

GRAN TIERRA ENERGY, INC.  
Form 10QSB  
November 17, 2006

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

**FORM 10-QSB**

(Mark One)

QUARTERLY REPORT UNDER SECTION 13 OR 15 (d)  
OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2006

TRANSITION REPORT UNDER SECTION 13 OR 15(d)  
OF THE EXCHANGE ACT

For the transition period from \_\_\_\_\_ to \_\_\_\_\_.

Commission file number 333-111656

**GRAN TIERRA ENERGY, INC.**  
(Exact name of small business issuer as specified in its charter)

Nevada  
(State or other jurisdiction of  
incorporation or organization)

Applied For  
(IRS Employer  
Identification No.)

300, 611 10<sup>th</sup> Avenue SW  
Calgary, Alberta, Canada T2R 0B2  
(Address of principal executive offices)

(403) 265-3221  
(Issuer's telephone number)

Check whether the small business issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the small business issuer was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

As of September 30, 2006, the latest practicable date, 95,455,759 of the issuer's common shares, \$.001 par value, were issued and outstanding.

Transitional Small Business Disclosure Format (Check one):

Yes  No

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**Gran Tierra Energy Inc.**  
**Condensed Consolidated Statement of Operations (Unaudited)**  
**Stated in US dollars**

	<b>Three months ended</b>		<b>Nine months ended</b>	
	<b>September 30,</b>		<b>September 30, 2006 and the</b>	
	<b>2006</b>	<b>2005</b>	<b>period from January 26 to</b>	<b>September 30, 2005</b>
	<b>\$</b>	<b>\$</b>	<b>\$</b>	<b>\$</b>
<b>Revenue</b>				
Oil and Natural Gas Sales	5,219,308	349,263	8,358,921	349,263
Interest Revenue	175,641	—	195,816	—
	5,394,949	349,263	8,554,737	349,263
<b>EXPENSES</b>				
Operating Expenses	1,259,888	125,000	2,702,507	125,000
General and Administrative	1,764,856	414,397	4,256,303	668,908
Interest Expenses	2,765	—	3,075	—
Depreciation, Depletion and Accretion	1,449,694	111,843	2,324,158	115,209
Foreign Exchange (gain)/loss	273,684	(24,703)	277,526	(21,064)
	4,750,887	626,537	9,563,569	888,053
<b>INCOME/(LOSS) BEFORE</b>				
<b>INCOME TAXES</b>	644,062	(277,274)	(1,008,832)	(538,790)
Income Taxes (Note 8)	710,417	7,370	848,200	7,370
<b>NET INCOME/(LOSS)</b>	(66,355)	(284,644)	(1,857,032)	(546,160)
<b>NET EARNINGS/(LOSS) PER</b>				
<b>SHARE</b>				
Basic	0.00	(0.02)	(0.03)	(0.11)
Diluted	0.00	(0.02)	(0.03)	(0.11)
Weighted average number of shares - Basic	95,455,759	12,083,333	63,043,998	4,903,297
Weighted average number of shares - Diluted	130,612,674	12,083,333	98,200,913	4,903,297

*See accompanying Notes to the Financial Statements*

**Gran Tierra Energy Inc.**  
**Condensed Consolidated Balance Sheets (Unaudited)**  
**Stated in US dollars**

	<b>September 30,</b> <b>2006</b>	<b>December 31,</b> <b>2005</b>
	\$	\$
<b>ASSETS</b>		
<b>CURRENT</b>		
Cash and cash equivalents	18,796,084	2,221,456
Restricted cash	12,617,263	400,427
Accounts receivable	7,137,920	808,960
Inventory	586,943	447,012
Prepaid expenses	247,073	42,701
Total Current Assets	39,385,283	3,920,556
Taxes Receivable	165,919	108,139
Property Plant and Equipment (Note 5)		
Proven oil and gas properties, net	25,859,978	7,886,914
Unproven oil and gas properties not amortized	18,292,211	-
Other, net	499,146	426,294
Goodwill	15,005,083	-
Deferred Income Taxes	-	29,228
	99,207,620	12,371,131
<b>LIABILITIES</b>		
<b>CURRENT</b>		
Accounts payable	6,486,464	1,142,930
Accrued liabilities	1,367,368	121,122
Taxes Payable	1,708,955	-
	9,562,787	1,264,052
Long term Payables	76,147	-
Asset Retirement Obligation (Note 7)	121,655	67,732
Deferred Income Taxes (Note 8)	7,849,421	-
Deferred Remittance Taxes	1,385,849	-
Total Liabilities	18,995,859	1,331,784
<b>SHAREHOLDERS' EQUITY</b>		
Share capital (Note 6)	95,455	43,285
Additional Paid in Capital	71,361,463	11,807,313
Warrants (Note 6)	12,831,553	1,408,429
Deficit	(4,076,711)	(2,219,680)
	80,211,760	11,039,347
	99,207,620	12,371,131

*See accompanying Notes to the Financial Statements*

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**Gran Tierra Energy Inc.**  
**Condensed Consolidated Statements of Cash Flows (Unaudited)**  
**Stated in US dollars**

	<b>Nine Months ended September 30,</b>	<b>For the Period from January 26, 2005 to September 30, 2005</b>
	<b>2006</b>	
	<b>\$</b>	<b>\$</b>
<b>CASH FLOWS RELATED TO THE FOLLOWING ACTIVITIES:</b>		
<b>OPERATING:</b>		
Net (loss) earnings	(1,857,032)	(546,160)
Adjustments for:		
Depreciation, Depletion and Accretion	2,324,158	115,209
Stock-based compensation	203,306	-
Deferred Income Taxes	123,193	-
Asset Retirement Obligation, settled	(9,218)	-
Taxes Receivable	(57,780)	-
Changes in non-cash working capital (Note 9)	1,497,304	(192,732)
	2,223,931	(623,683)
<b>FINANCING</b>		
Short term loan	-	6,655,223
Proceeds from issuance of common shares and warrants, net of issuance costs	70,826,137	1,713,412
	70,826,137	8,368,635
<b>INVESTING</b>		
Property and equipment additions, net of asset retirement obligation assumed	(6,011,735)	(6,934,542)
Other	(28,940)	-
Business Combination, net of cash acquired (Note 3)	(38,217,930)	-
Restricted Cash	(12,216,835)	(377,491)
	(56,475,440)	(7,312,033)
<b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>	<b>16,574,628</b>	<b>432,919</b>
<b>CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD</b>	<b>2,221,456</b>	<b>-</b>
<b>CASH AND CASH EQUIVALENTS, END OF PERIOD</b>	<b>18,796,084</b>	<b>432,919</b>

*See accompanying Notes to the Financial Statements*





**GRAN TIERRA ENERGY INC.****Condensed Consolidated Statement of Shareholders' Equity (unaudited)**

Stated in US dollars

	September 30, 2006	December 31, 2005
	\$	\$
<b>Share Capital</b>		
Balance beginning of period	43,285	-
Issue of common shares	52,170	43,285
Balance end of period	95,455	43,285
<b>Additional paid-in-capital</b>		
Balance beginning of period	11,807,313	-
Issue of common shares	59,350,844	11,754,402
Stock-based compensation expense	203,306	52,911
Balance end of period	71,361,463	11,807,313
<b>Warrants</b>		
Balance beginning of period	1,408,429	-
Issue of warrants	11,476,118	1,408,429
Redemption of warrants	(52,994)	-
Balance end of period	12,831,553	1,408,429
<b>Deficit</b>		
Balance beginning of period	(2,219,680)	-
Net loss	(1,857,032)	(2,219,680)
Balance end of period	(4,076,712)	(2,219,680)

(See notes to the consolidated financial statements)

## 1. DESCRIPTION OF BUSINESS AND GOING CONCERN

Gran Tierra Energy Inc. (the “Company”) is a publicly traded oil and gas exploration and production company with operations in Argentina and Colombia.

The Company’s ability to continue as a going concern is dependent upon obtaining the necessary financing to acquire oil and natural gas interests and generating profitable operations from its oil and natural gas interests in the future. The Company’s financial statements as at and for the nine month period ended September 30, 2006 have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities and commitments in the normal course of business. The Company incurred a net loss of \$1,857,032 for the period ended September 30, 2006, and, as at September 30, 2006, had a deficit of \$4,076,711. The Company expects to incur substantial expenditures to further its capital investment programs and the Company’s cash and cash flow from operating activities may not be sufficient to satisfy its current obligations and meet its capital investment programs.

To address the above, management of the Company completed a sale and issuance of common shares during the second quarter of 2006. A total of \$75,000,000 was raised through the sale of 50,000,000 units. Issue costs totalled \$6,000,077, for net proceeds of \$68,999,923. A portion of these proceeds was used to acquire producing and exploration assets in Colombia which add immediate cash flow, and provide exploration opportunities.

In addition, management of the Company is pursuing the following:

- raise additional capital through issuance of debt. The Company is currently negotiating a debt facility that would provide capital for future expansion activities.
- build a portfolio of production, development, and exploration opportunities using additional capital raised and cash provided by future operating activities.

