



**2012 ANNUAL INFORMATION FORM**

**March 12, 2013**

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### APPENDICES:

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## GLOSSARY OF SELECTED TERMS

Capitalized terms in this Annual Information Form have the meanings set forth below:

### *Entities*

**Board of Directors** means our board of directors.

**Debenture Trustee** means Valiant Trust Company.

**Exchangeable Shareholders** means holders of Exchangeable Shares.

**Newco** means 1563101 Alberta Ltd.

**Oakmont** means Oakmont Energy Ltd.

**Old Zargon** means Zargon Oil & Gas Ltd., prior to completion of the Arrangement.

**Shareholders** means holders of Common Shares.

**TSX** means Toronto Stock Exchange.

**Trust** means Zargon Energy Trust.

**Unitholders** means holders of Trust Units.

**Zargon, we, us or our** means Zargon Oil & Gas Ltd. and its controlled entities on a consolidated basis, and where the context requires, also means our predecessor issuer, the Trust and its controlled entities on a consolidated basis prior to the completion of the Arrangement.

**ZEC** means 1563101 Alberta Ltd.

**ZEI** means Zargon ExchangeCo Inc.

**ZEL** means Zargon Energy Ltd.

**ZUSH** means Zargon U.S. Holdings Ltd.

### *Independent Engineering*

**COGE Handbook** means the Canadian Oil and Gas Evaluation Handbook.

**CSA 51-324** means Staff Notice 51-324 – *Glossary to NI 51-101 – Standards of Disclosure for Oil and Gas Activities* of the Canadian Securities Administrators.

**McDaniel** means McDaniel & Associates Consultants Ltd., independent petroleum consultants of Calgary, Alberta.

**McDaniel Report** means the report prepared by McDaniel dated February 20, 2013 evaluating the crude oil, natural gas and natural gas liquids reserves attributable to our oil and natural gas assets at December 31, 2012.

**NI 51-101** means National Instrument 51-101 – *Standards of Disclosure for Oil and Natural Gas Activities*.

***Securities and Other Terms***

**Arrangement** means the arrangement among the Trust, Old Zargon, Newco, ZEI, Oakmont, ZEL, Zargon Acquisition Corp., Zargon Oil & Gas Partnership, the holders of Trust Units and the holders of Exchangeable Shares pursuant to Section 193 of the *Business Corporations Act* (Alberta) which commenced on December 31, 2010 and was completed on January 1, 2011.

**Credit Agreement** means the credit agreement dated June 14, 2012 as amended, which is described in Note 10 to our consolidated financial statements for the year ended December 31, 2012.

**Common Shares** means our issued and outstanding common shares.

**Convertible Debentures** means the \$57.5 million aggregate principal amount of our 6.00% convertible unsecured subordinated debentures due June 30, 2017, which are currently convertible at the option of the holder, at any time, into fully paid Common Shares at a conversion price of \$18.80 per Common Share.

**Debenture Indenture** means the indenture between us and the Debenture Trustee governing the terms of the Convertible Debentures.

**Exchangeable Shares** means exchangeable shares of Old Zargon.

**SEC** means the United States Securities and Exchange Commission.

**Shareholders** means holders of Common Shares.

**Trust Unit** means trust units of the Trust.

**ABBREVIATIONS**

**Oil and Natural Gas Liquids**

Bbl	barrel
bb/d	barrels per day
Mbbl	thousand barrels
MMbbl	million barrels
NGLs	natural gas liquids

**Natural Gas**

gj	gigajoule
Mcf	thousand cubic feet
MMcf	million cubic feet
bcf	billion cubic feet
Mcf/d	thousand cubic feet per day
MMcf/d	million cubic feet per day
MMbtu	million British Thermal Units

**Other**

ASP	means alkaline surfactant polymer
BOE or boe	means barrel of oil equivalent
boe/d	barrels of oil equivalent per day
Mboe	thousand barrels of oil equivalent
Mmboe	million barrels of oil equivalent
Psi	pounds per square inch
WTI	West Texas Intermediate
°API	the measure of the density or gravity of liquid petroleum products derived from a specific gravity
\$000s	thousands of dollars

## CONVERSION

The following table sets forth certain conversions between Standard Imperial Units and the International System of Units (or metric units).

<u>To Convert From</u>	<u>To</u>	<u>Multiply By</u>
Mcf	cubic metres	28.174
cubic metres	cubic feet	35.494
bbls	cubic metres	0.159
cubic metres	bbls	6.289
feet	metres	0.305
metres	feet	3.281
miles	kilometres	1.609
kilometres	miles	0.621
acres	hectares	0.405
hectares	acres	2.471
gigajoules	MMbtu	0.948
MMbtu	gigajoules	1.0551

We have adopted the standard of 6 mcf: 1 bbl when converting natural gas to oil and 1 bbl: 6 mcf when converting oil to natural gas. **Boe's may be misleading, particularly if used in isolation. A boe conversion ratio of 6 mcf: 1 bbl is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. In addition, given that the value ratio based on the current price of crude oil as compared to natural gas is significantly different from the energy equivalency of 6:1, utilizing a conversion on a 6:1 basis may be misleading as an indication of value.**

All dollar amounts set forth in this Annual Information Form are in Canadian dollars, except where otherwise indicated.

