GREENFIELDS PETROLEUM
CORPORATION

Consolidated Financial Statements

For the years ended
December 31, 2011 and 2010

Deloitte.

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INDEPENDENT AUDITOR'S REPORT

To the Shareholders of Greenfields Petroleum Corporation:

We have audited the accompanying consolidated financial statements of Greenfields Petroleum Corporation, which comprise the consolidated statements of financial position as at December 31, 2011, December 31, 2010 and January 1, 2010, and the consolidated statements of net loss, consolidated statements of comprehensive loss, consolidated statements of changes in equity and consolidated statements of cash flows for the years ended December 31, 2011 and December 31, 2010, and the notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements
Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility
Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion
In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Greenfields Petroleum Corporation as at December 31, 2011, December 31, 2010 and January 1, 2010, and its financial performance and its cash flows for the years ended December 31, 2011 and December 31, 2010 in accordance with International Financial Reporting Standards.

Emphasis of matter
Without qualifying our opinion, we draw attention to Note 2 to the consolidated financial statements which indicate that the Corporation's requirements to manage the timing of planned capital programs and obtain sufficient financing to fund its planned future operations and future development costs. These requirements and other matters as described in Note 2 indicate the existence of a material uncertainty that may cast significant doubt upon Corporations' ability to continue as a going concern.

Deloitte & Touche LLP

Chartered Accountants
April 30, 2012
Calgary, Alberta

GREENFIELDS PETROLEUM CORPORATION
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
US$000's

		As at December 31, 2011	As at December 31, 2010 (Note 27)	As at January 1, 2010 (Note 27)
Assets				
Current Assets				
Cash and cash equivalents	(Note 5)	25,289	47,977	1,326
Short term investments	(Note 6)	3,488	-	-
Trade receivables	(Note 7)	3,310	3,373	-
Receivables from related parties	(Note 8)	1,838	2,727	85
Other receivable		61	-	-
Prepaid expenses and deposits	(Note 9)	310	273	33
Inventories	(Note 10)	2,263	-	-
		36,559	54,350	1,444
Non-Current Assets				
Investments		228	291	326
Note receivable from related party	(Note 8)	8,965	-	-
Advances for capital equipment	(Note 11)	10,792	-	-
Deferred tax assets	(Note 20)	-	1,588	-
Property and equipment	(Note 11)	4,583	1,087	8
		61,127	57,316	1,778
Liabilities and Equity				
Current Liabilities				
Accounts payable and accrued liabilities	(Note 12)	4,255	2,279	99
Short term borrowing	(Note 13)	1,018	-	-
Provisions	(Notes 14 & 22)	1,000		
Payables to related parties	(Note 8)	612	2,361	-
Warrants	(Note 15)	976	2,219	-
		7,861	6,859	99
Non-current Liabilities				
Notes payable to related parties	(Note 8)	16,745	-	-
Shareholders' Equity				
Common shares / Member Units	(Note 16)	15	15	4,255
Paid in capital		56,705	56,526	-
Share-based payments reserve	(Note 17)	3,830	1,361	-
Deficit		(23,983)	(7,445)	(2,576)
Investments revaluation reserve		(46)	-	-
Total Shareholders' Equity		36,521	50,457	1,679
		61,127	57,316	1,778

See accompanying Notes to the Consolidated Financial Statements

(signed) "John W. Harkins"
John W. Harkins
Director

(signed) "Michael J. Hibberd"
Michael J. Hibberd
Director

GREENFIELDS PETROLEUM CORPORATION
CONSOLIDATED STATEMENTS OF NET LOSS

US$000's except per share amounts

($ Thousands, except per share amounts)	Years Ended December 31, 2011	2010 (Note 27)
Revenues		
Petroleum and natural gas	20,974	5,078
Transportation and storage fees	2,134	-
Management service fees	3,693	3,013
	26,801	8,091
Expenses		
Operating	20,407	2,509
Transportation	146	153
Exploration and evaluation	1,011	-
Pre-licensing costs	2,613	235
Administrative (Note 21)	15,347	10,492
Depreciation and amortization (Note 11)	168	15
	39,692	13,404
Loss from operating activities	(12,891)	(5,313)
Dividends, interest and other income	(494)	-
Interest expense	293	-
Loss on investments	108	226
Impairment of receivables (Note 8)	1,087	-
Provisions (Notes 14 & 22)	1,954	-
Change in fair value of warrants (Note 15)	(1,225)	908
Loss before income taxes	(14,614)	(6,447)
Deferred income tax expense (recovery) (Note 20)	1,924	(1,578)
Net Loss	(16,538)	(4,869)
Per share		
Net loss per share, basic and diluted (Note 16)	($1.11)	($0.54)

CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

US$000's

	Years Ended December 31, 2011	2010
Net Loss	(16,538)	(4,869)
Loss arising from revaluation of available for sale financial assets during the year	(46)	-
	(46)	-
Total comprehensive loss	(16,584)	(4,869)

See accompanying Notes to the Consolidated Financial Statements

GREENFIELDS PETROLEUM CORPORATION
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY
US$000's

	Years Ended December 31,	
	2011	2010
Member units		
Balance, beginning of year	-	4,255
Issued per long term incentive plan	-	330
Value of unvested restricted units	-	(176)
Distribution to unitholders	-	(4)
		4,405
Cancellation of member units	-	(4,405)
Balance, end of year	-	-
Common stock		
Balance, beginning of year	15	-
Common shares issued upon conversion	-	7
Issued pursuant to private placements	-	3
Issued pursuant to public offering	-	5
Balance, end of year	15	15
Paid in capital		
Balance, beginning of year	56,526	-
Common shares issued upon conversion	-	4,399
Issued pursuant to private placements	-	15,995
Issued pursuant to public offering	-	40,426
Repurchase of common shares	(208)	(21)
Share issue costs	-	(4,587)
Private placement broker commission	(55)	209
Warrant exercise	44	37
Share-based payments	62	59
Excess tax benefit - share grants	336	9
Balance, end of year	56,705	56,526
Share-based payments reserve (Note 17)		
Balance, beginning of year	1,361	-
Share-based payments (Note 17)	2,469	1,361
Balance, end of year	3,830	1,361
Deficit		
Balance, beginning of year	(7,445)	(2,576)
Net loss	(16,538)	(4,869)
Balance, end of year	(23,983)	(7,445)
Investment revaluation reserve		
Balance, beginning of year	-	-
Other comprehensive income for the year	(46)	
Balance, end of year	(46)	-
Total Shareholders' Equity	36,521	50,457

See accompanying Notes to the Consolidated Financial Statements

GREENFIELDS PETROLEUM CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
US$000's

	Years Ended December 31,	
	2011	2010 (Note 27)
Operating Activities		
Income before taxes	(14,614)	(6,447)
Adjustments:		
Share-based payments (Note 17)	2,531	1,576
Depreciation and amortization	168	15
Dividends and interest from investments	(223)	-
Interest income on related party notes receivable	(265)	-
Interest expense on related party notes payable	293	-
Loss on investment	-	217
Change in fair value of warrants (Note 15)	(1,225)	908
Cash interest received	40	-
	(13,295)	(3,731)
Change in non-cash operating working capital (Note 19)	489	(2,004)
Cash used in operating activities	(12,806)	(5,735)
Financing Activities		
Proceeds from issue of common shares	28	57,702
Share issue costs	(55)	(4,326)
Distributions to unitholders	-	(32)
Repurchase of common shares	(208)	-
Change in non-cash working capital (Note 19)	(318)	318
Proceeds from related party notes payable (Note 8)	16,452	-
Cash from financing activities	15,899	53,662
Investing Activities		
Purchase of property and equipment	(2,947)	(1,094)
Advances for capital equipment	(10,792)	-
Notes receivable from related parties	(8,700)	-
Short term investments (Note 6)	(3,578)	(182)
Cash dividends received	117	-
Cash interest received	56	-
Dividends from equity investment	63	-
Cash used in investing activities	(25,781)	(1,276)
(Decrease) Increase in Cash and Cash Equivalents	(22,688)	46,651
Cash and Cash Equivalents, beginning of year	47,977	1,326
Cash and Cash Equivalents, end of year (Note 5)	25,289	47,977

See accompanying Notes to the Consolidated Financial Statements

1. INCORPORATION AND NATURE OF OPERATIONS

Greenfields Petroleum Corporation ("**Greenfields**" or the "**Company**") completed a redomestication from the State of Delaware to the Cayman Islands on August 18, 2011. The head office of the Company is located at 211 Highland Cross Drive, Suite 227, Houston, Texas, 77073, U.S.A., and the registered office is located at Walker House, 87 Mary Street, Grand Cayman, KY1-9005, Cayman Islands. The Company's common shares are listed on Toronto's TSX – Venture Exchange ("**TSX-V**") under the trading symbol "GNF". *See Note 25 – Redomestication of the Company.*

The Company is a junior oil and natural gas exploration and development corporation focused on the development and production of proven oil and gas reserves principally in the Republic of Azerbaijan ("**Azerbaijan**").

On December 22, 2009, Bahar Energy Limited ("**Bahar Energy**"), a joint venture in which the Company owns a 33.33% interest, entered into an Exploration, Rehabilitation, Development and Production Sharing Agreement (the "**ERDPSA**") with the State Oil Company of Azerbaijan ("**SOCAR**") and its affiliate SOCAR Oil Affiliate ("**SOA**") in respect of the offshore block known as the Bahar Project, which project consists of the Bahar Gas Field and the Gum Deniz Oil Field. Bahar Energy has an 80% participating interest, and SOA has a 20% participating interest, in the ERDPSA (together the "**Contractors** or **Contractor Parties**"). Bahar Energy Operating Company Limited ("**BEOC**") was formed for the purpose of acting as Operator of the Bahar Project on behalf of the Contractor Parties under the ERDPSA.

For the first three years of the ERDPSA, 5% of the production (referred to as "Compensatory Production") is delivered to SOCAR. In year four, the percentage increases to 10% of production until the cumulative Compensatory Production delivered equals a specified target amount for oil and for natural gas, calculated separately.

On April 27, 2010, the Azerbaijan Parliament, also referred to as Milli Mejlis, ratified the ERDPSA with SOCAR and its affiliate SOA. On September 29, 2010, the Company was notified by SOCAR that all conditions precedent of the ERDPSA were satisfied and the ERDPSA became effective on October 1, 2010.