Should the going concern assumption not be appropriate and the Company not be able to realize its assets and settle its liabilities and commitments in the normal course of operations, these consolidated financial statements would require adjustments to the amounts and classifications of assets and liabilities.

## 2. SIGNIFICANT ACCOUNTING POLICIES

These interim consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America (“GAAP”). The preparation of financial statements in accordance with GAAP requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the interim consolidated financial statements, and revenues and expenses during the reporting period. The company believes that the information and disclosures presented are adequate to make the information presented not misleading.

The note disclosure requirements of annual consolidated financial statements provide additional disclosures to that required for interim consolidated financial statements. Accordingly, these interim consolidated financial statements should be read in conjunction with our consolidated financial statements as at and for the year ended December 31, 2005 included in the Company’s 2005 Annual Report on Form 10-KSB. The accounting policies followed are described in note 2 of the consolidated financial statements included in the Company’s 2005 Annual Report on Form 10-KSB.



**Gran Tierra Energy Inc.**

**Notes to the Condensed Consolidated Financial Statements (Unaudited)  
For the Nine Month Period Ended September 30, 2006  
Stated in US dollars**

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***Goodwill***

Goodwill represents the excess of purchase price of business combinations over the fair value of net assets acquired and is tested for impairment at least annually. The impairment test requires allocating goodwill and all other assets and liabilities to assigned reporting units. The fair value of each reporting unit is estimated and compared to the net book value of the reporting unit. If the estimated fair value of the reporting unit is less than the net book value, including goodwill, then the goodwill is written down to the implied fair value of the goodwill through a charge to expense. Because quoted market prices are not available for Gran Tierra's reporting units, the fair values of the reporting units are estimated based upon several valuation analyses, including comparable companies, comparable transactions and premiums paid. The goodwill on Gran Tierra's financial statements was a result of the Argosy acquisition, and relates entirely to the Colombia reporting segment.

***New Accounting Pronouncements***

In September 2005, the Emerging Issues Task Force (EITF) reached a consensus on Issue No. 04-13, *Accounting for Purchases and Sales of Inventory with the Same Counterparty*. This issue addresses the question of when it is appropriate to measure purchase and sales of inventory at fair value and record them in cost of sales and revenues and when they should be recorded as exchanges measured at the book value of the item sold. The EITF concluded that purchases and sales of inventory with the same counterparty that are entered into in contemplation of one another should be combined and recorded as exchanges measured at the book value of the item sold. The consensus has been applied to new arrangements entered into and modifications or renewals of existing agreements, beginning in the second quarter of 2006. The adoption of this statement did not have a material impact on our results of operations or financial position.

In February 2006, the Financial Accounting Standards Board (FASB) issued statement 155, *Accounting for Certain Hybrid Financial Instruments - an amendment of FASB Statements no. 133 and 140*. This statement resolves issues addressed in Statement 133 Implementation Issue no. D1 "Application of Statement 133 to Beneficial Interests in Securitized Financial Assets." This implementation guidance indicated that entities could continue to apply guidance related to accounting for beneficial interests in paragraphs 14 and 362 of Statement 140, which indicate that any security that can be contractually prepaid or otherwise settled in such a way that the holder of the security would not recover substantially all of its recorded investment should be subsequently measured like investments in debt securities classified as available for sale or trading, and may not be classified as held to maturity. Also, Implementation issue D1 indicated that holders of beneficial interests in securitized financial assets that are not subject to paragraphs 14 and 362 of Statement 140 are not required to apply Statement 133 to those beneficial interests, pending further guidance. Statement 155 eliminates the exemption from Statement 133 for interests in securitized financial assets. It also allows the preparer to elect fair value measurement at acquisition, at issuance or when a previously recognized financial instrument is subject to a remeasurement event. We do not expect the adoption of this statement will have a material impact on our results of operations or financial position.

**Gran Tierra Energy Inc.**

**Notes to the Condensed Consolidated Financial Statements (Unaudited)  
For the Nine Month Period Ended September 30, 2006  
Stated in US dollars**

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In March 2006, the FASB issued statement 156 *Accounting for Servicing of Financial Assets - an amendment of FASB Statement No. 140*. Under statement 140, servicing assets and servicing liabilities are amortized over the expected period of estimated net servicing income or loss and assessed for impairment or increased obligation at each reporting date. This statement requires that all separately recognized servicing assets and servicing liabilities be initially measured at fair value, if practicable. Subsequent measurement of servicing assets and servicing liabilities at fair value is permitted, but not required. If derivatives are used to mitigate risks inherent in servicing assets and servicing liabilities, those derivatives must be accounted for at fair value. Servicing assets and servicing liabilities subsequently measured at fair value must be presented separately in the statement of financial position and there are additional disclosures for all separately recognized servicing assets and servicing liabilities. We do not expect the adoption of this statement will have a material impact on our results of operations or financial position.

In June 2006, the FASB issued interpretation no 48 *Accounting for Uncertainty in Income Taxes - an Interpretation of FASB Statement No. 109*. This interpretation clarifies the accounting for uncertainty in income taxes recognized in a company's financial statements in accordance with FASB Statement No. 109. Recognition of a tax position should be based on whether it is more likely than not that a tax position will be sustained. The tax position is measured at the largest amount of benefit that is greater than 50% likely of being realized upon settlement. This interpretation is effective for fiscal years beginning after December 15, 2006. We do not expect the adoption of this interpretation will have material impact on our results of operations or financial position.

In September 2006, the Securities and Exchange Commission (SEC) release Staff Accounting Bulletin (SAB) No. 108 regarding the effects of prior year misstatements in considering current year misstatements for the purpose of a materiality assessment. The opinion in SAB 108 is that in the case of an error that has occurred and been immaterial in a number of previous years, the cumulative effect should be considered in assessing the materiality of the error in the current year. If the cumulative effect of the error is material, then the current year statements, as well as prior year statements should be restated. In the case of restated prior year statements, previously filed reports do not need to be amended, if the error was considered immaterial to previous year's financial statements. However the statements should be amended the next time they are filed. The effects of this guidance should be applied cumulatively to fiscal years ending after November 15, 2006. Additional disclosure should be made regarding any cumulative adjustments made in the current year financial statements. We do not expect the adoption of this SAB will have material impact on our results of operations or financial position.

**3. BUSINESS COMBINATION**

Gran Tierra entered into a Securities Purchase Agreement dated May 25, 2006 with Crosby Capital LLC ("Crosby") to acquire all of the limited partnership interests of Argosy Energy International ("Argosy") and all of the issued and outstanding capital stock of Argosy Energy Corp. On June 20, 2006 Gran Tierra closed the Argosy acquisition and paid consideration to Crosby consisting of \$37.5 million cash, 870,647 shares of the Company's common stock and overriding and net profit interests in certain of Argosy's assets valued at \$1 million. The value of the overriding and net profit interests was based on present value of expected future cash flows. All of Argosy Energy International's assets are in Colombia.



**Gran Tierra Energy Inc.**

**Notes to the Condensed Consolidated Financial Statements (Unaudited)**  
**For the Nine Month Period Ended September 30, 2006**  
**Stated in US dollars**

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The acquisition has been accounted for using the purchase method, and the results of Argosy Energy International have been consolidated with Gran Tierra Energy from June 20, 2006. The following table shows the allocation of the purchase price based on the fair values of the assets and liabilities acquired:

	\$
Cash Paid, net	36,414,385
Common Shares Issued	1,305,971
Transaction Costs	497,574
Total Purchase Price	38,217,930
Purchase Price allocated:	
Oil and Gas Assets	32,553,211
Goodwill (1)	15,005,083
Accounts Receivable	5,361,887
Inventories	567,355
Long Term Investments	6,772
Accounts Payable and Accrued Liabilities	(6,085,109)
Long Term Liabilities	(49,763)
Deferred Tax Liabilities	(9,141,506)
Total Purchase Price allocated	38,217,930

(1) Goodwill is not deductible for tax purposes.

The purchase price allocation has changed from the preliminary allocation performed on June 21, 2006. At June 21, 2006, the company was awaiting the results of an independent reserve audit, and relied on the information provided by Argosy for the preliminary allocation. The reserve report was received in September, 2006 and resulted in a reallocation of the purchase price. The changes are as follows:

	\$
Oil and Gas assets (Decrease)	(8,005,709)
Goodwill Increase	1,411,303
Deferred Tax Liabilities Decrease	6,097,406
Inventories Increase	497,000
Total Change	-

**Gran Tierra Energy Inc.****Notes to the Condensed Consolidated Financial Statements (Unaudited)  
For the Nine Month Period Ended September 30, 2006  
Stated in US dollars**

The Argosy acquisition added 1,182,000 barrels of proven oil reserves to Gran Tierra (net after royalty) as of June 30, 2006.

The unaudited pro forma results for the year ended December 31, 2005 and the period ended September 30, 2006 are shown below, as if the acquisition had occurred on January 1, 2005. Pro forma results are not indicative of actual results or future performance.