## NOTICE TO READER

### Special Note Regarding Forward-Looking Statements

Certain statements contained in this Annual Information Form, and in certain documents incorporated by reference into this Annual Information Form, constitute forward-looking statements. These statements relate to future events or our future performance. All statements other than statements of historical fact may be forward-looking statements. Forward-looking statements are often, but not always, identified by the use of words such as "seek", "anticipate", "budget", "plan", "continue", "estimate", "expect", "forecast", "may", "will", "project", "predict", "potential", "targeting", "intend", "could", "might", "should", "believe" and similar expressions (including the negative thereof). In addition, there are forward-looking statements in this Annual Information Form under the headings: "*General Development of Our Business*" relating to our business strategy; "*Description of Our Business*" relating to our business plan and strategy, including our plans to refocus our business, our plans relating to our Little Bow ASP project, our capital expenditure plans and our acquisition and disposition program; "*Description of Our Business – Disclosure of Reserves Data and Other Oil and Natural Gas Information*" as to our reserves, future net revenues from our reserves and the anticipated after-tax value of such revenues, pricing and inflation and exchange rates, future development costs and the sources of funding of our future development costs; the development of our proved undeveloped reserves and probable undeveloped reserves; "*Description of Our Business – Disclosure of Reserves Data and Other Oil and Natural Gas Information*" as to our future development activities and the results therefrom, land expiries, hedging policies, reclamation and abandonment obligations, tax horizon, production estimates, exploration and development activities, including our development plans, the timing thereof, and the anticipated capital expenditures associated with the ASP project, anticipated finding and developments costs and field netbacks. This information involves known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking information. By their nature, forward-looking statements are subject to numerous risks and uncertainties, some of which are beyond our

control, including such as those relating to results of operations and financial condition, general economic conditions, industry conditions, changes in regulatory and taxation regimes, volatility of commodity prices, escalation of operating and capital costs, regulatory approvals required in connection with our Little Bow ASP project, currency fluctuations, the availability of services, imprecision of reserve estimates, geological, technical, drilling and processing problems, environmental risks, weather, the lack of availability of qualified personnel or management, stock market volatility, the ability to access sufficient capital from internal and external sources and competition from other industry participants for, among other things, capital, services, acquisitions of reserves, undeveloped lands and skilled personnel. Such forward-looking information is provided for the purpose of providing information about management's current expectations and plans relating to the future to allow investors to have a greater understanding of our business. Readers are cautioned that reliance on such information may not be appropriate for other purposes, such as making investment decisions.

You are cautioned that the assumptions, including among other things, future oil and natural gas prices; future capital expenditures levels; future production levels; future exchange rates; the cost of developing and expanding our assets; our ability to obtain equipment in a timely manner to carry out development activities; our ability to market our oil and natural gas successfully to current and new customers; the impact of increasing competition; our ability to obtain financing on acceptable terms; and our ability to add production and reserves through our development and acquisition activities used in the preparation of such information, although considered reasonable at the time of preparation, may prove to be imprecise and, as such, undue reliance should not be placed on forward-looking statements. Our actual results, performance, or achievement could differ materially from those expressed in, or implied by, these forward-looking statements. We can give no assurance that any of the events anticipated will transpire or occur, or if any of them do, what benefits we will derive from them. The forward-looking information contained in this document is expressly qualified by this cautionary statement. Our policy for updating forward-looking statements is that we disclaim, except as required by law, any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

We believe the expectations reflected in these forward-looking statements are reasonable but no assurance can be given that these expectations will prove to be correct and such forward-looking statements included in, or incorporated by reference into, this Annual Information Form should not be unduly relied upon. These statements speak only as of the date of this Annual Information Form or as of the date specified in the documents incorporated by reference into this Annual Information Form, as the case may be.

In addition to the forward-looking statements identified above, this Annual Information Form, and the documents incorporated by reference, contains forward-looking statements pertaining to the following:

- our business plan and strategy;
- the performance characteristics of our oil and natural gas properties;
- oil and natural gas production levels;
- drilling, completion and workover activities;
- expectations for infrastructure modifications;
- projections of market prices and costs and the related sensitivities of dividends;
- supply and demand for oil and natural gas;
- expectations regarding the ability to raise capital and to continually add to reserves through acquisitions and development;
- treatment under governmental regulatory regimes and tax laws;
- our dividend policy and payment of dividends;
- our capital expenditures programs;

- the sources of funding of our capital expenditures and future acquisitions; and
- our plans, capital expenditures and expectations for our ASP project.

Actual results could differ materially from those anticipated in these forward-looking statements as a result of numerous known and unknown risks and uncertainties and other factors set forth below and elsewhere in this Annual Information Form, many of which are beyond our control. Such factors include, but are not limited to:

- declines in oil and natural gas prices;
- variations in interest rates and foreign exchange rates;
- uncertainties relating to the global economy and access to capital, stock market volatility, market valuations and increased borrowing costs;
- refinancing risk for existing debt and debt service costs;
- access to external sources of capital, borrowings and equity sales;
- risks associated with our hedging activities;
- geological, technical, drilling and processing problems;
- third party credit risk;
- risks associated with the exploitation of our properties and our ability to acquire reserves;
- government regulation and control and changes in governmental legislation;
- changes in income tax laws, royalty rates and other incentive programs;
- uncertainties associated with estimating oil and natural gas reserves;
- risks associated with acquiring, developing and exploring for natural gas and other aspects of our operations;
- risks associated with the marketability of oil and natural gas;
- changes in climate change laws and other environmental regulations;
- risks associated with the exploitation of our properties and our ability to acquire reserves;
- the failure to realize anticipated benefits of acquisitions and dispositions or to manage growth;
- competition in the oil and natural gas industry;
- depletion of our reserves;
- risks associated with large projects or expansion of our activities;
- risks associated with retention of key personnel;
- risks associated with securing and maintaining our properties;
- seasonality; and
- risks associated with the timing of payment of dividends.