Upon assuming control of operations on October 1, 2010, Bahar Energy was required to complete and submit to SOCAR within 90 days the draft rehabilitation and production plan for the Bahar and Gum Deniz fields. The plan, referred to as the "Rehabilitation and Production Programme", was submitted to SOCAR in late December 2010. Under the ERDPSA, Bahar Energy will have the obligation to achieve, not later than three (3) years from the date of SOCAR's approval of the "Rehabilitation and Production Programme", an average daily rate of petroleum production from the contract rehabilitation area during ninety (90) consecutive days 150% of the average 2008 production rates. Meeting the 150% production rate will result in the realization of the full 25 year term of the agreement for the Contract Rehabilitation Area. If Bahar Energy fails to meet the 150% production target within the three year timeframe, SOCAR shall have the right to terminate the ERDPSA in relation to the Contract Rehabilitation Area. Approval of the "Rehabilitation and Production Programme" was received from SOCAR on June 22, 2011 establishing the start date for the three year period in which the production target must be met.

In addition to the 150% production levels for continuance of the ERDPSA for the 25 year term, Bahar Energy is obligated to carry SOA's 20% share of expenditures in the rehabilitation area until production rates are two times the 2008 production rates at which time SOA becomes fully responsible for funding their share of expenditures. The SOA carry for the rehabilitation area is reimbursed out of SOA's share of entitlement petroleum or revenues currently produced from the rehabilitation area. Any unrecovered balance is carried forward from one period to the next. Since the carried costs are reimbursed from current petroleum production and the revenues they create, the impact on Bahar Energy's cash flows are

not materially affected.

Operating Environment of the Company

The Republic of Azerbaijan displays certain characteristics of an emerging market, including the existence of a currency that is not freely convertible in most countries outside of the Republic of Azerbaijan, restrictive currency controls and relatively high inflation. The tax, currency and customs legislation within Azerbaijan is subject to varying interpretations, and changes, which can occur frequently. The future economic direction of the country is largely dependent upon the effectiveness of economic, financial and monetary measures undertaken by the government, together with tax, legal, regulatory and political developments. Management is unable to predict all developments which could have an impact on the Azerbaijani economy and consequently what effect, if any, they could have on the future financial position of the Company. Management believes it is taking all the necessary measures to support the sustainability and development of the Company's business.

2. BASIS OF PRESENTATION

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("**IFRS**") as issued by the International Accounting Standards Board ("**IASB**"). Previously, the Company prepared its annual consolidated financial statements in accordance with Canadian generally accepted accounting principles then applicable to publicly accountable enterprises ("**GAAP**").

As these consolidated financial statements present the Company's initial financial results of operations and financial position under IFRS as at and for the twelve months ended December 31, 2011, including 2010 comparative period, they have been prepared in accordance with IFRS 1, "First-time Adoption of International Financial Reporting Standards".

The preparation of these consolidated financial statements resulted in changes to accounting policies as compared with the most recent annual consolidated financial statements prepared in accordance with GAAP. The accounting policies set out in Note 3 have been retrospectively and consistently applied except where specific exemptions permitted an alternative treatment upon transition to IFRS in accordance with IFRS 1. The impact of the transition from GAAP to IFRS is presented in Note 27.

The policies applied in these consolidated financial statements are based on IFRS issued and outstanding as of April 30, 2012, the date the Board of Directors approved the statements.

The Company is producing, developing and exploring oil and gas properties. The recovery of amounts capitalized for oil and gas properties and assets under construction in the statement of financial position are dependent upon its ability to increase production and complete the development of properties, including related financing requirements. To date, the Company's expenses have exceeded its revenues. These consolidated financial statements have been prepared on a going concern basis, under which the Company is assumed to be able to realize its assets and discharge its liabilities in the normal course of operations. The Company's on-going activities are dependent upon its ability to manage the timing of the planned capital program and/or to obtain sufficient financing to fund its planned future operations and future development costs. Although management is confident that necessary financing will be obtained, there is no certainty that such financing will be obtained on terms acceptable to management which may cast significant doubt about the Company's ability to continue as going concern. The consolidated financial statements do not reflect adjustments that would be necessary if the going concern assumptions were not appropriate. Such adjustments could be material.

The presentation and functional currency of the Company is the United States dollar.

3. SIGNIFICANT ACCOUNTING POLICIES

Consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries and its proportionate share of the accounts of joint ventures. Investments in companies in which the Company maintains control are consolidated in these financial statements. The equity in the subsidiary that is not controlled by the Company is presented in equity as non-controlling interest. Inter-company transactions and balances have been eliminated.

Investments in companies

Investments in affiliated companies over which the Company does not have control, but exercises significant influence, are accounted for on an equity basis. The carrying value is adjusted thereafter to include the Company's pro rata share of post-acquisition income of the investee, computed using the consolidation method, and is reduced by profit distributions received or receivable from the investee. The Company discontinues the use of the equity method from the date when it ceases to have significant influence over an investment and accounts for the investment as a financial instrument, subsidiary or a joint venture as appropriate.

Investments in companies in which the Company does not maintain significant influence or joint control are accounted for on the cost basis.

Critical judgments and estimation uncertainty

The preparation of financial statements in accordance with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as at the date of the consolidated statement of financial position as well as the reported amounts of revenues, expenses, and cash flows during the years presented. Such estimates relate primarily to unsettled transactions and events as of the date of the consolidated financial statements.

In particular, the amounts recorded for depletion and depreciation of property and equipment, the provision for asset retirement obligations ("**ARO**") and the test for impairment and impairment reversals of property and equipment are based on estimates of oil production rates, commodity prices, future costs and other relevant assumptions.

Compensation costs recorded for the share option plan as well as the fair value measurement of the warrants are subject to estimation as they are calculated using the Black-Scholes option pricing model which is based on significant assumptions such as volatility, dividend yield, expected term and forfeiture rate.

Warrants, if converted by the holder, are settled in common shares at the option of the holder. This obligation results in a derivative liability in accordance with IFRS standards. As a result of measuring the liability at fair value under IFRS, fluctuations in the estimated fair value will affect the derivative liability gains and losses that are recognized. The fair value of the liability is determined using the Black Scholes valuation model which is based on the period end share price and the exercise price of the warrants, and assumptions for the risk-free interest rate, expected dividends, and the volatility of the share price. The fair value re-measurement process requires significant judgment and estimates and as such, the actual

settlement of the derivative liability could differ materially from the fair value recorded and could impact future results.

The measurement of income tax expense and the related assets on the consolidated statement of financial position is subject to uncertainty associated with future recoverability of oil and natural gas reserves, commodity prices, the timing of future events and changes in legislation, tax rates and interpretations by tax authorities.

Actual results could differ from these estimates and the differences could be material. The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized prospectively.

Cash and cash equivalents

Cash and cash equivalents include bank deposits and money market investment accounts with maturities of three months or less when purchased.

Accounts receivable

Accounts receivable are recorded based on the Company's revenue recognition policy. The allowance for doubtful accounts provides for specific doubtful receivables, as well as general counterparty credit risk evaluated using observable market information and internal assessments.

Exploration and evaluation costs ("E&E")

Oil and gas exploration, development and production costs are accounted for using the modified successful efforts method. As such, pre-license costs, geological and geophysical costs, lease rentals of undeveloped properties and dry hole and bottom hole contributions are charged to expense when incurred.

All other E&E costs are capitalized, including the cost of acquiring unproved properties and the costs associated with drilling exploratory wells. When recoverable reserves are determined, the relevant expenditure is tested for potential impairment and then transferred to property and equipment. However, if recoverable reserves have not been established, the capitalized costs are charged to expense after the conclusion of appraisal activities. Exploration well costs for which sufficient reserves have been found to justify commercial production will continue to be capitalized as long as sufficient progress is being made to assess the reserves and economic viability of the well and/or related project. When this is no longer the case, the costs are written off.

Property and equipment ("P&E")

P&E is stated at cost less accumulated depreciation and impairment charges and includes the costs of transfers of commercially viable and technically feasible E&E assets, oil and gas development and production assets and Company assets. The initial cost of an asset comprises its purchase price or construction cost, any costs directly attributable to bringing the asset into operation, the initial estimate of the decommissioning liability and capitalized borrowing costs for qualifying assets.

Major replacements are capitalized if it is probable that future economic benefits associated with the item will flow to the Company; the replaced asset is derecognized. Repair and maintenance costs are charged as an expense when incurred.

Depreciation and amortization

Capitalized costs of oil and gas properties are depleted using the unit of production method; acquisition costs of properties are amortized over the Company's best estimate of recoverable reserves. For purposes of these calculations, production and reserves of natural gas are converted to barrels on an energy equivalent basis at a ratio of six thousand cubic feet of natural gas for one barrel of oil. To the extent significant development costs are incurred in connection with undeveloped reserves, such costs are excluded from depletion until the reserves are developed and the assets are ready for their intended use.

The Company's other assets consist mainly of leasehold improvements, computers, software, furniture and fixtures, and support equipment not directly related to oil and gas properties. For these assets depreciation methods and rates have been selected so as to amortize the net cost of each asset over its expected useful life to its estimated residual value.

For assets other than oil and gas properties associated with the Company's proportionate share in the Bahar Energy ERDPSA, depreciation is recorded over the useful life of the asset or the expected economic term of the ERDPSA, whichever is less. Residual values for these assets are assumed to be zero as ownership transfers to SOCAR once all capital costs have been recovered by Contractors. The Contractors' to the ERDPSA and BEOC have continued rights to use these assets after transfer over the economic life of the contract.

Financial assets

The Company assesses at each balance sheet date whether there is any objective evidence that a financial asset is impaired except those reported at fair value through profit or loss. If evidence exists, the measurement of impairment depends on the type of financial asset under review.

The impairments of unquoted equity instruments that are not carried at fair value because their fair value cannot be reliably measured are measured as the difference between the original carrying amount of the financial asset and the present value of estimated future cash flows discounted at the current market rate of return for similar financial assets (if lower); this impairment loss cannot be reversed.

The impairments of assets carried at amortized cost are measured as the difference between the assets carrying amount and the present value of future cash flows discounted at the original effective interest rate. These impairment losses can be reversed if the decrease in impairment can be related objectively to an event occurring after the impairment was recognized.

Non-financial assets

Non-financial assets are assessed for indications of impairment or reversals of previous impairments at the end of each reporting period. If any indication of impairments exists, the recoverable amount of the assets is estimated and, if the carrying amount exceeds the recoverable amount, an impairment loss is recognized for the difference. An asset's recoverable amount is the higher of its fair value less costs to sell and its value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. In determining fair value less cost to sell, recent market transactions are taken into account, if available. If no transactions can be identified, an appropriate valuation model is used.

Impairment is measured for individual assets unless the asset does not generate separately identifiable cash inflows, in which case it is measured for the cash-generating unit ("**CGU**") that the asset belongs to.