	2006	2005
Revenue	15,677,337	12,950,000
Net Income (loss)	3,156,372	(459,000)
Earnings per share (Basic)	0.03	(0.01)
Earnings per share (diluted)	0.03	(0.01)

**4. SEGMENT AND GEOGRAPHIC REPORTING**

The Company's reportable segments are Argentina and Colombia. The Company is primarily engaged in the exploration and production of oil and natural gas. The accounting policies for the segments are the same as those described in Note 2 of the Notes to the Consolidated Financial Statements on the Company's form 10-KSB for 2005.

The Colombia assets were acquired in the second quarter of 2006, and the Argentina assets were acquired on September 1, 2005. Therefore the comparable segmented information for 2005 includes only one month of operations for Argentina, and there is no comparable 2005 information for Colombia.

The following tables present information on the Company's reportable geographic segments:

	Third Quarter, 2006			Nine months ended September 30, 2006		
	Colombia	Argentina	Total	Colombia	Argentina	Total
Revenues	3,616,833	1,602,474	5,219,308	4,077,035	4,281,885	8,358,921
Depreciation, Depletion and Accretion	1,042,234	394,520	1,436,755	1,164,560	1,125,302	2,289,863
Segment Income (loss) before income taxes	1,385,561	88,950	1,474,511	1,560,233	270,492	1,830,725
Segment Capital Expenditures	3,741,500	844,563	4,586,063	3,818,500	2,086,063	5,904,563



## Gran Tierra Energy Inc.

**Notes to the Condensed Consolidated Financial Statements (Unaudited)**  
**For the Nine Month Period Ended September 30, 2006**  
**Stated in US dollars**

	Third Quarter, 2005			Nine months ended September 30, 2005		
	Colombia	Argentina	Total	Colombia	Argentina	Total
Revenues	-	349,263	349,263	-	349,263	349,263
Depreciation, Depletion and Accretion	-	113,000	113,000	-	113,000	113,000
Segment Income before income taxes	-	21,055	21,055	-	21,055	21,055
Segment Capital Expenditures	-	6,884,426	6,884,426	-	6,884,426	6,884,426

  

	September 30, 2006			December 31, 2005		
	Colombia	Argentina	Total	Colombia	Argentina	Total
Property, Plant and Equipment, net	35,211,746	9,234,430	44,446,176	-	8,209,556	8,209,556
Goodwill	15,005,083	-	15,005,083	-	-	-

The following is a reconciliation of income before income taxes for reportable segments to consolidated income before income taxes:

	Third Quarter, 2006	Nine months ended September 30, 2006
Income before income taxes for reportable segments	1,474,511	1,830,725
Corporate Expenses	(830,449)	(2,839,557)
Consolidated income (loss) before income taxes	644,062	(1,008,832)

  

	Third Quarter, 2005	Period from January 26, 2005 to September 30, 2005
Income before income taxes for reportable segments	21,055	21,055
Corporate Expenses	294,328	555,844
Consolidated income (loss) before income taxes	(273,273)	(534,789)

The following is a reconciliation of capital expenditures for reportable segments to consolidated capital expenditures:

	Third Quarter, 2006	Nine months ended September 30, 2006
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Total capital expenditures for reportable segments	4,586,063	5,904,563
Corporate capital expenditures	31,845	107,172
Consolidated capital expenditures	4,617,908	6,011,735

**Gran Tierra Energy Inc.**

**Notes to the Condensed Consolidated Financial Statements (Unaudited)**  
**For the Nine Month Period Ended September 30, 2006**  
**Stated in US dollars**

	Third Quarter, 2005	Period from January 26, 2005 to September 30, 2005
Total capital expenditures for reportable segments	6,884,426	6,884,426
Corporate capital expenditures	50,116	50,116
Consolidated capital expenditures	6,934,542	6,934,542

The following is a reconciliation of reportable net property, plant and equipment to consolidated net property, plant and equipment:

	September 30, 2006	December 31, 2005
Property, Plant and Equipment, net for reportable segments	44,446,176	8,209,556
Corporate property, plant and equipment, net	205,158	103,652
Consolidated property, plant and equipment, net	44,651,335	8,313,208

**5. CAPITAL ASSETS**

	<b>September 30, 2006</b>		
	Cost \$	Accumulated Depletion and Depreciation \$	Net Book Value \$
<b>Oil and natural gas properties</b>			
Proven	28,307,817	(2,682,656)	<b>25,625,161</b>
Unproven	18,292,211	-	<b>18,292,211</b>
Materials and supplies	234,817	-	<b>234,817</b>
Furniture and Fixtures	656,192	(461,461)	<b>194,731</b>
Computer equipment	485,763	(205,167)	<b>280,596</b>
Automobiles	43,901	(20,082)	<b>23,819</b>
	48,020,701	(3,369,366)	<b>44,651,335</b>

## Gran Tierra Energy Inc.

Notes to the Condensed Consolidated Financial Statements (Unaudited)  
 For the Nine Month Period Ended September 30, 2006  
 Stated in US dollars

	<b>December 31, 2005</b>		
	Cost	Accumulated Depletion and Depreciation	Net Book Value
	\$	\$	\$
Oil and natural gas properties	8,331,767	(444,853)	<b>7,886,914</b>
Materials and supplies	300,177	-	<b>300,177</b>
Furniture and Fixtures	20,167	(4,805)	<b>15,362</b>
Computer equipment	73,682	(2,649)	<b>71,033</b>
Automobiles	49,534	(9,812)	<b>39,722</b>
	8,775,327	(462,119)	<b>8,313,208</b>

Following is a description of properties and projects in unproven oil and gas properties, which are not currently subject to amortization

Block	Description	Acquisition Cost	Exploration Cost	Transfer to Amortizable	Total	Timing of Amortization
Rio Magdalena	Popa Exploration well	1,000,000	3,500,000		4,500,000	Q1 2007
Rio Magdalena	Exploration Land	4,052,301		(55,000)	3,997,301	2008
Talora	Exploration Land	402,720	20,000	(6,000)	416,720	2008
Chaza	Exploration Land	2,588,912	38,000		2,626,912	2008
Mecaya	Exploration Land	381,799	29,000		410,799	2008
Primavera	Exploration Land	282,427	54,000		336,427	2008
Santana	Linda Probable reserves	378,378			378,378	Q4 2007
Santana	Mary Probable reserves	1,010,077			1,010,077	Q4 2007
Santana		96,198			96,198	Q4 2007

	Miraflores				
	Probable reserves				
Santana	G&G data	380,000		(380,000)	-
	Exploration				
Guayuyaco	Land	3,791,841	67,000		3,858,841 2008
	Probable reserves	693,558		(33,000)	660,558 Q4 2007
Guayuyaco	G&G Data	1,044,000		(1,044,000)	-
Guayuyaco	Seismic	431,000		(431,000)	-
	New Projects	390,000		(390,000)	-
Total		16,923,211	3,708,000	(2,339,000)	18,292,211

All fields are in Colombia.

**Gran Tierra Energy Inc.**

**Notes to the Condensed Consolidated Financial Statements (Unaudited)**  
**For the Nine Month Period Ended September 30, 2006**  
**Stated in US dollars**

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**6. SHARE CAPITAL**

	Number of Shares	Amount \$
<b>Balance, January 1, 2006</b>	<b>43,285,112</b>	<b>43,285</b>
Common shares issued, at par value of \$0.001 per share	52,170,647	52,170
<b>Balance, September 30, 2006</b>	<b>95,455,759</b>	<b>95,455</b>

*Share capital*

Share capital consists of 78,471,632 common voting shares of the Company and 16,984,127 exchangeable shares of Goldstrike Exchange Co. (collectively, "common stock"). Each exchangeable share is exchangeable only into one common voting share of the Company. The holders of common stock are entitled to one vote for each share on all matters submitted to a stockholder vote and are entitled to share in all dividends that the board of directors, in its discretion, declares from legally available funds. The holders of common stock have no pre-emptive rights, no conversion rights, and there are no redemption provisions applicable to the common stock.

*Warrants*

At September 30, 2006, the Company had 14,472,622 warrants outstanding to purchase 7,236,311 common shares for \$1.25 per share and 55,841,208 warrants outstanding to purchase 27,920,604 common shares for \$1.75 per share.

*Registration Rights Payments*

The shares and warrants have registration rights associated with their issuance.

The 15,047,606 units issued in the fourth quarter of 2005 and first quarter of 2006 have liquidated damages payable in the amount of 1% of the purchase price of the unit per month payable each month the registration statement is not declared effective beyond the mandatory effective date (July 10<sup>th</sup>, 2006). Total amount accrued to September 30, 2006 for these liquidated damages is \$261,182.