In addition, statements relating to "reserves" are deemed to be forward-looking statements, as they involve the implied assessment, based on certain estimates and assumptions, that the reserves described can be profitably produced in the future.

**Readers are cautioned that the foregoing lists of factors are not exhaustive. The forward-looking statements contained in this Annual Information Form, and the documents incorporated by reference herein, are expressly qualified by this cautionary statement. We do not undertake any obligation to publicly update or revise any forward-looking statements except as required by applicable law.**

## Access to Documents

Any document referred to in this Annual Information Form and described as being filed on SEDAR at *www.sedar.com* (including those documents referred to as being incorporated by reference in this Annual Information Form) may be obtained free of charge from us at Suite 700, 333 – 5<sup>th</sup> Avenue S.W., Calgary, Alberta, T2P 3B6.

## ZARGON OIL & GAS LTD.

### General

We continued as "Zargon Oil & Gas Ltd." upon the amalgamation of Old Zargon, Newco, ZAC, ZEI and Oakmont on January 1, 2011 pursuant to the Arrangement. The Arrangement involved an internal reorganization of the Trust and certain of its subsidiaries through which the trust structure was replaced with a corporate structure and the Trust was dissolved. Pursuant to the Arrangement: (i) on December 31, 2010, the Trust Units were exchanged for common shares of Newco on a one-for-one basis, the Exchangeable Shares were exchanged for common shares of Newco on the basis of 1.84716 common shares of Newco for each outstanding Exchangeable Share, and Newco acquired all of the assets and assumed all of the liabilities of the Trust; and (ii) on January 1, 2011, the Trust was dissolved and Old Zargon, Newco, ZAC, ZEI and Oakmont amalgamated. Following the Arrangement, we, together with our subsidiaries, owned, directly or indirectly, the same assets that were owned by the Trust and its subsidiaries immediately prior to the Arrangement. The Arrangement has been accounted for as a continuity of interests and, unless otherwise indicated, all information presented for the pre-Arrangement period in this Annual Information Form relates to the Trust.

Our registered, head and principal office is located at Suite 700, 333 – 5<sup>th</sup> Avenue S.W., Calgary, Alberta, T2P 3B6.

### Inter-Corporate Relationships

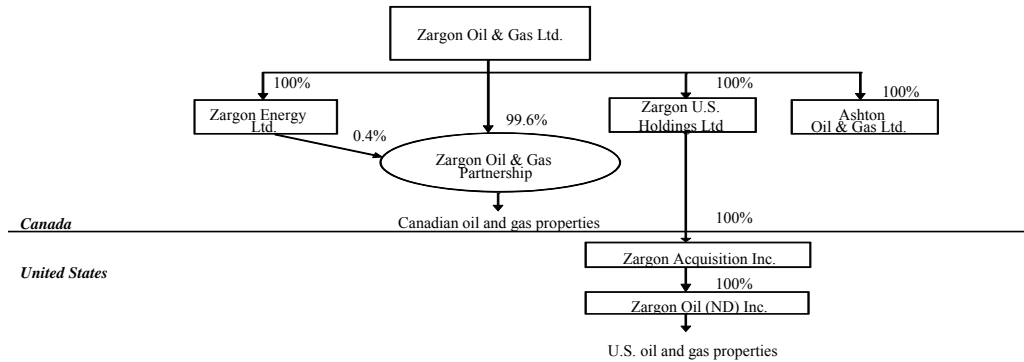
The following are the names and percentages of voting securities that we own and the jurisdiction of incorporation, continuance or formation of our subsidiaries and partnership either, direct and indirect, as at the date hereof.

	Percentage of voting securities (directly or indirectly)	Nature of Entity	Jurisdiction of Incorporation/ Formation
Zargon Energy Ltd.	100%	Corporation	Alberta
Zargon Oil & Gas Partnership	100%	General Partnership	Alberta
Ashton Oil & Gas Ltd.	100%	Corporation	Alberta
Zargon U.S. Holdings Ltd.	100%	Corporation	Alberta
Zargon Acquisition Inc.	100%	Corporation	Wyoming
Zargon Oil (ND) Inc.	100%	Corporation	Delaware



## Our Organization Structure

The following diagram describes the inter-corporate relationships between us and our material subsidiaries and partnership.



## GENERAL DEVELOPMENT OF OUR BUSINESS

### History and Development

On May 31, 2010, we completed an acquisition of working interests in various southern Alberta medium and heavy gravity oil pools with approximately 350 boe/d of existing production, along with approximately 6.9 thousand net acres of undeveloped land for a cash purchase price of approximately \$25 million. The majority of the acquired assets were either situated adjacent to or in the vicinity of our Little Bow property. Following the acquisition, we held a 100 percent working interest in our proposed Little Bow Mannville I Pool Alkaline Surfactant Polymer tertiary recovery flood.

During the second and third quarters of 2010, we completed a series of dispositions of certain non-core assets for total proceeds of approximately \$28.9 million. The asset sales related to a fully marketed property disposition package that included 17 non-core minor oil properties that were producing approximately 375 boe/d.

On September 9, 2010, we acquired all of the existing and outstanding common shares of Oakmont, a private oil and natural gas company, for total consideration of approximately 0.336 million Trust Units and the assumption of approximately \$3.41 million of net debt, for a total transaction value of approximately \$9.36 million. We acquired approximately 99.5 percent of the outstanding common shares of Oakmont pursuant to a share purchase agreement with Oakmont and the holders of the common shares of Oakmont and the balance of the outstanding common shares of Oakmont pursuant to the compulsory acquisition provisions of the *Business Corporations Act* (Alberta). At the time of the acquisition, Oakmont was producing approximately 280 boe/d consisting of 110 bbl/d of crude oil and 1.03 Mcf/d of natural gas. These assets are primarily located within our Alberta Plains South core area and are adjacent to our Little Bow and Grand Forks properties.