A CGU is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets.

E&E assets are tested for impairment when indicators of impairment exist or when technical feasibility and commercial viability are established and the assets are reclassified to P&E. E&E assets are allocated to related CGUs when they are assessed for impairment, but the group of CGUs cannot exceed the operating segment. E&E assets that are determined not to be technically feasible and commercially viable are charged to net income.

A previously recognized impairment loss (on assets other than goodwill) is reversed to the extent that the events or circumstances that triggered the original impairment have changed. The reversal is limited so that the carrying amount of the asset does not exceed its recoverable amount, or exceed the carrying amount that would have been determined, net of depreciation and amortization ("**D&A**"), had no impairment loss been recognized for the asset in prior years.

Share-based payments

Share-based payment costs attributed to all share options granted to employees, directors and service providers are measured at fair value at the date of grant using the Black-Scholes option pricing model and expensed over the vesting period with a corresponding increase to employee benefits reserve. Upon exercise of stock options, the consideration received, together with the amount previously recognized in share-based payments reserve, is recorded as an increase to common stock and paid in capital.

Income taxes

Income tax is recognized through profit or loss except to the extent that it relates to items recognized directly in shareholders' equity, in which case the income tax is recognized directly in shareholders' equity.

The Company uses the liability method to account for income taxes. Under this method, deferred income taxes are based on the difference between assets and liabilities reported for financial accounting purposes from those reported for income tax. Deferred income tax assets and liabilities are measured using the substantively enacted tax rates expected to apply to taxable income in the years in which the temporary differences are expected to be recovered or settled. Deferred income tax assets are recognized to the extent future recovery is probable. Deferred tax assets are reduced to the extent that it is no longer probable that sufficient taxable income will be available to allow all or part of the asset to be recovered due to the uncertainty of timing or to the extent that other events not directly controlled by the Company must occur to allow future asset recovery. Deferred tax assets and tax liabilities are offset to the extent there is a legal right to settle on a net basis.

Revenue recognition

Revenues from the sale of crude oil, natural gas and natural gas liquids are recognized when title passes from the Company to its customer. Crude oil, condensate and natural gas produced and sold by the Company below or above its entitlement share in the related resource properties results in production underliftings or overliftings. Underliftings are recorded as inventory and overliftings are recorded as deferred revenue.

Revenue represents the Company's share of entitlement pursuant to the ERDPSA with SOCAR and does not include the government's share of profit sharing petroleum.

BEOC sells natural gas under a contract which includes clauses for Minimum Annual Quantity ("**MAQ**")

and Minimum Payment Price ("**MPP**"). Together the articles stipulate when the buyer does not take the MAQ volumes, it will pay for the shortfall volumes at the MPP and it has twenty-four months to make-up the volumes and pay the difference between the contract price and the MPP or after twenty-four months buyer forfeits rights to the undelivered gas and the MPP paid for those volumes. The Company initially recognizes undelivered natural gas volumes as a deferred credit at the MPP value until which time the buyer either settles and revenue is recorded at the contract price or after twenty-four months the buyer forfeits rights in the undelivered gas and revenue is recorded at the MPP.

Transportation fees represent revenue for hydrocarbon volumes transported by the Company for another producer who requires pipeline access to oil markets. Storage fees represent revenue for storing, handling and other processing for the same previously mentioned producer who lacks its own field facilities. The transportation and storage fees are recognized on a monthly basis when earned and when ultimate collection is reasonably assured.

Management service fees represent revenue for administrative, operational and technical support provided to Bahar Energy and a legal entity in which the Company has an equity investment. The management fees are recognized on a monthly basis when earned and when ultimate collection is reasonably assured.

Interest income is recognized as earned, over the term of the investment.

Provisions

A provision is recognized if, as a result of a past event, the Company has a present legal or constructive obligation that can be estimated reliably and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by recognizing the present value of the estimated future cash flows, discounted using a risk-free rate.

Asset retirement

The Company, under the ERDPSA in Azerbaijan, will be responsible for the funding into an abandonment fund for the abandonment of assets managed under the agreement. For the Contract Rehabilitation Area, the obligation is to establish an Abandonment Fund escrow account and make systematic contributions into the fund which are immediately chargeable as operating costs for cost recovery purposes. The Company does not have abandonment obligations beyond this funding requirement. The maximum contractual commitment of the contractor parties is to fund up to 15% of cumulative capital costs.

Under the terms of the ERDPSA, within twelve months following the effective date (October 1, 2010), the Contractor parties and SOCAR were to agree and accept the mechanism for making contributions into the Abandonment Fund for the Contract Rehabilitation Area. As of the date of these financial statements, the "Protocol on the Abandonment of Fixed Assets" has been drafted and approved by the Bahar project Steering Committee for submission to SOCAR for approval. The provisions of the protocol specify that an abandonment plan with cost estimate shall be completed no later than one year prior to the tenth calendar year following the effective date of October 1, 2010 with funding of the Abandonment Fund to commence July 1, 2021. The calculation of the quarterly amounts to be funded into the Abandonment Fund are based on the estimated abandonment costs (limited to 15% of cumulative capital costs), cumulative production from the date the Abandonment Fund is established and estimated remaining recoverable reserves.

For the Contract Exploration Area under the ERDPSA, no abandonment obligation exists until there has been a commercial discovery and cumulative production from this contract area reaches 50% of the

recoverable reserves identified in the development plan. At that time, the same funding procedures noted for the Contract Rehabilitation Area will be employed. There is no abandonment obligation in the event that Bahar Energy terminates the ERDPSA or if the exploration term for the Contract Exploration Area is allowed to expire.

The Company will record expenses associated with the abandonment funding obligations as they become contractually due. Since this is a financial obligation only to make systematic cash deposits into the Abandonment Funds, which are then reimbursed through cost recovery under the ERDPSA, the Company records no ARO associated with the Bahar project and currently has no other assets that require abandonment recognition.

Carried interest

The Company conducts certain international operations jointly with foreign governments in accordance with production-sharing agreements pursuant to which proved reserves are recognized using the economic interest method. Under these agreements, the Company pays both its share and the government's share of operating and capital costs. The Company recovers the government's share of these costs from future revenues or production over several years. The government's share of operating costs is included in operating expense when incurred, and capital costs are included in P&E and expensed to DD&A in the period recovered. All recoveries are recorded as revenue in the period of recovery.

Leases

The Company classifies leases entered into as either finance or operating leases. Leases that transfer substantially all of the benefits and risks of ownership to the Company are accounted for as finance leases, which are capitalized and are amortized on a straight-line basis over the period of expected use. Rental payments under operating leases are expensed as incurred.

Per share amounts

Basic per share amounts are calculated using the weighted average number of common shares outstanding during the period. Diluted per share amounts are calculated based on the treasury stock method, which assumes that any proceeds obtained on the exercise of in-the-money stock options and warrant would be used to purchase common shares at the average market price during the period.

Financial instruments

Financial instruments are measured at fair value on initial recognition of the instrument, into one of the following five categories:

- fair value through profit or loss ("**FVTPL**")
- loans and receivables
- held-to-maturity investments
- available for-sale financial assets or
- other financial liabilities

Subsequent measurement of financial instruments is based on their initial classification. Financial assets and financial liabilities are either classified as FVTPL or "designated at fair value through profit or loss" and are measured at fair value and changes in fair value are recognized in net income. Available-for-sale financial instruments are measured at fair value with changes in fair value recorded in other

comprehensive income until the instrument is derecognized or impaired. The remaining categories of financial instruments are measured at amortized cost using the effective interest rate method.

Transaction costs related to financial assets and liabilities at fair value through profit or loss are recognized in profit and loss; when incurred transaction costs are added to the fair value of the all other financial instruments on initial recognition.

Derivative instruments are carried at fair value and reported as assets when they have a positive fair value and as liabilities when they have a negative fair value. Derivatives may be embedded in other financial instruments or contractual arrangements. Derivatives embedded in other instruments are valued as separate derivatives when their economic characteristics and risks are not clearly and closely related to those of the host contract, the terms of the embedded derivative are the same as those of a free standing derivative and the combined contract is not held for trading. When the Company is unable to measure the fair value of the embedded derivative separately, the combined contract is treated as a financial asset or liability that is FVTPL and measured at fair value with changes therein recognized in the consolidated statement of net loss.

Warrants

Warrants have an exercise price denominated in Canadian dollars while the Company's functional currency is U.S. dollars. As the amount of U.S. dollars that the Company will ultimately receive for each share issued is variable, the warrants must be classified as a financial liability at fair value through profit or loss. Accordingly, they are measured at fair value each statement of financial position date using the Black-Scholes option pricing model with changes in fair value (including the foreign exchange impact) recognized in profit or loss.

Foreign currency translation

Items included in the financial statements of each of the Company's entities are measured using the currency of the primary economic environment in which the entity operates (the functional currency). The Company and its subsidiaries, joint ventures and partnerships have a United States ("**U.S.**") dollar functional currency. Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions or valuation when items are remeasured. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in the statement of net loss, except when deferred in other comprehensive income as qualifying cash flow hedges and qualifying net investment hedges.

Borrowing Costs

Borrowing costs that are directly attributable to the acquisition or construction of an asset that necessarily takes a substantial period of time to get ready for its intended use are capitalized as part of the cost of that asset. Borrowing costs are capitalized by applying interest rates attributable to the project being financed and includes both general and specific borrowings. Interests rates applied from general borrowings are computed using the weighted average borrowing rate for the period.

4. FUTURE ACCOUNTING CHANGES

The Company has reviewed new and revised accounting pronouncements that have been issued but are not yet effective as of April 30, 2012.

IFRS 9 – Financial Instruments. In November 2009, the IASB issued IFRS 9, "Financial Instruments", which is the result of the first phase of the IASB's project to replace IAS 39, "Financial Instruments: Recognition and Measurement". In October 2010, the standard was revised. The new and revised standard replaces the current multiple classification and measurement models for financial assets and liabilities with a single model that has only two classification categories: amortized cost and fair value. The standard is required to be adopted for periods beginning January 1, 2015. The adoption of this standard should not have a material impact on the Company's consolidated financial statements.

In May 2011, the IASB issued IFRS 10 "Consolidated Financial Statement", IFRS 11 "Joint Arrangements", IFRS 12 "Disclosures of Interests in Other Entities", and amendments to IAS 27 "Separate Financial Statements" and IAS 28 "Investments in Associates and Joint Ventures".

IFRS 10 creates a single consolidation model by revising the definition of control in order to apply the same control criteria to all types of entities, including joint arrangements, associates and special purpose vehicles.