The 50,000,000 units issued in June 2006 have liquidated damages payable each month the registration statement is not declared effective beyond the mandatory effective date, being 120 days after the closing date of June 20, 2006 or 150 days if the registration statement is subsequently reviewed by the Securities Exchange Commission:

- 1% of the purchase price for the 1<sup>st</sup> month after the mandatory effective date
- 1.5% of the purchase price for the 2<sup>nd</sup> and 3<sup>rd</sup> month after the mandatory effective date
- 2% of the purchase price for the 4<sup>th</sup> and 5<sup>th</sup> months after the mandatory effective date and
- ½% increase each quarter thereafter

**Gran Tierra Energy Inc.****Notes to the Condensed Consolidated Financial Statements (Unaudited)  
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The total amount of liquidated damages shall not exceed 25% of the purchase price for the units. Under these provisions the maximum payment the company would make would be \$18,750,000.

*Stock options*

The Company has granted options to purchase common shares to certain directors, officers, employees and consultants. Each option permits the holder to purchase one common share at the stated exercise price. The options vest over three years and have a term of ten years, or end of service to the Company, which ever occurs first. At the time of grant, the exercise price equals the market price. The following options have been granted:

	Number of Options	Weighted Average Exercise Price (\$/option)
<b>Outstanding, January 1, 2006</b>	1,940,000	1.12
Granted	-	-
Cancelled	(110,000)	1.12
<b>Balance, September 30, 2006</b>	<b>1,830,000</b>	<b>1.12</b>

The table below summarizes unexercised stock options at September 30, 2006:

Exercise Price (\$/option)	Number of Options Outstanding	Weighted Average Expiry (years)
\$0.80	1,580,000	9.1
\$2.62	250,000	9.2
<b>Total</b>	<b>1,830,000</b>	<b>9.1</b>

No stock options were exercisable at September 30, 2006.

Total stock-based compensation expense included in general and administrative expense was \$203,306. The Black-Scholes option pricing model was used to determine the fair value of the option grants with the following assumptions:

**Gran Tierra Energy Inc.**

**Notes to the Condensed Consolidated Financial Statements (Unaudited)**  
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Dividend yield (\$ per share)	0.00
Volatility (%)	57.0
Risk-free interest rate (%)	2.33
Expected life (years)	3.0
Forfeiture percentage (% per year)	10.0

The weighted average fair value per option is \$0.35.

**7. ASSET RETIREMENT OBLIGATION**

Changes in the carrying amounts of the asset retirement obligations associated with our oil and natural gas properties are as follows:

	September 30, 2006	December 31, 2005
	\$	\$
<b>Balance beginning of period</b>	<b>67,732</b>	<b>-</b>
Obligations assumed with property acquisitions	57,682	66,931
Expenditures made on asset retirements	(9,218)	-
Accretion	5,459	801
<b>Balance, end of period</b>	<b>121,655</b>	<b>67,732</b>

**8. INCOME TAXES**

The Company has losses of approximately \$5,331,000 that can be carried forward and applied against future taxable income. A valuation allowance has been taken for the potential income tax benefit associated with the losses incurred by the Company, due to uncertainty of utilisation of the tax losses.

The income tax expense (recovery) reported differs from the amount computed by applying the statutory rate to loss before income taxes for the following reasons:



**Gran Tierra Energy Inc.**

**Notes to the Condensed Consolidated Financial Statements (Unaudited)**  
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	<b>September 30, 2006</b>	<b>September 30, 2005</b>
	\$	\$
Loss before income taxes	<b>(1,008,832)</b>	<b>(534,789)</b>
Statutory income tax rate	<b>34%</b>	<b>34%</b>
Income tax benefit expected	<b>(343,003)</b>	<b>(181,828)</b>
Stock-based compensation	<b>69,124</b>	<b>-</b>
Tax losses in other jurisdictions, not recognized	<b>1,122,079</b>	<b>189,197</b>
Income tax expense	<b>848,200</b>	<b>7,369</b>

The deferred income tax liability of \$7,849,421 on the balance sheet is related entirely to Colombia operations, for the following items:

	<b>September 30, 2006</b>
	\$
Property, Plant and Equipment	8,006,421
Other long term assets and liabilities	(157,000)
Total	7,849,421

**9. CHANGES IN NON-CASH WORKING CAPITAL**

The changes in non-cash working capital are comprised of the following:

	<b>September 30, 2006</b>	<b>September 30, 2005</b>
	\$	\$
Increase in Accounts receivable	(986,272)	(423,914)
Increase in Prepaids	(185,586)	-
Decrease in Inventory	110,073	-
Increase in Accounts payable	1,032,811	147,176
Increase in Accrued liabilities	568,874	76,637
Increase in Taxes Payable	957,404	7,369
Net Change in Non-cash Working Capital	1,497,304	(192,732)

## 10. COMMITMENTS

The Company entered into a lease beginning February 2006 for office space in Calgary, Canada that expires January 31, 2011 for \$6,824 per month, and a lease beginning March 2006 for office space in Buenos Aires, Argentina that expires February 29, 2008 for \$2,000 per month. In Colombia, the Company holds leases on 3 cars, one expiring September 27, 2007 for \$2,264 per month, one expiring May 3, 2009 for \$932 per month and one expiring September 25, 2008 for \$1,496. There are also a two office leases expiring April 1, 2009 and February 28, 2007 for \$696 and \$2,326 respectively, and one housing accommodation lease for \$1,739 expiring June 1, 2007. These leases are operating leases.

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**Gran Tierra Energy Inc.**

**Notes to the Condensed Consolidated Financial Statements (Unaudited)**  
**For the Nine Month Period Ended September 30, 2006**  
**Stated in US dollars**

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Future minimum lease payments under these leases at September 30, 2006 are as follows:

	\$
2006	54,831
2007	177,097
2008	118,887
2009	89,330
2010	81,888
2011	6,824
<b>Total minimum lease payments</b>	<b>528,857</b>

The company entered into four capital leases in February March and June 2006 for office equipment in Calgary. The length of the leases range from expiration in February 2008 until February 2011. At September 30, 2006 capital assets included \$34,405 related to assets under capital leases and total monthly payments are approximately \$1,140.

Future minimum lease payments under these leases at September 30, 2006 are as follows:

	\$
2006	3,420
2007	13,680
2008	8,958
2009	4,366
2010	3,874
2011	646
<b>Total minimum lease payments</b>	<b>34,944</b>

Interest expense incurred under these capital leases to September 30, 2006 was \$910.

**Gran Tierra Energy Inc.**

**Notes to the Condensed Consolidated Financial Statements (Unaudited)  
For the Nine Month Period Ended September 30, 2006  
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*Guarantees*

Corporate indemnities have been provided by the Company to directors and officers for various items including, but not limited to, all costs to settle suits or actions due to their association with the Company and its subsidiaries and/or affiliates, subject to certain restrictions. The Company has purchased directors' and officers' liability insurance to mitigate the cost of any potential future suits or actions. Each indemnity, subject to certain exceptions, applies for so long as the indemnified person is a director or officer of one of the Company's subsidiaries and/or affiliates. The maximum amount of any potential future payment cannot be reasonably estimated.

The Company may provide indemnifications in the normal course of business that are often standard contractual terms to counterparties in certain transactions such as purchase and sale agreements. The terms of these indemnifications will vary based upon the contract, the nature of which prevents the Company from making a reasonable estimate of the maximum potential amounts that may be required to be paid. Management believes the resolution of these matters would not have a material adverse impact on the Company's liquidity, consolidated financial position or results of operations.

**11. Disagreement with Ecopetrol**

As of September 30, 2006 the contracting parties of Guayuyaco Association Contract, Ecopetrol and Argosy Energy International, consulted with their legal advisors to clarify the procedure for allocation of oil produced and sold during the long term test of the Guayuyaco-1 and Guayuyaco-2 wells. Ecopetrol has advised Argosy of a material difference in the interpretation of the procedure established in the Clause 3.5 of Attachment-B of the Guayuyaco association Contract. Ecopetrol interprets the contract to provide that the extend test production up to a value equal to 30% of the direct exploration costs of the wells is for Ecopetrol's account only and serves as reimbursement of its 30% back in to the Guayuyaco discovery. Argosy's contention is that this amount is merely the recovery of 30% of the direct exploration costs of the wells and not exclusively for benefit of Ecopetrol. While Argosy believes its interpretation of the Guayuyaco Association Contract is correct, the resolution of this issue is still pending of agreement between the parties or determination through legal proceedings.

The estimated value of disputed production is \$2,361,188 which possible loss is shared 50% (\$1,180,594) with Solana Petroleum Exploration (Colombia) S.A. partner in the contract and 50% Argosy. No amount has been accrued in the financial statements related to this disagreement.

**12. Subsequent Events**

On February 22, 2006, the Company filed a Current Report on Form 8-K disclosing that the Company had made an offer to acquire certain interests of Compañía General de Combustibles S.A. ("CGC"). The Company offered to purchase CGC's participation interests in a total of eight properties in Argentina. As disclosed in the Company's

Current Report on Form 8-K filed on August 8, 2006 the transaction is subject to Argentinean court approvals, the potential exercise of rights of first refusal and the need to obtain third-party consents.