On January 1, 2011 we completed the Arrangement which involved an internal reorganization of the Trust and certain of its subsidiaries through which the trust structure was replaced with a corporate structure and the Trust was dissolved. Pursuant to the Arrangement: (i) on December 31, 2010, the Trust Units were exchanged for common shares of Newco on a one-for-one basis, the Exchangeable Shares were exchanged for common shares of Newco on the basis of 1.84716 common shares of Newco for each outstanding Exchangeable Share, and Newco acquired all of the assets and assumed all of the liabilities of the Trust; and (ii) on January 1, 2011, the Trust was dissolved and Old Zargon, Newco, ZAC, ZEI and Oakmont amalgamated. As a result of the Arrangement, we, together with our subsidiaries, own, directly or indirectly, the same assets that were owned by the Trust and its subsidiaries

immediately prior to the Arrangement and we assumed all of the liabilities of the Trust and its subsidiaries immediately prior to the Arrangement.

On January 1, 2011 we amended and restated the Credit Agreement to incorporate the effects of the Arrangement.

During the first quarter of 2011, we completed property dispositions totalling \$2.00 million. These disposition packages of minor non-core properties were part of our ongoing efforts to improve our operational footprint and focus.

On April 7, 2011 we completed a public offering of 1,725,000 Common Shares on a bought deal basis (including 225,000 Common Shares issued pursuant to the exercise in full of the over-allotment option granted to the underwriters) at \$22.60 per Common Share for total gross proceeds of approximately \$38.99 million.

On July 7, 2011, we completed the disposition of our Antler and Manor, Williston Basin properties for a cash consideration, after adjustments, of approximately \$23.87 million. In aggregate, these two southeast Saskatchewan properties were producing 260 bbl/d, and had included 7,800 net acres of undeveloped land.

On August 23, 2011, we completed the acquisition of a partner interest in the Alberta Plains North Jarrow property for a cash consideration, after adjustments, of \$6.25 million. The acquisition brought approximately 1.30 Mmcf/d of natural gas production. Most importantly, this transaction increased our interest to 100 percent in two Jarrow Units and the related compression and gathering facilities, which is consistent with our strategy to consolidate interests in our core properties.

On September 6, 2011, we completed the sale of 3,200 net acres of undeveloped land in the Whitecourt area of Alberta, for a cash consideration of \$5.00 million. There was no production associated with the Whitecourt lands.

On May 1, 2012, we closed a public offering of \$50,000,000 aggregate principal amount of Convertible Debentures at a price of \$1,000 per Convertible Debenture. On May 4, 2012, we completed the sale of an additional \$7,500,000 aggregate principal amount of Convertible Debentures at a price of \$1,000 per Convertible Debenture pursuant to the over-allotment option granted in connection with the previously completed public offering of Convertible Debentures. The Convertible Debentures bear interest at a rate of six per annum, which is payable semi-annually, in arrears, on June 30 and December 31 of each year commencing on December 31, 2012. The Convertible Debentures mature on June 30, 2017.

On June 18, 2012, we completed the sale of 275 bbl/d of oil pertaining to all of our southwest Manitoba assets and selected properties in the Elswick area of southeast Saskatchewan for proceeds of approximately \$36 million. With the closing of these property sales, we also entered into renewed Credit Facility with a borrowing base of \$165 million.

On February 20, 2013, we sanctioned the construction of the tertiary recovery ASP oil exploitation project at our Little Bow oil property in Southern Alberta. This ASP project entails the injection of large volumes of a dilute chemical solution into a partially depleted oil reservoir to recover incremental oil reserves. With sanctioning, phases 1 and 2 of the Little Bow ASP project will be Canada's ninth operational ASP project.

In February of 2013 we disposed of 1,100 net acres of undeveloped land and 10 boe/d in the Karr area of Alberta for \$3.5 million.

### **Significant Acquisitions**

We have not completed any significant acquisitions during our most recently completed financial year for which disclosure is required under Part 8 of National Instrument 51-102 – *Continuous Disclosure Obligations*.

## DESCRIPTION OF OUR BUSINESS

### General

We are an Alberta-based corporation engaged in the business of oil and natural gas exploration, exploitation, development, acquisition and production in Canada and the United States.

Our business plan is to deliver sustainable and profitable oil and natural gas property exploitation and production activities in the oil and natural gas industry. To accomplish this, we have adopted an integrated growth strategy with active exploitation and exploration drilling within our core areas, together with focused acquisitions.

All of our activities are directed towards maximizing value for our Shareholders. This will be achieved through a combination of investing capital to enhance the value of our assets, operating our producing oil and natural gas properties in a low cost manner to maximize the recovery of reserves, and by paying monthly dividends to our Shareholders. We direct our efforts to increase the value of our assets through exploitation drilling and associated exploitation activities and enhanced oil recovery activities as well as by the periodic acquisition of undeveloped and producing oil and natural gas properties. We intend to acquire oil and natural gas producing properties and to participate in exploitation activities that are generally considered to be low risk in nature in the oil and natural gas industry. However, we intend to allocate a percentage of our annual capital budget to moderate risk exploitation and lower risk exploration opportunities on our properties.

In recent years we have worked to refocus our business on six clearly defined long-life oil exploitation projects plus our Little Bow ASP tertiary oil recovery initiative. Now in 2013, with a more simplified and concentrated business, we will focus on the construction and implementation of the Little Bow ASP tertiary recovery project, while profitably advancing our remaining six oil exploitation projects.