IFRS 11 establishes a principle-based approach to the accounting for joint arrangements by focusing on the rights and obligations of the arrangement and limits the application of proportionate consolidation accounting to arrangements that meet the definition of a joint operation.

IFRS 12 is a comprehensive disclosure standard for all forms of interests in other entities, including joint arrangements, associates and special purpose vehicles.

The amended IAS 28 establishes the accounting for investments in associates and defines how the equity method is applied when accounting for associates and joint ventures.

The amended IAS 27 establishes the accounting and disclosure requirements for investments in subsidiaries, joint ventures, and associates when an entity prepares separate financial statements and replaces the current IAS 27 "Consolidated and Separate Financial Statements" as the consolidation guidance is included in IFRS 10.

Retrospective application of these standards with relief for certain transactions is effective for fiscal years beginning on or after January 1, 2013, with earlier application permitted if all five standards are collectively adopted. The implementation of the issued standard is not expected to have a significant impact on the Company's financial position or results.

IAS 12 – Income Taxes. IAS 12 "Income Taxes" was amended on December 20, 2010 to remove subjectivity in determining on which basis an entity measures the deferred tax relating to an asset. The amendment introduces a presumption that an entity will assess whether the carrying value of an asset will be recovered through the sale of the asset. The amendment to IAS 12 is effective for reporting periods beginning on or after January 1, 2012. The implementation of the issued standard is not expected to have a significant impact on the Company's financial position or results.

IFRS 13 – Fair Value Measurement. In May 2011, the IASB issued IFRS 13 Fair Value Measurement, which establishes a single source of guidance for all fair value measurements; clarifies the definition of fair value; and enhances the disclosures on fair value measurement. Prospective application of this

standard is effective for fiscal years beginning on or after January 1, 2013, with early application permitted. The implementation of the issued standard is not expected to have a significant impact on the Company's financial position or results.

IAS 1 – Presentation of Items on Other Comprehensive Income. In June 2011, the IASB issued amendments to IAS 1, "Presentation of Items of Other Comprehensive Income", to split items of other comprehensive income (OCI) between those that are reclassed to income and those that are not. The standard is required to be adopted for periods beginning on or after July 1, 2012. The implementation of the issued standard is not expected to have a significant impact on the Company's financial position or results.

IAS 19 – Employee Benefits. In June 2011, the IASB issued amendments to IAS 19 "Employee Benefits". The amendments will improve the recognition and disclosure requirements for defined benefit plans. The new requirements are effective for annual periods beginning on or after January 1, 2013, with earlier application permitted. This amendment will not impact our financial statements.

IFRS 7 – Financial Instruments: Disclosures. In December 2011, the IASB issued final amendments to IFRS 7, "Financial Instruments: Disclosures" relating to the requirements for the offsetting of a financial asset and financial liabilities when offsetting is permitted under IFRS. The disclosure amendments are required to be adopted retrospectively for periods beginning January 1, 2013.

IAS 32 – Financial Instruments: Presentation. In December 2011, the IASB issued amendments to IAS 32 "Financial Instruments: Presentation" to address inconsistencies when applying the offsetting criteria outlined in this standard. These amendments clarify certain of the criteria required to be met in order to permit the offsetting of financial assets and financial liabilities. The standard is required to be adopted retrospectively for periods beginning January 1, 2014.

5. CASH AND CASH EQUIVALENTS

The Company periodically invests its idle cash in deposits and short term money market investments with maturity dates of less than three months. At December 31, 2011, the Company had a total of $20.8 million (December 31, 2010 - $ 40.0 million) invested in cash equivalents earning a money market rate of interest.

Cash and cash equivalents include the Company's proportionate share of cash in Bahar Energy of $1.3 million at December 31, 2011 (2010 - $ 3.1 million).

6. SHORT TERM INVESTMENTS

(US$000's)	December 31, 2011	December 31, 2010	January 1, 2010
Corporate bonds at amortized cost	3,534	-	-
Fair market value adjustment	(46)	-	-
	3,488	-	-

The Company periodically invests in investment grade corporate bonds and income producing blue chip equity instruments. At December 31, 2011, the Company had a total of $3.5 million (December 31, 2010 - $ nil) invested in BBB grade or better corporate bonds with maturities ranging from three to twenty eight

months. For the year ended December 31, 2011, the Company earned interest income of $56 thousand (2010 – $ nil).

7. TRADE RECEIVABLES

(US$000's)	December 31, 2011	December 31, 2010	January 1, 2010
Petroleum	1,923	1,683	-
Natural gas	529	1,690	-
Transportation and storage fees	858	-	-
	3,310	3,373	-

8. RELATED PARTY TRANSACTIONS

Receivables from related parties

At December 31, 2011, the Company had a balance of $1.8 million (December 31, 2010 - $2.7 million) in accounts receivable with Bahar Energy. During 2011 the Company recorded an impairment provision of $1.1 million (2010 - $ nil) associated with pre-effective date costs invoiced to Bahar Energy. Management is continuing to pursue the collection of these costs. Management does not believe the remaining $1.8 million, of which $1.1 million is considered past due, poses a collection risk as these charges are associated with amounts invoiced in the normal course of business on "Affiliate Service Orders" ("**ASO**") approved by BEOC. Management considers all of the balances due are collectable including those amounts currently impaired.

For the year ended December 31, 2011 the Company recorded $3.5 million in management service fees for management, administrative and technical services performed at cost for Bahar Energy under ASO's noted above. For the year ended December 31, 2010 the Company recorded management service fees of $2.5 million related to pre-effective date costs invoiced to Bahar Energy, of which $1.4 million has been paid and the remaining $1.1 million impaired until collection can be assured.

Note receivable from related party

At December 31, 2011, the Company has a note and interest receivable balance of $ 9 million (December 31, 2010 - $ nil) related to a loan made to Bahar Energy under the "Common Terms Agreement" ("**CTA**").

Interest accumulates at the three month London Interbank Offer Rate ("**LIBOR**") quoted on a calendar quarter plus 4.5%. *See Note 22, Commitments and Contingencies and Note 8, Notes payable below.*

Compensation of key management personnel

Key management personnel include the Chief Executive Officer, Chief Operating Officer, Chief Financial Officer, Chief Technical Officer and Senior Vice President Engineering. Compensation paid to and share-based compensation attributable to key management personnel consists of the following:

(US$000's)	December 31, 2011	December 31, 2010
Short-term benefits	1,543	1,399
Share-based payments	931	974
Termination benefits	182	-
	2,656	2,373

The compensation of directors and key executives is determined by the compensation committee having regard to the performance of individuals and market based.

Payables to related parties

At December 31, 2011, the Company had a $ 0.6 million (December 31, 2010 - $2.4 million) payable balance to certain shareholders of Bahar Energy associated with amounts invoiced on "Affiliate Service Orders" ("**ASO**") and other direct invoicing for services provided to Bahar Energy Operating Company Ltd. ("**BEOC**"), a jointly controlled entity. The payable balance at December 31, 2010 is for the funding by the shareholders of their share of pre-effective date petroleum operation expenses invoiced to the Bahar project after the effective date of October 1, 2010.

Under the terms of the ERDPSA, the affiliates of Bahar Energy may bill for management, administrative, support and technical support services provided to BEOC under ASO's, which billing rates are to be at partners' cost not to exceed commercial rates that would typically be charged by a third party. For the year ended December 31, 2011 the Company recorded $3.0 million associated with its proportionate share of costs billed by affiliates of Bahar Energy to BEOC (2010 - $2.7 million). The costs billed in 2010 are primarily pre-effective date costs incurred by Bahar Energy affiliates with respect to expenditure associated with assuming Bahar operations under the ERDPSA on October 1, 2010.

Notes payable to related parties

At December 31, 2011, the Company, through its 33.33% interest in Bahar Energy, had a related party notes payable balance of $16.7 million (December 31, 2010 – $ nil) payable to shareholders of Bahar Energy. The notes payable balance is the result of funding under the CTA between the shareholders of Bahar Energy whereby each shareholder agrees to grant a credit facility to Bahar Energy up to specific amounts during a commitment period, limited to the amounts included in the annual signed Loan Agreements, which are based on the annual work plan approved under the ERDPSA.

Bahar Energy may request a draw or advance under a Loan Agreement subject to the terms of the CTA. The proceeds from each loan that is advanced under the Loan Agreement shall be applied to the approved Annual Work Program and Budget of the ERDPSA and for general corporate purposes as authorized by the shareholders of Bahar Energy. Interest accumulates at the three month LIBOR rate quoted on a calendar quarter plus 4.5%, which the Company has deemed to be an appropriate commercial rate.

Loan repayment will be funded from the future cash flows from the ERDPSA that remain after retention by Bahar Energy of funds required for near term operations and adequate cash reserves. Because current

projections of cash flows from the Bahar project to repay the loan extend beyond a twelve month period, the Company has classified both the "Notes receivable from related party" and the "Notes payable to related parties" as non-current assets and liabilities.

9. PREPAID EXPENSES AND DEPOSITS

At December 31, 2011, the Company had non-refundable prepaid expenses and deposits balance of $0.3 million (December 31, 2010 - $0.3 million).

10. INVENTORIES

At December 31, 2011, the Company had inventories of $2.3 million (December 31, 2010 - $ nil), relating to operating materials and supplies consisting of spare parts, consumables, lubricants and fuel.

11. PROPERTY AND EQUIPMENT

(US$000's)	Assets Under Construction [1]	Oil and Gas Properties [1]	Corporate and Other	Total
Fixed Assets				
As at January 1, 2010	-	-	10	10
Additions	352	666	76	1,094
As at December 31, 2010	352	666	86	1,104
Additions	3,010	189	465	3,664
Transfers	(352)	352	-	-
As at December 31, 2011	3,010	1,207	551	4,768
Accumulated DD&A				
As at January 1, 2010	-	-	2	2
Additions	-	3	12	15
As at December 31, 2010	-	3	14	17
Additions	-	69	99	168
As at December 31, 2011	-	72	113	185
Net property and equipment				
As at January 1, 2010	-	-	8	8
As at December 31, 2010	352	663	72	1,087
As at December 31, 2011	3,010	1,135	438	4,583

[1] Assets Under Construction and Oil and Gas Properties represent the Company's proportionate share in Bahar Energy.

At December 31, 2011 the Company has a balance of $10.8 million in non-refundable advances for capital equipment purchases (December 31, 2010 – $ nil), primarily related to casing, tubing and wellhead equipment purchases for new drilling in the Gum Deniz and Bahar fields scheduled to commence in June 2012.