**Gran Tierra Energy Inc.**

**Notes to the Condensed Consolidated Financial Statements (Unaudited)**

**For the Nine Month Period Ended September 30, 2006**

**Stated in US dollars**

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The Company has received evidence that court approval in Argentina has now been granted. On November 2, 2006 the Company purchased interests in four properties (a 93.18% participation in the Valle Morado Block, a 100% interest in the Santa Victoria Block and the remaining 50% interests in the Nacatimbay and Ipaguazu Blocks (in which the Company currently holds 50% interests)) for a total consideration of \$2.1 million. The Company is considering its options whether to acquire the interests in the remaining four properties, which interests remain subject to rights of first refusal among joint venture partners and other third party consents.

Gran Tierra signed a License Contract for the Exploration and Exploitation of Hydrocarbons covering Block 122 in Peru on June 8, 2006. Terms of the License define a seven-year exploration term with four periods, each with minimum work obligations. Final ratification by the government of Peru occurred on November 3, 2006. The minimum commitment for the first work period of 18 months, which is mandatory, is \$0.5 million. The subsequent three work periods are optional to the Company.

## **Item 2: Management's Discussion and Analysis**

### **Forward Looking Statements**

This Quarterly Report on Form 10-QSB contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934. This Quarterly Report includes statements regarding our plans, goals, strategies, intent, beliefs or current expectations. These statements are expressed in good faith and based upon a reasonable basis when made, but there can be no assurance that these expectations will be achieved or accomplished. These forward looking statements can be identified by the use of terms and phrases such as “believe,” “plan,” “intend,” “anticipate,” “target,” “estimate,” “expect,” and the like, future-tense or conditional constructions ( “may,” “could,” “should,” etc.). Items contemplating or making assumptions about, actual or potential future sales, market size, collaborations, and trends or operating results also constitute such forward-looking statements.

Although forward-looking statements in this Quarterly Report reflect the good faith judgment of management, forward-looking statements are inherently subject to known and unknown risks, business, economic and other risks and uncertainties that may cause actual results to be materially different from those discussed in these forward-looking statements. Readers are urged not to place undue reliance on these forward-looking statements, which speak only as of the date of this Quarterly Report. We assume no obligation to update any forward-looking statements in order to reflect any event or circumstance that may arise after the date of this Quarterly Report, other than as may be required by applicable law or regulation. Readers are urged to carefully review and consider the various disclosures made by us in our reports filed with the Securities and Exchange Commission which attempt to advise interested parties of the risks and factors that may affect our business, financial condition, results of operation and cash flows. This discussion should be read in conjunction with the consolidated financial statements including the related footnotes. If one or more of these risks or uncertainties materialize, or if the underlying assumptions prove incorrect, our actual results may vary materially from those expected or projected.

The following discussion should be read in conjunction with the attached financial statements and notes thereto. Except for the historical information contained herein, the matters discussed below are forward-looking statements that involve certain risks and uncertainties, including, among others, the risks and uncertainties discussed below.

### **Overview**

Gran Tierra is an independent international energy company involved in oil and natural gas exploration and exploitation. We plan to continually increase our oil and natural gas reserves through a balanced strategy of exploration drilling, development and acquisitions in South America. Initial countries of interest are Argentina, Colombia and Peru.

Gran Tierra took its current form on November 10, 2005 when the former Gran Tierra Energy Inc., a privately held corporation in Alberta (“Gran Tierra Canada”), was acquired by an indirect subsidiary of Goldstrike Inc., a Nevada corporation, which was publicly traded on the NASD Over-the-Counter Bulletin Board. Goldstrike adopted the assets, management, business operations, business plan and name of Gran Tierra Canada. The predecessor company in the transaction was the former Gran Tierra Canada; the financial information of the former Goldstrike was eliminated at consolidation. This transaction was accounted for as a reverse takeover of Goldstrike Inc. by Gran Tierra Canada.

We currently hold several interests in the Noroeste region of Argentina, including a non-operating (14%) interest in the Palmar Largo joint venture involving several producing fields; an operating 50% interest in the El Vinalar Block, also currently producing, and; a non-operating 50% interest in two minor properties, both currently non-producing. We acquired the Palmar Largo and minor property interests on September 1, 2005 and the acquisition of the El Vinalar interest became effective on June 30, 2006. Gran Tierra began operations in Colombia on June 20, 2006 through the acquisition of Argosy Energy International. Argosy holds interests in a portfolio of producing and non-producing assets in Colombia. Before the acquisitions in Argentina and Colombia, we had no oil and gas interests or properties. The acquisitions were funded through a series of private placements between September 2005 and February 2006 and additional private placements in June 2006.



We entered into a Securities Purchase Agreement dated May 25, 2006 with Crosby Capital LLC to acquire all of the limited partnership interests of Argosy Energy International and all of the issued and outstanding capital stock of Argosy Energy Corp. On June 20, 2006 we closed the Argosy acquisition and paid consideration to Crosby consisting of \$37.5 million cash, 870,647 shares of our common stock and overriding and net profit interests in certain of Argosy's assets valued at \$1 million. The value of the overriding and net profit interests was based on present value of expected future cash flows. All of Argosy Energy's assets are in Colombia.

On June 30, 2006 we closed a farm-in arrangement with Golden Oil Corporation whereby we purchased 50% of the El Vinalar field in Argentina for \$950,000. We also have agreed to pay 100% of the first \$2.7 million in costs of a sidetrack well related to this farm-in agreement.

Our ability to continue as a going concern is dependent upon obtaining the necessary financing to acquire oil and natural gas interests and generating profitable operations from our oil and natural gas interests in the future. Our financial statements as at and for the period ended September 30, 2006 have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities and commitments in the normal course of business. We incurred a net loss of \$1,857,032 for the nine months ended September 30, 2006. At September 30, 2006 we had an accumulated deficit of \$4,076,711. We expect to incur substantial expenditures to further our capital investment programs and our cash flow from operating activities and current cash balances may not be sufficient to satisfy our current obligations and meet our capital investment objectives.

To address our ability to continue as a going concern, we have raised additional capital through the sale and issuance of common shares, and may do so again in the future. We plan to expand our portfolio of production, development, step-out and exploration opportunities using additional capital raised and cash provided from future operating activities. We are also negotiating a credit facility with a major bank.

On June 20, 2006 we completed the sale of 43,336,051 units of our securities for total proceeds of \$65,004,076. Each unit consisted of one share of common stock and one warrant to purchase one half of a common share for five years at an exercise price of \$1.75 per whole share. On June 29, 2006 there was a second closing of the offering of units of our securities, selling 3,636,629 units for proceeds of \$5,454,954. Finally, on June 30, 2006 we closed the offering with an additional sale of 3,027,320 units for \$4,540,980. In total, Gran Tierra raised \$75,000,000 from the sale of 50,000,000 units of securities. Issue costs totaled \$6,000,077 for the three closings.

Net loss for the third quarter of 2006 was \$66,355, or \$0.00 per share. This compares to a loss of \$284,644 for the third quarter of 2005. Per share calculations for the third quarter of 2006 are based on basic weighted average shares outstanding of 95,455,759 for the three month period ended September 30, 2006. Revenue for the third quarter was \$5,394,949. Operating expenses totaled \$1,259,888 and total expenses were \$4,750,887 for the third quarter of 2006. All results reflect a full quarter of operations at El Vinalar and Palmar Largo in Argentina and for Argosy Energy in Colombia. These results compare to net revenue of \$1,049,629 for the first quarter of 2006, and \$2,089,984 for the second quarter of 2006. Operating expense was \$353,080 in quarter one and \$1,089,540 in quarter two for 2006, total expenses were \$2,211,120 and \$2,581,393 respectively. We incurred a loss of \$1,218,948 for the first quarter of 2006 and a loss of \$571,734 for the second quarter.

For the nine months ended September 30, 2006 the net loss was \$1,857,032, or \$0.03 per share, based on weighted average shares outstanding for the nine months ended September 30, 2006 of 63,043,998. Net revenue was \$8,554,737 and operating expenditures totaled \$2,702,507, depletion, depreciation and accretion expense was \$2,324,158 and total expenses were \$9,563,569. Operating cash flow was positive \$2,223,931, capital expenditures were \$6,011,735, and financing activities provided inflow of \$70,826,137.

We began oil and gas operations in Argentina on September 1, 2005 and therefore operating results for 2005 are not directly comparable to results for 2006 which include Palmar Largo for the entire period and the impacts of El Vinalar and the Argosy acquisition. Net revenue was \$349,263 and operating expenses were \$125,000 both for the third quarter and the nine months ended September 30, 2005. General and administrative expenditures for the third quarter of 2005 were \$414,397 and were \$668,909 for the nine months ended September 30, 2005. Net loss for the third quarter of 2005 was \$284,644 or \$0.02 per share, based on 12,083,333 weighted average shares outstanding. Net loss for the nine months ended September 30, 2005 was \$546,160 or \$0.11 per share on 4,903,297 weighted average shares outstanding. Capital expenditures for the nine months ended September 30, 2005 were \$6,934,542, with depletion, depreciation and amortization of \$115,209 for net capital additions of \$6,819,333. These amounts include the purchase of 14% interest in Palmar Largo and 50% interests in Nacatimbay and Ipaguazu. Operating cash flow for the nine months to September 30, 2005 was an outflow of \$623,683 and financing activities provided cash inflow of \$8,368,365.