### Capital Expenditures

We may approve future capital expenditures or farmouts. Future capital expenditures on our properties will generally be of the type that are intended to maintain or improve production from our properties. We may finance capital expenditures from production revenues, the proceeds of the issue of additional Common Shares or other securities or from the proceeds of disposition of properties, borrowings, and farmouts or with working capital.

We may acquire additional properties and related tangible equipment and fund such acquisitions from production revenues, the net proceeds of any issue of additional Common Shares or other securities or from the proceeds of disposition of properties, or from borrowings, farmouts or with working capital. We may sell any of our interests in properties. In connection with the sale of any interests in our properties, we will determine whether the net proceeds of the sale should be reinvested in additional properties or capital expenditures, used to repay borrowings or distributed to our Shareholders.

### Potential Acquisitions

We evaluate potential acquisitions of all types of oil and natural gas and other energy-related assets as part of our ongoing acquisition program. We are normally in the process of evaluating several potential acquisitions at any one time which individually or together could be material. We are not able to predict whether any opportunities will result in one or more acquisitions.

### Competitive Conditions

The oil and natural gas industry is intensely competitive in all its phases. We compete with numerous other participants in the search for, and the acquisition of, oil and natural gas properties and in the marketing of oil and natural gas. Our competitors include resource companies, which may have greater financial resources, staff and facilities than ours. Competitive factors in the distribution and marketing of oil and natural gas include price and methods and reliability of delivery. We believe that our competitive position is equivalent to that of other oil and gas issuers of similar size and at a similar stage of development.

**Cyclical and Seasonal Impact of Industry**

Our operational results and financial condition will be dependent on the prices received for oil and natural gas production. Oil and natural gas prices have fluctuated widely during recent years and are determined by supply and demand factors, including weather and general economic conditions, as well as conditions in other oil and natural gas regions. Any decline in oil and natural gas prices could have an adverse effect on our financial condition. We mitigate such price risk through closely monitoring the various commodity markets and establishing price risk management programs, as deemed necessary and through maintaining financial flexibility. See "*Risk Factors – Risks Relating to Our Business and Operations – Declines in oil and natural gas prices will adversely affect our financial condition*" and "*Risk Factors – Risks Relating to Our Business and Operations – Our hedging activities may negatively impact our income and our financial condition*".

**Renegotiation or Termination of Contracts**

As at the date hereof, we do not anticipate that any aspect of our business will be materially affected in the remainder of 2013 by the renegotiation or termination of contracts or subcontracts other than with respect to our Credit Agreement which has a term date of June 26, 2013 and may be extended for a further 364-day period upon our request. If the Credit Facility is not extended, it will convert into a 365-day term loan and is repayable in full at the end of such term. See "*Risk Factors – Risks Relating to Our Business and Operations – Our Credit Agreement may be extended prior to June 26, 2013 and failure to extend may, and higher rates, will adversely affect our financial condition*".

**Bankruptcy and Similar Procedures**

There have been no bankruptcy, receivership or similar proceedings against us, or any voluntary receivership, bankruptcy or similar proceeding by us within the three most recently completed financial years or proposed for us for our current financial year.

**Material Restructuring Transactions**

Other than the Arrangement, there has been no material restructuring transactions involving us within the three most recently completed financial years or currently proposed for us for our current financial year.

**Human Resources**

At December 31, 2012, we employed 60 full-time employees, including 45 office and 15 field employees.

**Disclosure of Reserves Data and Other Oil and Natural Gas Information**

This statement of reserves data and other oil and gas information set forth below is dated February 20, 2013. The effective date of the statement is December 31, 2012 and the preparation date of the statement is February 20, 2013. Readers should also refer to the Report of Management and Directors on Oil and Gas Disclosure attached hereto as Appendix A and the Report on Reserves Data by McDaniel attached hereto as Appendix B.

The reserves data set forth below is based upon an evaluation by McDaniel with an effective date of December 31, 2012 contained in the McDaniel Report. The reserves data summarizes our crude oil, natural gas liquids and natural gas reserves and the net present values of future net revenue for these reserves using forecast prices and costs. The McDaniel Report has been prepared in accordance with the standards contained in the COGE Handbook and the reserve definitions contained in NI 51-101 and CSA 51-324. We engaged McDaniel to provide an evaluation of our proved and proved plus probable reserves and no attempt was made to evaluate possible reserves.

Our reserves are in Canada in the provinces of Alberta and Saskatchewan, and in the United States in North Dakota.

We determined the future net revenue and present value of future net revenue after income taxes by utilizing McDaniel's before income tax future net revenue and our estimate of income tax. Our estimate of cash income tax makes use of the following assumptions: corporate income tax at the current legislated rate; annual general and administrative expenses at the current rate; interest expense at the current rate; tax pool deductions utilizing our existing estimated \$313 million of tax pools and forecasted additions to our tax pools from capital expenditures as forecast by McDaniel and any such other additional deductions and adjustments as is and would be consistent with the manner in which we file and would file future tax returns. The after-tax net present value of our oil and gas properties reflects the tax burden of our properties on a stand-alone basis. It does not provide an estimate of the value of us as a business entity, which may be significantly different.

Estimated values of future net revenues presented in the tables below do not represent the fair market value of the reserves. There is no assurance that the forecast prices and costs assumptions will be attained and variances could be material. The recovery and reserve estimates of our crude oil, natural gas liquids and natural gas reserves provided herein are estimates only and there is no guarantee that the estimated reserves will be recovered. Actual crude oil, natural gas and natural gas liquid reserves may be greater than or less than the estimates provided herein. Readers should review the definitions and information contained in "*Definitions and Notes to Reserves Data Tables*" below in conjunction with the following tables and notes. For more information as to the risks involved, see "*Risk Factors – Risks Relating to Our Business and Operations*".