In accordance with the provisions of the ERDPSA, title to fixed and moveable assets will be transferred to SOCAR upon the earlier of the end of the calendar quarter following the date when all capital costs incurred by the Company are recovered or the termination of the ERDPSA. The definitions of operating costs and capital costs contained within the ERDPSA require subjective interpretation in determining the classification of these expenditures. The classification of these costs as operating expenditures is consistent with the annual work program and the budgets which have been approved by the Steering and Operating Committee of BEOC.

In accordance with the terms of the ERDPSA, Contractor parties and BEOC are granted the exclusive right of use for petroleum operations, without charge by SOCAR, all assets previously used by "Gum Adasi" Oil and Gas Production Division of SOCAR, that existed prior to the ERDPSA effective date. These assets are made available for use in petroleum operations to the Company for the economic life of the ERDPSA. However, SOCAR retains the right of ownership to such capital assets, therefore the Company's property and equipment related to the ERDPSA do not include values of those assets transferred to the Company from SOCAR that existed prior to the effective date.

12. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

(US$000's)	December 31, 2011	December 31, 2010	January 1, 2010
Trade accounts payable	2,406	1,988	99
Accrued liabilities	1,837	291	-
Other payable	12	-	-
	4,255	2,279	99

13. SHORT TERM BORROWING

At December 31, 2011 the Company has recorded a liability associated with short term borrowing of $1 million (December 31, 2010 – $ nil) to reflect its 33.33% share of temporary bank loans arranged by BEOC to cover short-term cash shortfalls due to the timing of commitments made by the organization and the receipt of revenue proceeds and operating cash call funding by Bahar Energy. The loans are typically repaid within 30 days.

The funds received from short term borrowing in December 2011 were repaid by BEOC in January 2012.

14. PROVISIONS

At December 31, 2011 the Company has recorded a provision for potential claims settlement in the amount of $1 million (2010 - $ nil). The provision arose from a former consultant's claim. The Company, in an attempt to resolve the matter, has proposed a consulting agreement with the consultant. The value of the cash portion of the agreement is $1.0 million. In addition, selected shareholders who are also officers of the Company will transfer shares of their own stock in the Company to the consultant.

15. WARRANTS

(US$000's)	Warrants	Amount
Balance January 1, 2010	-	-
Warrants Issued	530,000	1,322
Fair Value Adjustment	-	908
Exercised (Exercise Price – CND $5.00)	(5,000)	(11)
Balance December 31, 2010	525,000	2,219
Fair Value Adjustment	-	(1,225)
Exercised (Exercise Price = CND $5.00)	(5,500)	(18)
Balance December 31, 2011	519,500	976

The initial value of the Canadian dollar denominated purchase warrants issued on February 24, 2010 was calculated using the Black-Scholes pricing model over the 24 month term of the warrants with a risk free interest rate of 0.87% based on 2 year term US treasury bonds and 104% volatility calculated on a composite of six Toronto Stock Exchange and TSX-V traded companies with similar company profiles.

The fair value as at the measurement dates of December 31, 2011 and December 31, 2010 was calculated using the Black-Scholes pricing model with reassessed volatility of 22% and 50% respectively, along with term, interest rate, and exchange rate assumptions consistent with these measurement dates and applied over both the warrant exercises and remaining net balances.

During January and February 2012 all 519,500 outstanding warrants at December 31, 2011 were exercised. *See Note 26 – Subsequent Events.*

16. SHAREHOLDERS' EQUITY

Authorized Share Capital

Authorized share capital of the Company consists of 49,900,000 common shares and 100,000 preferred shares, each at US $.001 par value.

Common Shares

Each common share carries equal voting rights, is non-preferential and participates evenly in the event of a dividend payment or in the winding up of the Company.

Preferred Shares

The Board may issue Preferred Shares at any time and from time to time in one or more series. The Board has the authority to issue Preferred Shares in series and determine the price, number, designation, rights, privileges, restrictions and conditions, including dividend rights, conversion rights, and rights with respect to the distribution of assets in the event of the dissolution or winding up of the Corporation and preferential rights, of each series without further vote or action by shareholders.

There were no preferred shares issued and outstanding at December 31, 2011 (December 31, 2010 – nil, January 1, 2010 - nil).

Share Capital continuity schedule:

Issued shares / member units: *(US$000's, except for share totals)*	Number of Common shares/ Units	Amount
Member units outstanding [1]		
As at January 1, 2010	6,450,000	4,255
Issued per LTIP *(See Note 17)*	500,000	154
Distribution to unitholders	-	(4)
	6,950,000	4,405
Cancellation of member units	(6,950,000)	(4,405)
As at December 31, 2010	-	-
Common shares outstanding		
As at January 1, 2010	-	-
Common shares issue upon conversion	6,950,000	4,405
Issued pursuant to private placements	3,044,077	15,998
Issued pursuant to public offering	4,870,250	40,432
Share issue costs	-	(4,378)
Repurchase of common shares	(3,306)	(21)
Warrants exercised	5,000	37
Share-based compensation	-	68
As at December 31, 2010	14,866,021	56,541
Share issue costs	-	(55)
Repurchase of common shares	(20,641)	(208)
Warrants exercised	5,500	44
Share-based compensation	-	398
As at December 31, 2011	14,850,880	56,720

[1] On February 19, 2010, the Company converted from a Texas limited liability company (LLC) to an incorporated company registered in the State of Delaware and all member units of the LLC were converted to common shares. *See Note 26 – Redomestication of the Company* for subsequent re-domicile of the Company completed in August 2011.

Reconciliation of Issued and Outstanding Shares

	December 31, 2011	December 31, 2010
Issued	14,874,827	14,869,327
Treasury shares acquired by Company *(See Note 17)*	(23,947)	(3,306)
Total Outstanding	14,850,880	14,866,021

On June 30, 2011, all 23,947 treasury shares acquired by the Company were cancelled (2010 – nil).

Per Share Information

For the twelve months ended December 31, 2011, basic per share amounts are calculated using the weighted average number of common shares outstanding of 14,849,797 (2010 – 8,962,607).

Per share loss *(US$000's, except for per share amount)*	December 31, 2011	December 31, 2010
Net loss	(16,538)	(4,869)
Basic and diluted loss per share	($1.11)	($0.54)

The average market value of the Company's common shares used for purposes of calculating the dilutive effect of share options and warrants was based on quoted market prices for the period that the equity instruments were outstanding. For the year ended December 31, 2011, 1,392,250 options (December 31, 2010 – 1,211,000 options) and 519,500 warrants (December 31, 2010 – 525,000) were excluded from calculating dilutive earnings as they were anti-dilutive.

17. SHARE BASED PAYMENTS

The Company has a stock option plan that governs the granting of options to employees, officers and directors. All options issued by the Company permit the holder to purchase a specific number of common shares of the Company at the stated exercise price. The Company has not issued stock options that permit the recipient to receive a cash payment equal to the appreciated value in lieu of stock.

Continuity of Stock Options	December 31, 2011		December 31, 2010	
	Number of shares underlying options	Average exercise price (CND$)	Number of shares underlying options	Average exercise price (CND$)
Outstanding, beginning of year	1,211,000	6.87	-	-
Granted	230,000	8.64	1,211,000	6.87
Forfeited	(48,750)	6.50	-	-
Outstanding, end of year	1,392,250	7.17	1,211,000	6.87
Exercisable, end of year	721,750	6.98	302,750	6.87

Share-based payments reserve

(US$000's)	Amount
Balance January 1, 2010	-
Stock options share-based payments	1,361
Balance December 31, 2010	1,361
Stock options share-based payments	1,515
Share-based settlement provision *(Note 14 & 22)*	954
Balance December 31, 2011	3,830

The exercise price of the share options range from CDN$6.50 to CDN$9.50 per common share with all options expiring on various dates between years 2016 and 2021. The share options vest 25% at date of grant and 25% on each of the first, second and third anniversaries of grant date. The 721,750 exercisable options as at December 31, 2011 have remaining contractual lives ranging from 4.67 to 9.39 years.

As a provision of the Company's Stock Option Plan, the optionee may make the following election when exercising options at the discretion of the Compensation Committee:

> *When an optionee incurs a tax liability in connection with an option which is subject to tax withholding under applicable tax laws and the optionee is obligated to pay the Company the required withholding amount due, the optionee may satisfy the tax withholding obligation in two methods other than payment in cash; (i) by surrendering to the Company common shares that have been owned by the optionee for more than six months on the date of surrender with a market value equal to the withholding tax obligation or (ii) by electing to have the Company withhold from the common shares to be issued upon exercise of the options the number of common shares having a market value equal to the tax amount required to be withheld.*

The fair value of each stock option granted was estimated on the date of grant using the Black-Scholes option pricing model with the following assumptions:

	2011	2010
Risk-free interest rate range	0.9% - 2%	1.33% - 1.49%
Expected life	4.0 years	4.0 years
Expected volatility	47.25%	49.53%
Expected dividend	-	-
Forfeiture [1]	-	-
Weighted average fair value	$3.40	$2.58

[1] Managements estimated forfeiture rate of 0% is based on the fact that option holders have long-term involvement with current and a predecessor company and the experience has showed little to no turnover within both organizations which would result in the forfeiture of option rights.

Acquisition of common shares

In February 2011, the Company acquired 20,641 common shares at fair market value of CDN$10.00 per share from certain employees as a result of share grants vesting from the February 2, 2010 Long Term Incentive Plan ("**LTIP**"). The LTIP provides the option to employees to pay cash or sell to the Company the number of shares equal to their statutory withholding tax due at vesting date to reimbursement the

Company for settling the employees' withholding tax obligation.

As a provision of the original 2010 LTIP, the Company is authorized to withhold from participants any amounts due in cash or shares for any applicable taxes payable at the minimum statutory rate in respect of the share grant awards. The tax withholding obligation of the participant in respect of the vesting share grants can be satisfied through the sale to the Company of such number of shares with a fair market value at vesting date equal to the tax withholding obligation.

During the third quarter of 2010, the Company acquired 3,306 common shares at CDN$6.50 from a former officer who had made the same election to sell shares to the Company noted above.

As at December 31, 2011, all treasury shares previously held by the Company as a result of the acquisition of common shares under the Company's LTIP have been cancelled.

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18. SEGMENTED INFORMATION

The Company's reportable and geographical segments are Azerbaijan and Corporate and Other. Other includes the Company's corporate offices and new venture business development activities outside of Azerbaijan. The accounting policies used for the reportable segments are the same as the Company's accounting policies.