### **Plan of Operations**

During 2006, we plan to participate in our current joint venture activities in Argentina. The Palmar Largo joint venture is engaged in a workover program for the year, to be funded from internal cash flows. Seven workovers were completed in the first nine months of 2006; one workover is currently in progress. We will be conducting a review of production enhancement and exploration opportunities at Nacatimbay and Ipaguazu. One well is planned for El Vinalar in late 2006.

In Colombia a total of three wells are planned for 2006. One well, Popa-1 in the Rio Magdalena block, was drilled at the end of the second quarter and is currently in a testing phase. One well is planned for each of the Guayuyaco and Talora Blocks. Exploration terms for the Rio Magdalena Block require the drilling of a second well by February 2007, and this well is currently planned for the fourth quarter of 2006.

Gran Tierra signed a License Contract with PeruPetro S.A. for the Exploration and Exploitation of Hydrocarbons covering Block 122 in Peru on June 8, 2006. Terms of the License define a seven-year exploration term with four periods, each with minimum work obligations. The minimum commitment for the first work period, which is mandatory, is \$0.5 million. The potential commitment over the seven-year period, at our option, is \$5.0 million and includes technical studies, seismic acquisition and the drilling of one exploration well. The License Contract defines an exploitation term of thirty years for commercial discoveries of oil. Block 122 is located on the eastern flank of the Maranon Basin of northern Peru, on the crest of the Iquitos Arch and covers 1.2 million acres. Final ratification by the government of Peru occurred on November 3, 2006.

In addition to current projects, we will pursue new ventures that may add production, development and exploration opportunities in South America, in areas of current activity and in new regions/countries. There is no assurance additional opportunities will be available, or if we participate in additional opportunities that those opportunities will be successful.

Based on projected production, prices and costs, we believe that our current cash position and cash flow from operations are sufficient to sustain current activity through to the end of 2007. New business opportunities will require equity and/or debt financing for acquisitions and/or future work programs.



We have not entered into any commodity derivative arrangements or hedging transactions. Although we have no current plans to do so, we may enter in to some swap and/or hedging arrangements in conjunction with future financings. We have no off-balance sheet arrangements.

## **Results of Operations for the period ended September 30, 2006**

### ***Revenues***

Production after royalties in Argentina averaged 338 barrels per day for the third quarter of 2006 including 295 barrels per day from Palmar Largo and 43 barrels per day from El Vinalar. Production for the nine-month period to September 30, 2006 averaged 303 barrels per day (288 barrels per day from Palmar Largo; 14 barrels per day for El Vinalar, which contributed to production beginning July 1 2006; 1 barrel per day for Nacatimbay where production was suspended on March 1 due to low flow conditions). During January and February of 2006, production at Nacatimbay averaged 3 barrels per day of condensate and 476 thousand cubic feet per day of natural gas after royalties. A remedial work program is being assessed to restore production at Nacatimbay. We cannot assure you that production can be restored.

Oil sales in Argentina averaged 422 barrels per day for the third quarter of 2006 including 376 barrels per day for Palmar Largo and 46 barrels per day for El Vinalar. For the nine-month period ended September 30, 2006, sales averaged 382 barrels per day (365 barrels per day at Palmar Largo, 16 barrels per day for El Vinalar, 1 barrel per day at Nacatimbay).

Production after royalties in Colombia averaged 704 barrels per day for the third quarter of 2006. Oil sales were 684 barrels per day on average during that period and were hampered by a temporary shut-down of pipeline facilities in July, 2006. As the Argosy acquisition was made in June 2006, no production was recorded in the prior year. Net production for the nine-month period ended September 30, 2006 includes results from June 21 only, averaging 266 barrels per day. Sales over the period averaged 260 barrels per day.

In Argentina, net revenue for the third quarter of 2006 was \$1,602,474 with an average sales price at \$41.27 per barrel. For the nine months ended September 30, 2006, net revenue was \$4,281,885 with an average sales price of \$41.06 per barrel. Revenues reflect an average royalty of 12% of production revenue minus transportation and storage costs.

In Colombia, we recorded production beginning June 21, 2006 in conjunction with our acquisition of Argosy Energy. Net revenue was \$3,616,833 for the third quarter and \$4,077,035 for the period from June 21 to September 30, 2006, reflecting royalty rates of 20% for the Santana block and 8% for the Guayuyaco block. Average sales price for the quarter was \$57.47. The average sales price for the nine-month period ended September 30, 2006 was \$57.44 per barrel.

Interest revenue was \$175,641 for the third quarter of 2006 and \$195,816 for the nine months ended September 30, 2006.

Net Revenue for the third quarter of 2005 was \$349,263, reflecting one month of sales from Palmar Largo. No revenue was recorded for the first half of 2005.

## Operating Expenses

For the three months ended September 30, 2006, operating expenses were \$1,259,888, and for the nine months ended September 30, 2006 operating expenses were \$2,702,507. For the nine-month period ended September 30, 2006 we had a full nine months of operating activities at Palmar Largo, two months at Nacatimbay before production was suspended on March 1, 2006, three months of activities at El Vinalar beginning July 1, 2006 and three months plus ten days of operations in Colombia beginning June 21, 2006.

Operating expenses in Argentina for the third quarter of 2006 totaled \$883,658 (\$22.76 per barrel), primarily at Palmar Largo and including transportation costs of \$116,949 (\$3.01 per barrel) plus an inventory adjustment of \$409,582 (\$10.55 per barrel) due to an underlift of crude oil volumes by a partner in the Palmar Largo joint venture. The impact of an agreement among the joint venture partners providing for the recovery of underlifted volumes has been accrued in September of 2006. Operating expenses in Argentina for the nine-month period ended September 30, 2006 were \$2,186,278 (\$20.96 per barrel) including transportation costs of \$310,901 (\$2.98 per barrel) and the inventory adjustment of \$409,582 (\$3.93 per barrel). Operating costs for 2006 have been impacted by workover activity at Palmar Largo, which expenditures are treated as an operating expense.

Operating expenses in Colombia were \$376,229 for the third quarter of 2006, and totaled \$516,229 including the ten day operating period from June 21 to June 30. This translates to \$5.98 per barrel for the third quarter and \$7.27 per barrel for the period June 21 to September 30, 2006.

For the period ended September 30, 2005 we had operations at Palmar Largo and Nacatimbay for 30 days. Operating expenses totaled \$125,000, (\$18.42 per barrel).

## Other Operating Expenses

Depreciation, depletion and accretion was \$1,449,694 for the third quarter of 2006 and for the nine months ended September 30, 2006 was \$2,324,158, including accretion of asset retirement obligations of \$2,896 and \$5,459 respectively. The majority of this expense represents the depletion of oil and gas assets in Argentina and the newly acquired Colombia properties. Depreciation, depletion and accretion recorded for the nine months ended September 30, 2005 was \$115,209 and was \$111,843 for the third quarter of 2005.

Remaining operating expenses for the third quarter of 2006 were principally general and administrative in nature, which totaled \$1,764,856. Of this amount, legal costs, accounting expenses, insurance premiums and consulting costs were \$384,917. The majority of these costs were associated with audit activities, share registration, and marketing initiatives. Salaries and benefits were \$687,948 and travel costs were \$71,749. Office costs were \$220,768, consultant expenses were \$60,275, bank expenses were \$45,706 and other expenses totaled \$293,493. Interest expense was \$2,765. Total general and administrative expenses for the third quarter of 2005 were \$414,397.

For the nine months ended September 30, 2006, general and administrative costs were \$4,256,303. Legal, accounting, insurance and consulting costs were \$1,667,241. Salaries and benefits and other employee costs were \$1,520,168 and travel costs were \$251,498. Office expenses totaled \$456,948, bank expenses were \$94,902 and other expenses were \$265,546. Interest expense was \$3,075. Total general and administrative expenses for the period from January 26, 2005 (inception) to September 30, 2005 were \$668,908.

Foreign exchange loss was \$273,684 for the third quarter of 2006 and \$277,526 for the nine months ended September 30, 2006.



## Net Income (Loss) Available to Common Shares

Net loss for the third quarter of 2006 was \$66,355, which equates to \$0.00/share. These results reflect a full quarter of operating activities at Palmar Largo, El Vinalar and Colombia. This compares to a loss of \$284,644 or \$0.02 per share for the third quarter of 2005.

For the nine months ended September 30, 2006 net loss was \$1,857,032, or \$0.03 per share. This loss reflects a full nine months of operating activities at Palmar Largo, two months of activities at Nacatimbay, three months at El Vinalar and three months plus ten days of operations in Colombia. The net loss for the period from January 26, 2005 (inception) to September 30, 2005 was \$546,160 or \$0.11 per share.