*Reserves Data (Forecast Prices and Costs)*

SUMMARY OF OIL AND GAS RESERVES  
AND NET PRESENT VALUES OF FUTURE NET REVENUE  
as of December 31, 2012  
FORECAST PRICES AND COSTS

**CANADA**

RESERVES CATEGORY	LIGHT AND MEDIUM OIL		HEAVY OIL		NATURAL GAS		NATURAL GAS LIQUIDS	
	Gross (Mbbbl)	Net (Mbbbl)	Gross (Mbbbl)	Net (Mbbbl)	Gross (MMcf)	Net (MMcf)	Gross (Mbbbl)	Net (Mbbbl)
<b>Proved</b>								
Developed Producing	6,312	5,448	3,859	3,270	26,614	23,350	109	74
Developed Non-Producing	269	239	156	143	3,229	2,716	16	11
Undeveloped	69	61	153	140	76	69	4	3
<b>Total Proved</b>	<b>6,650</b>	<b>5,748</b>	<b>4,168</b>	<b>3,553</b>	<b>29,919</b>	<b>26,135</b>	<b>129</b>	<b>88</b>
<b>Probable</b>	<b>2,724</b>	<b>2,304</b>	<b>6,190</b>	<b>5,060</b>	<b>18,898</b>	<b>16,134</b>	<b>99</b>	<b>70</b>
<b>Total Proved Plus Probable</b>	<b>9,374</b>	<b>8,052</b>	<b>10,358</b>	<b>8,613</b>	<b>48,817</b>	<b>42,269</b>	<b>228</b>	<b>158</b>

RESERVES CATEGORY	NET PRESENT VALUES OF FUTURE NET REVENUE BEFORE INCOME TAXES DISCOUNTED AT (%/year)				
	0 (\$000s)	5 (\$000s)	10 (\$000s)	15 (\$000s)	20 (\$000s)
<b>Proved</b>					
Developed Producing	421,083	339,209	285,426	247,737	219,941
Developed Non-Producing	14,711	12,203	10,257	8,744	7,555
Undeveloped	7,906	5,895	4,476	3,448	2,683
<b>Total Proved</b>	<b>443,700</b>	<b>357,307</b>	<b>300,159</b>	<b>259,929</b>	<b>230,179</b>
<b>Probable</b>	<b>358,033</b>	<b>208,916</b>	<b>129,583</b>	<b>82,229</b>	<b>51,686</b>
<b>Total Proved Plus Probable</b>	<b>801,733</b>	<b>566,223</b>	<b>429,742</b>	<b>342,158</b>	<b>281,865</b>

RESERVES CATEGORY	NET PRESENT VALUES OF FUTURE NET REVENUE AFTER INCOME TAXES DISCOUNTED AT (%/year)				
	0 (\$000s)	5 (\$000s)	10 (\$000s)	15 (\$000s)	20 (\$000s)
<b>Proved</b>					
Developed Producing	390,046	320,307	273,252	239,556	214,255
Developed Non-Producing	10,919	9,318	8,044	7,030	6,212
Undeveloped	5,900	4,409	3,357	2,590	2,018
<b>Total Proved</b>	<b>406,865</b>	<b>334,034</b>	<b>284,653</b>	<b>249,176</b>	<b>222,485</b>
<b>Probable</b>	<b>266,366</b>	<b>153,246</b>	<b>92,581</b>	<b>56,174</b>	<b>32,589</b>
<b>Total Proved Plus Probable</b>	<b>673,231</b>	<b>487,280</b>	<b>377,234</b>	<b>305,350</b>	<b>255,074</b>

BY PRODUCTION GROUP  
as of December 31, 2012  
FORECAST PRICES AND COSTS

RESERVES CATEGORY	PRODUCTION GROUP	FUTURE NET REVENUE BEFORE INCOME TAXES (discounted at 10%/year) (\$000s)	UNIT VALUE <sup>(1)</sup> BEFORE INCOME TAXES (discounted at 10%/year) (\$/bbl or \$/Mcf)
Proved	Light and Medium Crude Oil (including solution gas and other by-products)	181,514	31.66
	Heavy Oil (including solution gas and other by-products)	105,449	29.81
	Natural Gas (including by-products but excluding natural gas from oil wells)	13,196	0.60
	<b>Total</b>	<b>300,159</b>	
Proved plus Probable	Light and Medium Crude Oil (including solution gas and other by-products)	235,420	29.32
	Heavy Oil (including solution gas and other by-products)	166,226	19.35
	Natural Gas (including by-products but excluding natural gas from oil wells)	28,096	0.83
	<b>Total</b>	<b>429,742</b>	

Note:

(1) Unit values are based on Company net reserve volumes.