The Company began its operations in Azerbaijan in the fourth quarter of 2010. Accordingly, segmented information for Azerbaijan reflects activity from the fourth quarter of 2010 only. The segment information related to Azerbaijan represents the Company's proportionate share of Bahar Energy revenues, expenses, assets and liabilities.

Total Assets and Liabilities

(US$000's)	December 31, 2011			December 31, 2010		
	Azerbaijan	Corporate and Other	Total	Azerbaijan	Corporate and Other	Total
Current assets	7,082	29,477	36,559	6,792	47,558	54,350
Non-current assets	-	9,193	9,193	176	1,703	1,879
Capital assets	15,304	71	15,375	1,023	64	1,087
Total assets	22,386	38,741	61,127	7,991	49,325	57,316
Current liabilities	(5,002)	(2,859)	(7,861)	(4,081)	(2,778)	(6,859)
Non-current liabilities	(16,745)	-	(16,745)	-	-	-

Capital Expenditures

	Year ended					
(US$000's)	December 31, 2011			December 31, 2010		
	Azerbaijan	Corporate and Other	Total	Azerbaijan	Corporate and Other	Total
Capital Expenditures	13,690 [(1)]	49	13,739	1,026	68	1,094

[(1)] Includes Advances for capital equipment of $10.8 million.

Statement of net loss by segment *(US$000's)*	**Year ended**					
	December 31, 2011			December 31, 2010		
	Azerbaijan[1]	Corporate and Other	Total	Azerbaijan[1]	Corporate and Other	Total
Revenues						
Petroleum and natural gas (external)	20,974	-	20,974	5,078	-	5,078
Transportation and storage fees (external)	2,134	-	2,134	-	-	-
Management services fees	-	3,693	3,693	-	3,013	3,013
	23,108	3,693	26,801	5,078	3,013	8,091
Expenses						
Operating	20,407	-	20,407	2,509	-	2,509
Transportation	146	-	146	153	-	153
Exploration and evaluation	1,011	-	1,011	-	-	-
Pre-licensing costs	-	2,613	2,613	-	235	235
Administrative	4,219	11,128	15,347	3,216	7,276	10,492
Depreciation and amortization	128	40	168	3	12	15
	25,911	13,781	39,692	5,881	7,523	13,404
Loss from operating activities	(2,803)	(10,088)	(12,891)	(803)	(4,510)	(5,313)
Dividends, interest and other income	-	(494)	(494)	-	-	-
Interest expense	293	-	293			
Loss on investments	-	108	108	-	226	226
Impairment of receivables	-	1,087	1,087			
Provisions	-	1,954	1,954			
Change in fair value of warrants	-	(1,225)	(1,225)	-	908	908
	(3,096)	(11,518)	(14,614)	(803)	(5,644)	(6,447)
Deferred Income tax expense (recovery)	281	1,643	1,924	(281)	(1,297)	(1,578)
Net loss	(3,377)	(13,161)	(16,538)	(522)	(4,347)	(4,869)

[1] All results reported under Azerbaijan represent the Company's 33.33% proportionate share in Bahar Energy.

Major customers

For the year ended December 31, 2011, 100% petroleum and natural gas revenues of $21 million (December 31, 2010 – $5.1 million) were derived from a single external customer, the State Oil Company of Azerbaijan. Petroleum and natural gas revenues for 2010 reflect operating results from October 1, 2011, the effective date of the ERDPSA.

For the year ended December 31, 2011 the Company recorded $3.5 million (2010 - $2.5 million) in management service fees for management, administrative and technical support services performed for BEOC. *(See Note 8 – Related Party Transactions)*

19. SUPPLEMENTAL CASH FLOW INFORMATION

Changes in non-cash working capital items related to operating activities:

	Year Ended December 31,	
(US$000's)	2011	2010
Trade receivables	63	(3,373)
Receivables from related parties	889	(2,642)
Other receivable	(7)	-
Prepaid expenses and deposits	(36)	(240)
Accounts payable and accrued liabilities	1,574	1,890
Short term borrowing	1,018	-
Provisions	1,000	-
Inventories	(2,263)	-
Payables to related parties	(1,749)	2,361
	489	(2,004)

Changes in non-cash working capital items related to financing activities:

	Year Ended December 31,	
(US$000's)	2011	2010
Accounts payable and accrued liabilities	(318)	318
	(318)	318

Changes in non-cash working capital items related to investing activities:

	Year Ended December 31,	
(US$000's)	2011	2010
Accounts payable and accrued liabilities	718	-
	718	-

20. DEFERRED INCOME TAXES

The provision for income taxes differs from the result that would have been obtained by applying the U.S. federal income tax rate of 35% to the loss before income taxes. The difference results from the following items:

(US$000's)	Year Ended December 31, 2011	2010
Deferred income tax expense (recovery) per statements	1,924	(1,578)
Adjustments in respect to prior years	(1,588)	-
Deferred income tax expense (recovery) – current year	336	(1,578)

(US$000's)	Year Ended December 31, 2011	2010
Comprehensive loss before income taxes	(14,660)	(6,447)
U.S. federal corporate income tax rate	35%	35%
Expected income tax (recovery) expense computed at statutory rates	(5,131)	(2,256)
Add (deduct) the tax effect of:		
Non-taxable / deductible items	1,089	213
Warrants fair value adjustment	(428)	318
Share-based payments	784	147
Deferred income tax (recovery) expense per calculation	(3,686)	(1,578)
Derecognition of deferred tax asset for current year	4,022	-
Deferred Income tax (recovery) expense per statements	336	(1,578)
Current year deferred income taxes consists of:		
Current tax (recovery)	(2,838)	(1,230)
Deferred tax (recovery)	(848)	(348)
Deferred Income tax (recovery) before tax asset derecognition	(3,686)	(1,578)
Derecognition of deferred tax asset	4,022	-
Adjustments in respect to prior years [(1)]	1,588	-
Deferred income tax expense (recovery)	1,924	(1,578)

[(1)] Includes derecognition of deferred tax asset previously recognized in equity.

Deferred Income Tax Asset

The components of the Company's unrecognized deferred tax assets arising from temporary differences and loss carryforwards as well as the associated amount of deferred tax recovery or expense recognized in the Company's statements of operations and comprehensive income are as follows:

A continuity of the net deferred income tax asset (liability) is detailed in the following table:

(US$000's)	Recognized in profit or loss	Recognized in equity	Total
Balance at January 1, 2010	-	-	-
Current loss carryforwards	1,240	-	1,240
Share-based compensation	335	10	345
Other non-capital losses	3	-	3
Balance at December 31, 2010	1,578	10	1,588
Current loss carryforwards	2,838		2,838
Share-based compensation	80	336	416
Other non-capital losses	768		768
As at December 31, 2011	5,264	346	5,610
Derecognition of deferred tax asset	(5,610)	-	(5,610)
As at December 31, 2011 after derecognition	(346)	346	-

At December 31, 2011, the Company has cumulative loss carryforward of approximately $10.6 million that will expire in 2030 and 2031. The Company expects to be able to fully utilize these losses and the associated deferred tax asset noted above, but has elected to derecognize the cumulative deferred tax asset until such time recovery and offset against future income can be assured.

Currently, the Company's primary income producing assets are held through its 33.3% ownership in Bahar Energy. The project, being in the early rehabilitation and development stage, requires significant development funding and re-investment of operating cash flows for the foreseeable future. Earnings from the Bahar project are not taxable to the Company until Bahar Energy declares dividends from the surplus funds generated from the ERDPSA. Before Bahar Energy can declare dividends, shareholders loans must be repaid with accumulated interest expense, which will be returned to the Company non-taxable.

Under IFRS, when an entity has a history of recent losses, the entity should recognize a deferred tax asset from unused tax losses and tax credits only to the extent that there is sufficient taxable temporary differences or there is convincing other evidence that sufficient taxable profits will be available against which unused taxable losses and tax credit can be utilized within the foreseeable future. IFRS also allows an entity to recognize previously unrecognized tax assets to the extent future profits will allow recovery before expiration.

With much of the early funds returned from Bahar Energy being non-taxable as loan repayments, the Company's potential taxable dividends horizon is beyond that normally allowed under IFRS for recognition of deferred tax assets. As noted above, the Company has elected to derecognize its accumulated deferred tax asset, but will continue to reassess the unrecognized deferred tax asset at the end of each reporting period.

Azerbaijan

The Company is tax protected under the terms of the ERDPSA in Azerbaijan. In accordance with the terms of the agreement, the Company determines the liability for income tax which would otherwise be payable in connection with its Azerbaijan operations. Any such tax determined in connection with the Company's operations is paid by the SOCAR from their share of production and the Company retains no liability for payment of income taxes.

21. EXPENSES BY NATURE

	Year ended	
(US$000's)	December 31, 2011	December 31, 2010
ADMINISTRATIVE		
Employee wages and benefits	3,782	2,267
Share-based payments	1,577	1,576
Professional service costs	4,076	2,120
Office, travel and other	1,693	1,313
Foreign office costs	4,219	3,216
Total expenses by nature	15,347	10,492

22. COMMITMENTS AND CONTINGENCIES

The following is a summary of the Company's contractual obligations and commitments as of December 31, 2011:

(US$000's)	**2012**	**2013**	**Thereafter**
Operating leases	76	-	-
Annual lease retention fees	72	72	-
	148	72	-

The Company has committed to a lease of office space for its corporate headquarters in the United States expiring in June 2012 and is current negotiating an extension.

Pursuant to the ERDPSA, Bahar Energy is obligated to pay annual acreage fees of $216 thousand, $72 thousand net to the Company, for a period of three years to the SOCAR beginning on the first anniversary date of the effective date of October 1, 2010. There are two years remaining of the three year commitment. In addition to the acreage fees, Bahar Energy is required to complete a "Minimum Exploration Work Program", which includes the shooting, processing and interpretation of a minimum of sixty (60) square kilometers of 3-D seismic over the contract area known as Bahar 2, the carrying out of sight survey in preparation for drilling operations and the drilling of a minimum of one exploration well if the 3-D seismic study identifies a viable exploration drilling target. The Exploration Work Program is to be carried out during the three years from effective date of the ERDPSA.

The Company has signed the Common Term Agreement between the shareholders of Bahar Energy Limited whereby each shareholder agrees to grant a credit facility to Bahar Energy up to specific amounts during a commitment period to fund the approved work programs of the Bahar project. As part of the CTA, the Company has also signed the 2011 Loan Agreement amended to fund up to $22 million during the period January 1, 2011 to December 31, 2011. During May 2011, the Company made the first advance under the 2011 Loan Agreement for $8.7 million. During the first quarter 2012 the Company funded its remaining obligation under the 2011 Loan Agreement up to the $22 million limit. Under a new 2012 Loan Agreement dated January 3, 2012, the Company has agreed to fund up to $28 million to Bahar Energy toward the approved 2012 Work Plan.