## Liquidity and Capital Resources

### *Liquidity*

Gross capital expenditures for the three months ended September 30, 2006 were \$4,617,908 and for nine months ended September 30, 2006 were \$6,011,735. Capital expenditures for the quarter were predominantly for development activity at Palmar Largo, for the purchase of El Vinalar, drilling activities in Colombia, and office equipment and leasehold improvements in both Calgary and Argentina. Capital expenditures in the first nine months of 2005 were \$6,934,542 which included the purchase of Palmar Largo, Nacatimbay and Ipaguazu interests in Argentina.

During the first three quarters of 2006, we funded the majority of our capital expenditures and operating expenditures from cash balances existing at the end of 2005, which were received through a series of private placements of equity in Gran Tierra in the fourth quarter of 2005 and the first quarter of 2006, and via private placements which closed in June, 2006. On June 20, 2006 we completed the sales of 43,336,051 units of our securities for total proceeds of \$65,004,076. Each unit consisted of one share of common stock and one warrant to purchase one half a common share for five years at an exercise price of \$1.75 per whole share. On June 29, 2006 there was a second closing of the offering of units of our securities, selling 3,636,629 units for proceeds of \$5,454,954. Finally, on June 30, 2006, we closed the offering with an additional sale of 3,027,320 units for \$4,540,980. In total, we raised \$75,000,000 from the sale of 50,000,000 units of securities, less issue costs of \$6,000,077 for net proceeds of 68,999,923. Our cash balance at September 30, 2006 was \$18,796,084 compared to \$2,221,456 at December 31, 2005 and \$21,263,776 at June 30, 2006. Restricted cash of \$12,617,263 as at September 30 will become available to the Company as follows:

- \$4,000,100 held in escrow relating to the Argosy acquisition is required to be replaced by a letter of credit. Release of these funds is expected by November 6, 2006.
- \$4,000,000 is being held by Standard Bank in support of the letter of credit noted above.
- \$3,100,000 will become available upon the expiry of the offer to purchase certain assets from CGC.
- \$200,426 is held in escrow with our joint venture partners in Palmar Largo against our future cash calls. These funds will be available October, 2006 unless we do not meet our cash call obligations in the interim period.
- \$1,280,993 is held in escrow related to the June 2006 financing. These funds will be released from escrow pending a request from Gran Tierra to the Alberta Securities Commission requesting an exemption from prospectus requirements for the trading of common shares of Gran Tierra for purchasers resident in Alberta under “accredited investor” exemptions.
- \$35,744 relates to interest earned on various escrow accounts, which will be released along with the principal funds involved.

We believe that our current operations can be maintained from existing cash flow and cash on hand barring unforeseen events or a severe downturn in oil and gas prices, until the end of 2007. Should our operating cash flow decline, we would examine measures such as reducing our capital expenditure program, issuance of debt, or issuance of equity.

Future growth and acquisitions will depend on our ability to raise additional funds through equity and/or debt markets. We have recently completed financing initiatives to support recent acquisition initiatives, which have also brought additional production and cash flow into our Company.

Our initiatives to raise debt or equity financing to fund capital expenditures or other acquisition and development opportunities may be affected by the market value of our common stock. If the price of our common stock declines, our ability to utilize our stock either directly or indirectly through convertible instruments for raising capital could be negatively affected. Also, raising funds by issuing stock or other equity securities would further dilute our existing stockholders, and this dilution would be exacerbated by a decline in stock price. Any securities we issue may have rights, preferences and privileges that are senior to our existing equity securities. Borrowing money may also involve pledging some or all of our assets.

### **Off-Balance Sheet Arrangements**

For the fiscal period ended September 30, 2006, we had no off-balance sheet arrangements as defined in Item 303(c) of Regulation S-B, promulgated by the SEC.

### **Subsequent Events**

On February 22, 2006, the Company filed a Current Report on Form 8-K disclosing that the Company had made an offer to acquire certain interests of Compañía General de Combustibles S.A. ("CGC"). The Company offered to purchase CGC's participation interests in a total of eight properties in Argentina. As disclosed in the Company's Current Report on Form 8-K filed on August 8, 2006 the transaction is subject to Argentinean court approvals, the potential exercise of rights of first refusal and the need to obtain third-party consents.

The Company has received evidence that court approval in Argentina has now been granted. On November 2, 2006 the Company purchased interests in four properties (a 93.18% participation in the Valle Morado Block, a 100% interest in the Santa Victoria Block and the remaining 50% interests in the Nacatimbay and Ipaguazu Blocks (in which the Company currently holds 50% interests)) for a total consideration of \$2.1 million. The Company is considering its options to acquire the interests in the remaining four properties, which interests remain subject to rights of first refusal among joint venture partners and other third party consents.

Gran Tierra signed a License Contract for the Exploration and Exploitation of Hydrocarbons covering Block 122 in Peru on June 8, 2006. Terms of the License define a seven-year exploration term with four periods, each with minimum work obligations. Final ratification by the government of Peru occurred on November 3, 2006.

## **CRITICAL ACCOUNTING ESTIMATES**

### **Use of Estimates**

The preparation of financial statements under generally accepted accounting principles in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.





### **Oil and Gas Accounting—Reserves Determination**

The process of estimating reserves is complex. It requires significant judgments and decisions based on available geological, geo-physical, engineering and economic data.

To estimate the economically recoverable oil and natural gas reserves and related future net cash flows, we incorporate many factors and assumptions including:

- expected reservoir characteristics based on geological, geophysical and engineering assessments;
- future production rates based on historical performance and expected future operating and investment activities;
- future oil and gas prices and quality differentials;
- assumed effects of regulation by governmental agencies; and
- future development and operating costs.

We believe these factors and assumptions are reasonable based on the information available to us at the time we prepare our estimates. However, these estimates may change substantially as additional data from ongoing development activities and production performance becomes available and as economic conditions impacting oil and gas prices and costs change.

Management is responsible for estimating the quantities of proved oil and natural gas reserves and for preparing related disclosures. Estimates and related disclosures are prepared in accordance with SEC requirements and generally accepted industry practices in the US as promulgated by the Society of Petroleum Engineers.

Reserve estimates, including the standardized measure of discounted future net cash flow and changes therein, are prepared at least annually by independent qualified reserves consultants.

The Board of Directors oversees the annual review of our oil and gas reserves and related disclosures. The Board meets with management periodically to review the reserves process, results and related disclosures and appoints and meets with the independent reserves consultants to review the scope of their work, whether they have had access to sufficient information, the nature and satisfactory resolution of any material differences of opinion, and in the case of the independent reserves consultants, their independence.

Reserves estimates are critical to many of our accounting estimates, including:

- Determining whether or not an exploratory well has found economically producible reserves.
- Calculating our unit-of-production depletion rates. Both proved and proved developed reserves estimates are used to determine rates that are applied to each unit-of-production in calculating our depletion expense. Proved reserves are used where a property is acquired and proved developed reserves are used where a property is drilled and developed.
- Assessing, when necessary, our oil and gas assets for impairment. Estimated future cash flows are determined using proved reserves. The critical estimates used to assess impairment, including the impact of changes in reserves

estimates, are discussed below.

### **Oil and Gas Accounting—Impairment**

We evaluate our oil and gas properties for impairment on a quarterly basis. We assess estimated discounted future cash flows for to determine if properties are impaired on a cost centre basis. If the 10% discounted future cash flows for a cost centre are less than the carrying amount, the cost centre is impaired and written down to its fair value.

We assessed our oil and gas properties for impairment at the end of the second quarter of 2006 and found no impairments were required based on our assumptions.

Cash flow estimates for our impairment assessments require assumptions about two primary elements—future prices and reserves.

It is difficult to determine and assess the impact of a decrease in our proved reserves on our impairment tests. The relationship between the reserves estimate and the estimated discounted cash flows is complex because of the necessary assumptions that need to be made regarding future production rates, future prices and future costs. Under full cost accounting, a ceiling test is performed to ensure that unamortized capitalized costs in each cost centre do not exceed their fair value. An impairment loss is recognized in net earnings when the carrying amount of a cost center is not recoverable and the carrying amount of the cost center exceeds its fair value. A cost center is defined as a country. Capitalized costs, less accumulated depreciation (carrying value) are limited to the sum of: the present value of estimated future net revenues from proved oil and gas reserves, less future value of unproven properties included in the costs being amortized; less income tax effects related to the differences between the book and tax basis of the properties. If unamortized capital costs within a cost center exceed the cost center ceiling, the excess shall be charged to expense and separately disclosed during the period in which the excess occurs. As a result, we are unable to provide a reasonable sensitivity analysis of the impact that a reserves estimate decrease would have on our assessment of impairment.

### **Asset Retirement Obligations**

We are required to remove or remedy the effect of our activities on the environment at our present and former operating sites by dismantling and removing production facilities and remediating any damage caused. Estimating our future asset retirement obligations requires us to make estimates and judgments with respect to activities that will occur many years into the future. In addition, the ultimate financial impact of environmental laws and regulations is not always clearly known and cannot be reasonably estimated as standards evolve in the countries in which we operate.