SUMMARY OF OIL AND GAS RESERVES  
AND NET PRESENT VALUES OF FUTURE NET REVENUE  
as of December 31, 2012  
FORECAST PRICES AND COSTS

**UNITED STATES**

RESERVES CATEGORY	LIGHT AND MEDIUM OIL		HEAVY OIL		NATURAL GAS		NATURAL GAS LIQUIDS	
	Gross (Mbbbl)	Net (Mbbbl)	Gross (Mbbbl)	Net (Mbbbl)	Gross (MMcf)	Net (MMcf)	Gross (Mbbbl)	Net (Mbbbl)
<b>Proved</b>								
Developed Producing	2,464	1,821	-	-	-	-	-	-
Developed Non-Producing	-	-	-	-	-	-	-	-
Undeveloped	-	-	-	-	-	-	-	-
<b>Total Proved</b>	<b>2,464</b>	<b>1,821</b>	-	-	-	-	-	-
<b>Probable</b>	<b>627</b>	<b>462</b>	-	-	-	-	-	-
<b>Total Proved Plus Probable</b>	<b>3,091</b>	<b>2,283</b>	-	-	-	-	-	-

RESERVES CATEGORY	NET PRESENT VALUES OF FUTURE NET REVENUE BEFORE INCOME TAXES DISCOUNTED AT (%/year)				
	0 (\$000s)	5 (\$000s)	10 (\$000s)	15 (\$000s)	20 (\$000s)
<b>Proved</b>					
Developed Producing	70,233	49,619	37,602	30,364	25,623
Developed Non-Producing	-	-	-	-	-
Undeveloped	-	-	-	-	-
<b>Total Proved</b>	<b>70,233</b>	<b>49,619</b>	<b>37,602</b>	<b>30,364</b>	<b>25,623</b>
<b>Probable</b>	<b>25,641</b>	<b>11,156</b>	<b>6,163</b>	<b>4,008</b>	<b>2,880</b>
<b>Total Proved Plus Probable</b>	<b>95,874</b>	<b>60,775</b>	<b>43,765</b>	<b>34,372</b>	<b>28,503</b>

RESERVES CATEGORY	NET PRESENT VALUES OF FUTURE NET REVENUE AFTER INCOME TAXES DISCOUNTED AT (%/year)				
	0 (\$000s)	5 (\$000s)	10 (\$000s)	15 (\$000s)	20 (\$000s)
<b>Proved</b>					
Developed Producing	39,226	29,212	22,441	18,252	15,492
Developed Non-Producing	-	-	-	-	-
Undeveloped	-	-	-	-	-
<b>Total Proved</b>	<b>39,226</b>	<b>29,212</b>	<b>22,441</b>	<b>18,252</b>	<b>15,492</b>
<b>Probable</b>	<b>14,676</b>	<b>6,527</b>	<b>3,592</b>	<b>2,329</b>	<b>1,671</b>
<b>Total Proved Plus Probable</b>	<b>53,902</b>	<b>35,739</b>	<b>26,033</b>	<b>20,581</b>	<b>17,163</b>



BY PRODUCTION GROUP  
as of December 31, 2012  
FORECAST PRICES AND COSTS

RESERVES CATEGORY	PRODUCTION GROUP	FUTURE NET REVENUE BEFORE INCOME TAXES (discounted at 10%/year) (\$000s)	UNIT VALUE <sup>(1)</sup> BEFORE INCOME TAXES (discounted at 10%/year) (\$/bbl or \$/Mcf)
Proved	Light and Medium Crude Oil (including solution gas and other by-products)	37,602	20.65
	Heavy Oil (including solution gas and other by-products)	-	-
	Natural Gas (including by-products but excluding natural gas from oil wells)	-	-
<b>Total</b>		<b>37,602</b>	
Proved plus Probable	Light and Medium Crude Oil (including solution gas and other by-products)	43,765	19.17
	Heavy Oil (including solution gas and other by-products)	-	-
	Natural Gas (including by-products but excluding natural gas from oil wells)	-	-
<b>Total</b>		<b>43,765</b>	

Note:

(1) Unit values are based on Company net reserve volumes.

SUMMARY OF OIL AND GAS RESERVES  
AND NET PRESENT VALUES OF FUTURE NET REVENUE  
as of December 31, 2012  
FORECAST PRICES AND COSTS

**AGGREGATE**

RESERVES CATEGORY	LIGHT AND MEDIUM OIL		HEAVY OIL		NATURAL GAS		NATURAL GAS LIQUIDS	
	Gross (Mbbbl)	Net (Mbbbl)	Gross (Mbbbl)	Net (Mbbbl)	Gross (MMcf)	Net (MMcf)	Gross (Mbbbl)	Net (Mbbbl)
<b>Proved</b>								
Developed Producing	8,776	7,269	3,859	3,270	26,614	23,350	109	74
Developed Non-Producing	269	239	156	143	3,229	2,716	16	11
Undeveloped	69	61	153	140	76	69	4	3
<b>Total Proved</b>	<b>9,114</b>	<b>7,569</b>	<b>4,168</b>	<b>3,553</b>	<b>29,919</b>	<b>26,135</b>	<b>129</b>	<b>88</b>
<b>Probable</b>	<b>3,351</b>	<b>2,766</b>	<b>6,190</b>	<b>5,060</b>	<b>18,898</b>	<b>16,134</b>	<b>99</b>	<b>70</b>
<b>Total Proved Plus Probable</b>	<b>12,465</b>	<b>10,335</b>	<b>10,358</b>	<b>8,613</b>	<b>48,817</b>	<b>42,269</b>	<b>228</b>	<b>158</b>

RESERVES CATEGORY	NET PRESENT VALUES OF FUTURE NET REVENUE BEFORE INCOME TAXES DISCOUNTED AT (%/year)				
	0 (\$000s)	5 (\$000s)	10 (\$000s)	15 (\$000s)	20 (\$000s)
<b>Proved</b>					
Developed Producing	491,316	388,828	323,028	278,101	245,564
Developed Non-Producing	14,711	12,203	10,257	8,744	7,555
Undeveloped	7,906	5,895	4,476	3,448	2,683
<b>Total Proved</b>	<b>513,933</b>	<b>406,926</b>	<b>337,761</b>	<b>290,293</b>	<b>255,802</b>
<b>Probable</b>	<b>383,674</b>	<b>220,072</b>	<b>135,746</b>	<b>86,237</b>	<b>54,566</b>
<b>Total Proved Plus Probable</b>	<b>897,607</b>	<b>626,998</b>	<b>473,507</b>	<b>376,530</b>	<b>310,368</b>

