P. Eng.	President- Foremost Income Fund
Dallas Droppo Q.C.	Partner- Blake, Cassels and Graydon LLP
Jim Grenon	President- TOM Capital Associates
Michael Hibberd	President- MJH Services Inc.
Brian Illing P. Geol	President and CEO- Iteration Energy Ltd.
Robert Waters CA	Senior VP and CFO- Enerplus Resource FundCorporate

Secretary

Tony Grenon	Managing Director- TOM Capital Associates
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Auditors

Ernst & Young LLP

Advisory – Forward-Looking Information

This MD&A was prepared on November 6, 2006 and is management's assessment of Iteration's historical financial and operating results. The reader should be aware that historical results are not necessarily indicative of future performance. This MD&A contains forward-looking statements relating to future events or future performance. In some cases, forward-looking statements can be identified by terminology such as "may", "will", "should", "expects", "projects", "plans", "anticipates" and similar expressions. These statements represent management's expectations or beliefs concerning, among other things, future operating results and various components thereof affecting the economic performance of Iteration. Undue reliance should not be placed on these forward-looking statements which are based upon management's assumptions and are subject to known and unknown risks and uncertainties, including the business risks discussed below, which may cause actual performance and financial results in future periods to differ materially from any projections of future performance or results expressed or implied by such forward-looking statements. Accordingly, readers are cautioned that events or circumstances could cause results to differ materially from those predicted. The Company undertakes no obligation, except as required by applicable securities legislation, 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 herein are expressly qualified by this cautionary statement. Readers are cautioned that the following list of risk factors is not exhaustive.

In particular, this discussion contains forward-looking statements and information pertaining to the following:

- The quantity and recoverability of our reserves;
- The timing and amount of future production;
- Prices for natural gas produced;
- Operating and other costs;
- Business strategies and plans of Management;
- Supply and demand of natural gas;
- Expectations regarding our ability to raise capital and to add to our reserves through acquisitions as well as exploration and development;
- The focus of capital expenditures on development activity rather than exploration;
- The sale, farming in, farming out or development of certain exploration properties using third party resources;
- The use of development activity and acquisitions to replace and add to reserves;
- The impact of changes in natural gas prices on cash flow after hedging;
- Drilling plans;
- The existence, operations and strategy of the commodity price risk management program;
- The approximate and maximum amount of forward sales and hedging to be employed;
- The Company's acquisition strategy, and the criteria to be considered and the benefits to be derived;
- The impact of Canadian federal and provincial governmental regulation on the Company relative to other issuers of similar size;
- Our treatment under governmental regulatory regimes;
- The goal to sustain or grow production and reserves through prudent management and acquisition;
- The emergence of accretive growth opportunities; and
- The Company's ability to benefit from the combination of growth opportunities and the means to grow through the capital markets.

Iteration's actual results could differ materially from those anticipated in our forward-looking statements as a result of the risk factors set forth below and elsewhere in this MD&A which include but are not limited to:

- Volatility in market prices for natural gas;
- Risks inherent in our operations;
- Uncertainties associated with estimating reserves;
- Competition for, among other things: capital, acquisitions of reserves, undeveloped lands and skilled personnel;
- Incorrect assessments of the value of acquisitions;
- Geological, technical, drilling and process problems;
- General economic conditions including fluctuations in the price of natural gas;
- Royalties payable in respect of Iteration's production;
- Governmental regulation of the oil and gas industry, including environmental regulation;
- Fluctuation in foreign exchange or interest rates;
- Unanticipated operational events that can reduce production or cause production to be shut-in or delayed;
- Stock market volatility and market valuations; and
- The need to obtain required approvals from regulatory authorities.

Additional Information on the Company

Other information about the Company, including the Management's Discussion and Analysis and the revised Annual Information Form for the year ended December 31, 2005, and Management's discussion and analysis for the quarter ended March 31, 2006 and June 30, 2006, which is available through the internet on the Company's SEDAR profile at www.sedar.com.