We record asset retirement obligations in our consolidated financial statements by discounting the present value of the estimated retirement obligations associated with our oil and gas wells and facilities and chemical plants. In arriving at amounts recorded, numerous assumptions and judgments are made with respect to ultimate settlement amounts, inflation factors, credit adjusted discount rates, timing of settlement and expected changes in legal, regulatory, environmental and political environments. The asset retirement obligations we have recorded result in an increase to the carrying cost of our property, plant and equipment. The obligations are accreted with the passage of time. A change in any one of our assumptions could impact our asset retirement obligations, our property, plant and equipment and our net income.

It is difficult to determine the impact of a change in any one of our assumptions. As a result, we are unable to provide a reasonable sensitivity analysis of the impact a change in our assumptions would have on our financial results. We are confident, however, that our assumptions are reasonable.

## Deferred Income Taxes

We follow the liability method of accounting for income taxes whereby future income tax assets and liabilities are recognized based on temporary differences in reported amounts for financial statement and tax purposes. We carry on business in several countries and as a result, we are subject to income taxes in numerous jurisdictions. The determination of our income tax provision is inherently complex and we are required to interpret continually changing regulations and make certain judgments. While income tax filings are subject to audits and reassessments, we believe we have made adequate provision for all income tax obligations. However, changes in facts and circumstances as a result of income tax audits, reassessments, jurisprudence and any new legislation may result in an increase or decrease in our provision for income taxes.

## NEW ACCOUNTING PRONOUNCEMENTS

In September 2005, the Emerging Issues Task Force (EITF) reached a consensus on Issue No. 04-13, *Accounting for Purchases and Sales of Inventory with the Same Counterparty*. This issue addresses the question of when it is appropriate to measure purchase and sales of inventory at fair value and record them in cost of sales and revenues and when they should be recorded as exchanges measured at the book value of the item sold. The EITF concluded that purchases and sales of inventory with the same counterparty that are entered into in contemplation of one another should be combined and recorded as exchanges measured at the book value of the item sold. The consensus should be applied to new arrangements entered into and modifications or renewals of existing agreements, beginning with the second quarter of 2006. We do not expect the adoption of this statement will have a material impact on our results of operations or financial position.

In February 2006, the Financial Accounting Standards Board (FASB) issued statement 155, *Accounting for Certain Hybrid Financial Instruments - an amendment of FASB Statements no. 133 and 140*. This statement resolves issues addressed in Statement 133 Implementation Issue no. D1 "Application of Statement 133 to Beneficial Interests in Securitized Financial Assets." This implementation guidance indicated that entities could continue to apply guidance related to accounting for beneficial interests in paragraphs 14 and 362 of Statement 140, which indicate that any security that can be contractually prepaid or otherwise settled in such a way that the holder of the security would not recover substantially all of its recorded investment should be subsequently measure like investments in debt securities classified as available for sale or trading, and may not be classified as held to maturity. Also, Implementation issue D1 indicated that holders of beneficial interests in securitized financial assets that are not subject to paragraphs 14 and 362 of Statement 140 are not required to apply Statement 133 to those beneficial interests, pending further guidance. Statement 155 eliminates the exemption from Statement 133 for interests in securitized financial assets. It also allows the preparer to elect fair value measurement at acquisition, at issuance or when a previously recognized financial instrument is subject to a remeasurement event. We do not expect the adoption of this statement will have a material impact on our results of operations or financial position.

In March 2006, the FASB issued statement 156 *Accounting for Servicing of Financial Assets - an amendment of FASB Statement No. 140*. Under statement 140, servicing assets and servicing liabilities are amortized over the expected period of estimated net servicing income or loss and assessed for impairment or increased obligation at each reporting date. This statement requires that all separately recognized servicing assets and servicing liabilities be initially measured at fair value, if practicable. Subsequent measurement of servicing assets and servicing liabilities at fair value is permitted, but not required. If derivatives are used to mitigate risks inherent in servicing assets and servicing liabilities, those derivatives must be accounted for at fair value. Servicing assets and servicing liabilities subsequently measured at fair value must be presented separately in the statement of financial position and there are additional disclosures for all separately recognized servicing assets and servicing liabilities. We do not expect the adoption of this statement will have a material impact on our results of operations or financial position.



In June 2006, the FASB issued interpretation no 48 *Accounting for Uncertainty in Income Taxes - an Interpretation of FASB Statement No. 109*. This interpretation clarifies the accounting for uncertainty in income taxes recognized in a company's financial statements in accordance with FASB Statement No. 109. Recognition of a tax position should be based on whether it is more likely than not that a tax position will be sustained. The tax position is measure at the largest amount of benefit that is greater than 50% likely of being realized upon settlement. This interpretation is effective for fiscal years beginning after December 15, 2006. We do not expect the adoption of this interpretation will have material impact on our results of operations or financial position.

In September 2006, the Securities and Exchange Commission (SEC) release Staff Accounting Bulletin (SAB) No. 108 regarding the effects of prior year misstatements in considering current year misstatements for the purpose of a materiality assessment. The opinion in SAB 108 is that in the case of an error that has occurred and been immaterial in a number of previous years, the cumulative effect should be considered in assessing the materiality of the error in the current year. If the cumulative effect of the error is material, then the current year statements, as well as prior year statements should be restated. In the case of restated prior year statements, previously filed reports do not need to be amended, if the error was considered immaterial to previous year's financial statements. However the statements should be amended the next time they are filed. The effects of this guidance should be applied cumulatively to fiscal years ending after November 15, 2006. Additional disclosure should be made regarding any cumulative adjustments made in the current year financial statements. We do not expect the adoption of this SAB will have material impact on our results of operations or financial position.



### **Item 3. Controls and Procedures**

#### **(a) Evaluation of Disclosure Controls and Procedures**

The term “disclosure controls and procedures” is defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). This term refers to the controls and procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files under the Exchange Act is recorded, processed, summarized, and reported within the required time periods.

Our Chief Executive Officer and Chief Financial Officer evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the period covered by this report as required by Rule 13a-15 of the Exchange Act. Based on their evaluation of our disclosure controls and procedures, they have concluded that as of the end of the period covered by this report our disclosure controls and procedures are effective in ensuring that material information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the rules and forms of the SEC and that such information is accumulated and communicated to management as appropriate to allow timely decisions regarding required disclosure.

#### **(b) Changes in Internal Control over Financial Reporting**

No change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) occurred during the period covered by this report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

**Item 1. Legal Proceedings**

From time to time we may become a party to litigation or other legal proceedings that are part of the ordinary course of our business, involving routine litigation that is incidental to our business.

As of September 30, 2006 the contracting parties of Guayuyaco Association Contract, Ecopetrol and Argosy Energy International, consulted with their legal advisors to clarify the procedure for allocation of oil produced and sold during the long term test of the Guayuyaco-1 and Guayuyaco-2 wells. Ecopetrol has advised Argosy of a material difference in the interpretation of the procedure established in the Clause 3.5 of Attachment-B of the Guayuyaco Association Contract. Ecopetrol interprets the contract to provide that the extend test production up to a value equal to 30% of the direct exploration costs of the wells is for Ecopetrol's account only and serves as reimbursement of its 30% back in to the Guayuyaco discovery. Argosy's contention is that this amount is merely the recovery of 30% of the direct exploration costs of the wells and not exclusively for benefit of Ecopetrol. While Argosy believes its interpretation of the Guayuyaco Association Contract is correct, the resolution of this issue is still pending of agreement between the parties or determination through legal proceedings. The estimated value of disputed production is \$2,361,188 which possible loss is shared 50% (\$1,180,594) with Solana Petroleum Exploration (Colombia) S.A. partner in the contract and 50% Argosy. No amount has been accrued in the financial statements related to this disagreement.

Currently, no other legal claims or proceedings are pending against us (i) which claim damages in excess of 10% of our current assets, (ii) which involve bankruptcy, receivership or similar proceedings, (iii) which involve federal, state or local environmental laws, or (iv) which involve any of our directors, officers, affiliates, or stockholders as a party with a material interest adverse to us. To our knowledge, no proceeding against us is currently contemplated by any governmental authority.

**Item 2. Unregistered Sales of Equity Securities & Use of Proceeds**

None

**Item 3. Defaults on Senior Securities**

None

**Item 4. Submission of Matters to a Vote of Security Holders**

None

**Item 5. Other Information**

None

**Item 6. Exhibits and Reports on Form 8-K**

The following exhibits are filed with or incorporated as part of this report as required by Item 601 of Regulation S-B:

<b>Exhibit No.</b>	<b>Description</b>	<b>Incorporated by Reference to Filings Indicated</b>
31.1	Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer*	
31.2	Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer*	
32	Section 1350 Certifications*	

\* filed herewith

**SIGNATURES**

In accordance with the requirements of the Exchange Act, the registrant has caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

GRAN TIERRA ENERGY,  
INC.

Date: November 17, 2006      /s/ Dana Coffield  
By: Dana Coffield  
Its: Chief Executive Officer

Date: November 17, 2006      /s/ James Hart  
By: James Hart  
Its: Chief Financial Officer

**EXHIBIT INDEX**

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