The Company has been contacted by a former consultant claiming rights to a referral fee. In an attempt to resolve this, the Company has proposed a consulting agreement with the consultant. The value of the

cash portion of the agreement is $1.0 million. In support of this, selected shareholders who are also officers of the Company will transfer shares of their own stock in the Company to the consultant. *(See Note 14 – Provisions)*

23. FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT

The Company is exposed to the following risks in respect of certain of the financial instruments held:

a) Credit risk

Credit risk is the risk of financial loss to the Company if counterparty to a financial instrument fails to meet its contractual obligations and arises principally from the Company's receivables from subsidiaries and affiliates for services performed under certain administrative services agreements and from advances made under certain joint venture agreements.

The Company's current accounts receivable balances mainly consist of trade receivables from the Company's share of oil and gas revenue, transportation and storage fees generated under the ERDPSA, receivables from affiliates as result of the funding of administrative expenses and costs in connection with the ERDPSA operations, and management fees for administrative and technical support provided to an entity the Company has an equity interest. The Company historically has not experienced any collection issues with its accounts receivable and all of the balances due are considered by management to be collectable at December 31, 2011, except as noted in *Note 8 – Related Party Transactions* (Receivables from related parties).

Cash and cash equivalents consist of bank deposits and short term money market investments held in major United States banks except for cash held in the Bahar Energy joint venture which is limited for use in the ERDPSA. The Company manages the credit exposure related to short term investments by selecting counterparties based on credit rating and monitors all investments to ensure a stable return, avoiding complex investment vehicles with higher risk such as asset-backed commercial paper. Cash held in local bank accounts in Baku, Azerbaijan for the Bahar Energy joint venture are also exposed to the risk of bank failure. That risk is mitigated by keeping amounts in local accounts to only those funds required for near term operations as well as to keep deposits in only the largest and most reputable financial institutions.

The Company's maximum exposure to credit risk at the statement of financial position date is as follows:

Credit risk *(US$000's)*	December 31, 2011	December 31, 2010	January 1, 2010
Cash and cash equivalents	25,289	47,977	1,326
Trade receivables	3,310	3,373	-
Receivables from related parties	1,838	2,727	85
Other receivable	61	-	-
	30,498	54,077	1,411

b) Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they become due. The Company's approach to managing liquidity is to ensure, as much as possible, that it will have sufficient liquidity to meet its obligations when due, under both normal and unusual conditions without incurring unacceptable costs, relinquishment of properties or risking harm to the Company's reputation.

The Company prepares annual and interim period capital expenditure budgets, which are regularly monitored and updated as considered necessary to provide current cash flow estimates. The Company also utilizes authorizations for expenditures on projects to further manage capital expenditures. To facilitate the capital expenditure program, the Company may raise debt and capital through the issuance of shares. Additional financing may be required to complete planned capital programs.

The Company's financial liabilities at December 31, 2011 and December 31, 2010 arose primarily from the recognition of its proportionate share of Bahar Energy liabilities for the Azerbaijan project. Payment terms on the Company's accounts payable and accrued liabilities are typically 30 to 60 days from invoice date and generally do not bear interest. Currently, the Company does not have any bank debt other than the short-term borrowing by Bahar Energy which is generally repaid with 30 days.

The following table summarizes the remaining contractual maturities of the Company's financial liabilities:

Liquidity Risk	December 31, 2011			December 31, 2010	January 1, 2010
(US$000's)	Within 1 year	Within 1 – 3 years	Total	Total	Total
Accounts payable and accrued liabilities	4,255	-	4,255	2,279	99
Short term borrowing	1,018	-	1,018	-	-
Provisions	1,000	-	1,000	-	-
Payables to related parties	612	-	612	2,361	-
Warrants	976	-	976	2,219	-
Notes payable to related parties	-	16,745	16,745	-	-
	7,861	16,745	24,606	6,859	99

c) Currency risk

Foreign currency risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate as a result of changes in foreign currency exchange rates. The Company has minimal exposure to foreign currency fluctuations as a significant portion of the Company's transactions are denominated in the United States dollar and the Company holds almost all of its excess cash in United States dollars.

At December 31, 2011 and December 31, 2010 the Company had no forward exchange contracts in place.

d) Commodity price risk

Commodity price risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate as a result of changes in commodity prices. Commodity prices for petroleum and natural gas are affected by the international economy that governs the level of supply and demand.

The Company's primary revenues are from oil and gas sales produced in Azerbaijan under the ERDPSA. Oil is sold through SOCAR and priced, on a quality differential basis, to the U.S. dollar-based Intercontinental Exchange ("**ICE**") at the Brent oil price at sales date. Natural gas is sold to SOCAR at a fixed price of $140/MCM ($3.96/MCF) under a take or pay formula. Gas over/underliftings are settled also at a fixed price for an initial term of five years.

At December 31, 2011 and December 31, 2010, the Company has no outstanding financial instruments, financial derivatives or physical delivery contracts subject to commodity price risk. Purchases and sales of financial assets are recognized on the settlement date, the date on which the Company receives or delivers the asset.

e) Interest rate risk

Interest rate risk arises from changes in market interest rates that may affect the fair value or future cash flows from the Company's financial assets or liabilities. The Company may partially mitigate its exposure to interest rate changes by holding a mix of both fixed and floating rate debt.

At December 31, 2011, the sensitivity in net earnings for each one percent change in interest rates is not significant.

Fair value of financial instruments

The fair values of financial instruments as at December 31, 2011 and 2010 are disclosed below by financial instrument category as follows:

(US$000's)		Hierarchy Level	December 31, 2011 Carrying Amount	December 31, 2011 Fair Value	December 31, 2010 Carrying Amount	December 31, 2010 Fair Value
Assets at FVTPL						
Cash and cash equivalents		1	25,289	25,289	47,977	47,977
Loans and receivables						
Trade receivables		-	3,310	3,310	3,373	3,373
Receivables from related party	(a)	-	1,838	1,838	2,727	2,727
Notes receivable from related party		-	8,965	8,965	-	-
Other receivables		-	61	61	-	-
Available for sale assets						
Short term investments		2	3,488	3,488	-	-
GFPI-USA	(b)	-	228	228	291	(b)
Other financial liabilities						
Accounts payable and accrued liabilities		-	4,255	4,255	2,279	2,279
Short term borrowing		-	1,018	1,018	-	-
Provisions		-	1,000	1,000		
Payables to related party	(c)	-	612	612	2,361	2,361
Notes payable to related parties	(d)	-	16,745	16,745	-	-
Liabilities at FVTPL						
Warrants		2	976	976	2,219	2,219

a. Balances consist of receivables from Bahar Energy resulting from amounts invoiced on "Affiliate Service Orders" **("ASO")** and other direct invoicing for services provided to Bahar Energy Operating Company Ltd. **("BEOC")**.
b. The investment is measured at cost, as the fair value of this instrument cannot reliably be determined.
c. Balances consist of liabilities to certain shareholders of Bahar Energy associated with amounts invoiced on "Affiliate Service Orders" **("ASO")** and other direct invoicing for services provided to Bahar Energy Operating Company Ltd. **("BEOC")**.
d. The balance represents liabilities arising from the funding of operations by shareholders of Bahar Energy in the form of interest bearing notes to be repaid from future cash flows from the ERDPSA. *See also Note 8, Related Party Transactions.*

Fair Value Hierarchy
Level 1 – Fair value measurement is determined by reference to unadjusted quoted prices in active markets for identical assets or liabilities.
Level 2 – Fair value measurement is based on inputs other than unadjusted quoted prices that are observable, either directly or indirectly.
Level 3 – Fair value measurement using inputs for the asset or liability that are not based on observable market data.

24. CAPITAL STRUCTURE AND MANAGEMENT

The Company considers its capital structure to include common share capital and working capital (a measurement defined as current assets less current liabilities, with current liabilities being as per the number on the face of the consolidated statement of financial position excluding warrants). In order to maintain or adjust the capital structure, the Company may from time to time issue common shares or other securities, sell assets, issue debt or adjust its operating or capital spending to manage current and projected working capital levels.

Composition of the Company's capital structure *(US$000's)*	December 31, 2011	December 31, 2010
Working Capital	29,674	49,710
Shareholders' Equity	36,521	50,457
Working Capital to Shareholders' Equity Ratio	81%	99%

25. REDOMESTICATION OF THE COMPANY

Redomestication of the Company from Delaware to the Cayman Islands

On August 18, 2011, the Company completed a corporate redomestication to the Cayman Islands, resulting in holders of securities of the Company holding securities of a Cayman Islands exempted company rather than a Delaware Corporation (the "Redomestication").

The Redomestication involved three primary steps:

- First, the Company merged with Greenfields Petroleum (Arizona) Corporation ("**AZco**"), an Arizona corporation and a wholly-owned subsidiary of the Company, with AZco surviving the merger and resulting in shareholders of the Company becoming shareholders of AZco ("**AZco Shareholders**");

- Second, AZco became a Cayman Islands exempted company pursuant to a transfer of domicile procedure under Arizona law and continuation procedure under Cayman Islands law; and

- Third, AZco amalgamated with Greenfields Petroleum (Cayman-Sub) Corporation ("**Cayco**"), a wholly-owned subsidiary of AZco formed in the Cayman Islands, pursuant to a scheme of arrangement involving AZco, Cayco and the AZco Shareholders at the effective time of the amalgamation, with Cayco surviving the amalgamation (following the amalgamation, referred to as "**Amalco**").

Prior to the Redomestication, the shares of the Company (the "**Greenfields Shares**") were subject to a one year distribution compliance period and deemed to be "restricted securities" under United States securities laws and were therefore subject to certain restrictions on transfer to U.S. persons (the "**Resale Restrictions**"). As such, all certificates evidencing the Greenfields Shares ("**Share Certificates**") bore a restrictive transfer legend and the Company's' trading symbol on the TSX-V contained a ".S" qualifier to alert investors to the existence of the Resale Restrictions.

Pursuant to the Redomestication, shareholders of the Company received one common share in the capital of Amalco ("**Amalco Share**") for each common share in the capital of the Company formerly held. All outstanding Company options and warrants will remain in effect and survive pursuant to the instruments governing such options and warrants, and represent the right to acquire Amalco Shares.

As a result of the Redomestication, Amalco qualifies as a "foreign private issuer" for the purposes of the United States securities laws, resulting in no restrictive transfer legend on the Amalco Shares currently outstanding, the ".S" qualifier not applying to the Amalco Shares and its trading symbol, and the Amalco Shares becoming generally freely tradable by its current U.S. Shareholders.
Immediately following the Redomestication, Amalco changed its name from "Greenfields Petroleum (Cayman-Sub) Corporation" and adopted "Greenfields Petroleum Corporation" as the final legal name to be used by Amalco. Trading in respect of the Amalco Shares on the TSX-V commenced on August 23, 2011 under the symbol "GNF" (with no ".S" qualifier applying to the new company's trading symbol).

Principal Effects of the Redomestication on Future Financial Reporting and Accounting

The financial accounting and reporting effects of the Redomestication transaction remained substantially similar to the accounting and reporting of the Company prior to the Redomestication. The series of Redomestication steps were transactions between entities under the common control of the same parties.

The accounting involving common control business combinations are outside the scope of IFRS 3 2008 and as yet there is no other specific IFRS guidance. In the absence of specific guidance, entities involved in common control business combination select an appropriate accounting policy using the hierarchy as described in IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors. Because the hierarchy permits the consideration of other standard-setting bodies, the guidance on group reorganization in US GAAP is useful in this circumstance.

As a result, the assets and liabilities of the combined companies are recorded and reported at book value. The post-redomestication balances of the consolidated financial statements of the newly amalgamated companies reflect those of the consolidated financial statements of the Company pre-redomestication. The post-redomestication amounts recorded in equity represents those of the Greenfields' pre-redomestication and the post-redomestication numbers of common shares, share based awards and warrants are those of Greenfields Petroleum Corporation (Cayman). The number of common shares, share-based awards and warrants have not changed as a result of the redomestication due to the one for one exchange ratio.

26. SUBSEQUENT EVENTS

- During January and February 2012, before the February 24, 2012 expiration of the Company's warrants issued pursuant to a private equity placement completed in February 2010, all 519,500 warrants outstanding at December 31, 2011 were exercised resulting in Greenfields raising CDN$2,597,500.

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27. TRANSITION TO IFRS

For all periods up to and including the year ended December 31, 2010, the Company prepared its Consolidated Financial Statements in accordance with Canadian generally accepted accounting principles ("Canadian GAAP" or "previous GAAP"). As a publicly listed company in Canada, the Company is required to prepare consolidated financial statements in accordance with International Financial Reporting Standards ("IFRS") for all periods after January 1, 2010, including comparative historical information.

In accordance with transitional provisions, the Company prepared its opening balance sheet as at January 1, 2010 (the transition date) and 2010 financial information using the accounting policies set out in Note 3. The consolidated financial statements for the year ended December 31, 2011 are the first annual financial statements that comply with IFRS by applying existing IFRS with an effective date of December 31, 2011 or earlier. This transition note explains the material adjustments required to adjust the financial statements from Canadian GAAP to IFRS.

In preparing these consolidated financial statements in accordance with IFRS 1, the following mandatory exceptions from full retrospective application of IFRS were applied.

- Estimates
    - The estimates made under Canadian GAAP are required to be applied to the balances in accordance with IFRS unless there is evidence that the estimates were in error or to reflect any adjustments made to accounting policies to comply with IFRS. Hindsight was not used to create or revise estimates and, accordingly, estimates previously made under Canadian GAAP are consistent with their application under IFRS.
- Non-controlling interests
    - At the date of transition, IFRS prescribes that certain requirements of IAS 27 "Consolidated and Separate Financial Statements" be applied prospectively. The company has adopted these exceptions and applies the relevant IAS 27 requirements prospectively.

The Company has applied the following optional exemptions under IFRS 1 to its opening balance sheet dated January 1, 2010:

- Business Combinations
    - IFRS 1 indicates that a first-time adopter may elect not to apply IFRS 3 Business Combinations retrospectively to business combinations that occurred before the date of transition to IFRS. The Company has taken advantage of this exemption and has applied IFRS 3 only to business combinations that occurred on or after January 1, 2010.

The following schedules represent the reconciliations from Canadian GAAP to IFRS for the respective periods. The adjustments presented in those reconciliations are noted below.

IFRS Adjustments

The following explains the significant differences between the Company's previous GAAP accounting policies and those applied by the Company under IFRS. IFRS policies have been retrospectively and consistently applied.

(a) Warrants

Warrants were issued as part of a private placement in February 2010 and were treated under previous GAAP as an equity instrument in Shareholders' Equity. Under IFRS they must be classified as a financial liability at fair value through profit or loss for two reasons:

- the warrants have an exercise price denominated in Canadian dollars while the Company's functional currency is US dollars. As such, the amount of US dollars that the Company will receive for each share issued is variable.

- the warrants were not "offered pro rata to all existing owners of the same class of its own shares".

As a result of this reclassification adjustment, the following adjustments were also necessary:

- Under IFRS, transaction costs related to financial assets/liabilities at fair value through profit or loss are recognized as an expense when incurred. As a result, the $0.124 million of warrant issue costs were reclassified to administrative expense when incurred in Q1 2010. Under previous GAAP, these costs were reflected in equity as they were netted against the value of the warrants.

- Financial liabilities at fair value through profit or loss must be remeasured to fair value at each statement of financial position date. As such, the revaluation adjustment is reflected as loss on fair value adjustment of warrants in the consolidated statements of net loss twelve months for the year ended December 31, 2010. Under previous GAAP, the warrants were not remeasured at fair value as they were classified as equity instruments.

(b) Cash held in jointly controlled entities

Under previous GAAP, cash and cash equivalents held in jointly controlled entities are not included among cash and cash equivalents of the consolidated group as their use cannot be unilaterally controlled by the Company and therefore was presented separately on the statement of financial position as restricted cash. Under IFRS, cash and cash equivalents held in jointly controlled entities are not presented separately on the statement of financial position, but must be disclosed in the notes accompanying the consolidated financial statements.

(c) Administrative expenses – billed to Bahar Energy

Under previous GAAP, the Company's billings in 2010 to Bahar Energy for expenses covered under the Technical Services Agreement were accounted for as a contra to administrative expenses. Under IFRS such billings are recognized as revenues.

27.1 TRANSITION TO IFRS

IFRS Opening Consolidated Statement of Financial Position

As at January 1, 2010

(US$000's)	Previous GAAP	IFRS Adjustment (Note 27)	IFRS
Assets			
Current Assets			
Cash and cash equivalents	1,326		1,326
Receivable from related party	85		85
Prepaid expenses and deposits	33		33
	1,444	-	1,444
Non-Current Assets			
Investments	326		326
Property and equipment	8		8
	1,778	-	1,778
Liabilities and Equity			
Current Liabilities			
Accounts payable and accrued liabilities	99		99
	99	-	99
Shareholders' Equity			
Common stock / member units	4,255		4,255
Deficit	(2,576)		(2,576)
Total Shareholders' Equity	1,679	-	1,679
	1,778	-	1,778

27.2 TRANSITION TO IFRS

Consolidated Statement of Financial Position

(US$000's)	as at December 31, 2010 Previous GAAP		IFRS Adjustment (Note 27)	IFRS
Assets				
Current Assets				
Cash and cash equivalents	44,839	(b)	3,138	47,977
Trade receivables	3,373		-	3,373
Receivable from related parties	2,727		-	2,727
Prepaid expenses and deposits	273		-	273
	51,212		3,138	54,350
Non-Current Assets				
Restricted cash	3,138	(b)	(3,138)	-
Investments	291		-	291
Deferred tax asset	1,588		-	1,588
Property and equipment	1,087		-	1,087
	57,316		-	57,316
Liabilities and Equity				
Current Liabilities				
Accounts payable and accrued liabilities	2,279		-	2,279
Payable to related parties	2,361		-	2,361
Warrants	-	(a)	2,219	2,219
	4,640		2,219	6,859
Shareholders' Equity				
Common stock / member units	15		-	15
Paid in capital	56,527	(a)	(1)	56,526
Warrants	1,186	(a)	(1,186)	-
Share-based payments reserve	1,361		-	1,361
Deficit	(6,413)	(a)	(1,032)	(7,445)
Total Shareholders' Equity	52,676		(2,219)	50,457
	57,316		-	57,316

27.3 TRANSITION TO IFRS

Consolidated Statement of Net Loss

Year Ended December 31, 2010

(US$000's, except per share amounts)	Previous GAAP		IFRS Adjustment (Note 27)	IFRS
Revenues				
Petroleum and natural gas	5,078		-	5,078
Management service fees	503	(c)	2,510	3,013
	5,581		2,510	8,091
Expenses				
Operating	2,509		-	2,509
Transportation	153		-	153
Pre-licensing costs	235		-	235
Administrative	7,858	(a)	124	10,492
		(c)	2,510	
Depreciation and amortization	15			15
	10,770		2,634	13,404
Loss from operating activities	(5,189)		(124)	(5,313)
Loss on investments	226		-	226
Change in fair value of warrants	-	(a)	908	908
Loss from operations before tax	(5,415)		(1,032)	(6,447)
Income tax recovery	(1,578)		-	(1,578)
Net loss	(3,837)		(1,032)	(4,869)
Total Comprehensive loss	(3,837)		(1,032)	(4,869)
Per share				
Net loss per share, basic & diluted	($0.43)		($0.11)	($0.54)

27.4 TRANSITION TO IFRS

Consolidated Statement of Cash Flows

Year Ended December 31, 2010

(US$000's)	Previous GAAP		IFRS Adjustment (Note 27)	IFRS
Operating activities				
Income before taxes	(5,415)	(a)	(1,032)	(6,447)
Items not affecting cash:				
Stock-based compensation	1,576		-	1,576
Depreciation and amortization	15		-	15
Loss on investment	217		-	217
Change in fair value of warrants		(a)	908	908
	(3,607)		(124)	(3,731)
Change in non-cash operating working capital	(2,004)		-	(2,004)
Cash Used in Operating Activities	(5,611)		(124)	(5,735)
Financing activities				
Proceeds from issue of common shares	57,702		-	57,702
Share issue costs	(4,132)	(a)	124	(4,008)
Distributions paid to unitholders	(32)		-	(32)
Cash From Financing Activities	53,538		124	53,662
Investing activities				
Property and equipment	(1,094)		-	(1,094)
Investments	(182)		-	(182)
Restricted cash held for use in a joint venture	(3,138)	(b)	3,138	-
Cash Used in Investing Activities	(4,414)		3,138	(1,276)
Increase in Cash and Cash Equivalents	43,513		3138	46,651
Cash and Cash Equivalents, Beginning of Year	1,326		-	1,326
Cash and Cash Equivalents, End of Year	44,839		3,138	47,977