RESERVES CATEGORY	NET PRESENT VALUES OF FUTURE NET REVENUE AFTER INCOME TAXES DISCOUNTED AT (%/year)				
	0 (\$000s)	5 (\$000s)	10 (\$000s)	15 (\$000s)	20 (\$000s)
<b>Proved</b>					
Developed Producing	429,272	349,519	295,693	257,808	229,747
Developed Non-Producing	10,919	9,318	8,044	7,030	6,212
Undeveloped	5,900	4,409	3,357	2,590	2,018
<b>Total Proved</b>	<b>446,091</b>	<b>363,246</b>	<b>307,094</b>	<b>267,428</b>	<b>237,977</b>
<b>Probable</b>	<b>281,042</b>	<b>159,773</b>	<b>96,173</b>	<b>58,503</b>	<b>34,260</b>
<b>Total Proved Plus Probable</b>	<b>727,133</b>	<b>523,019</b>	<b>403,267</b>	<b>325,931</b>	<b>272,237</b>

BY PRODUCTION GROUP  
as of December 31, 2012  
FORECAST PRICES AND COSTS

RESERVES CATEGORY	PRODUCTION GROUP	FUTURE NET REVENUE BEFORE INCOME TAXES (discounted at 10%/year) (\$000s)	UNIT VALUE <sup>(1)</sup> BEFORE INCOME TAXES (discounted at 10%/year) (\$/bbl or \$/Mcf)
Proved	Light and Medium Crude Oil (including solution gas and other by-products)	219,116	29.01
	Heavy Oil (including solution gas and other by-products)	105,449	29.81
	Natural Gas (including by-products but excluding natural gas from oil wells)	13,196	0.60
<b>Total</b>		<b>337,761</b>	
Proved plus Probable	Light and Medium Crude Oil (including solution gas and other by-products)	279,185	27.07
	Heavy Oil (including solution gas and other by-products)	166,226	19.35
	Natural Gas (including by-products but excluding natural gas from oil wells)	28,096	0.83
<b>Total</b>		<b>473,507</b>	

Note:

(1) Unit values are based on Company net reserve volumes.

TOTAL FUTURE NET REVENUE  
(UNDISCOUNTED)  
as of December 31, 2012  
FORECAST PRICES AND COSTS

(\$000s) RESERVES CATEGORY	REVENUE	ROYALTIES	OPERATING COSTS	DEVELOPMENT COSTS	ABANDONMENT AND RECLAMATION COSTS	FUTURE NET REVENUE BEFORE INCOME TAXES	INCOME TAXES	FUTURE NET REVENUE AFTER INCOME TAXES
<b>Proved Reserves</b>								
Canada	1,077,641	157,330	426,323	6,889	43,399	443,700	36,835	406,865
United States	232,908	60,818	95,202	-	6,655	70,233	31,007	39,226
<b>Total</b>	<b>1,310,549</b>	<b>218,148</b>	<b>521,525</b>	<b>6,889</b>	<b>50,054</b>	<b>513,933</b>	<b>67,842</b>	<b>446,091</b>
<b>Proved Plus Probable Reserves</b>								
Canada	2,014,846	316,524	725,894	123,457	47,238	801,733	128,502	673,231
United States	309,416	80,907	125,208	-	7,427	95,874	41,972	53,902
<b>Total</b>	<b>2,324,262</b>	<b>397,431</b>	<b>851,102</b>	<b>123,457</b>	<b>54,665</b>	<b>897,607</b>	<b>170,474</b>	<b>727,133</b>

**Definitions and Notes to Reserves Data Tables:**

- Columns may not add due to rounding.
- The crude oil, natural gas liquids and natural gas reserve estimates presented in the McDaniel Report are based on the definitions and guidelines contained in the COGE Handbook, NI 51-101 and CSA 51-324. A summary of certain of those definitions is set forth below.

*Reserve Categories*

Reserves are estimated remaining quantities of oil and natural gas and related substances anticipated to be recoverable from known accumulations, from a given date forward, based on:

- analysis of drilling, geological, geophysical and engineering data;
- the use of established technology; and
- specified economic conditions.

Reserves are classified according to the degree of certainty associated with the estimates.

**Proved reserves** are those reserves that can be estimated with a high degree of certainty to be recoverable. It is likely that the actual remaining quantities recovered will exceed the estimated proved reserves.

**Probable reserves** are those additional reserves that are less certain to be recovered than proved reserves. It is equally likely that the actual remaining quantities recovered will be greater or less than the sum of the estimated proved plus probable reserves.

Other criteria that must also be met for the categorization of reserves are provided in the COGE Handbook.

Each of the reserve categories (proved and probable) may be divided into the following developed and undeveloped categories:

**Developed reserves** are those reserves that are expected to be recovered from existing wells and installed facilities or, if facilities have not been installed, that would involve a low expenditure (for example, when compared to the cost of drilling a well) to put the reserves on production. The developed category may be subdivided into producing and non-producing.

**Developed producing reserves** are those reserves that are expected to be recovered from completion intervals open at the time of the estimate. These reserves may be currently producing or, if shut-in, they must have previously been on production, and the date of resumption of production must be known with reasonable certainty.

**Developed non-producing reserves** are those reserves that either have not been on production, or have previously been on production, but are shut-in, and the date of resumption of production is unknown.

**Undeveloped reserves** are those reserves expected to be recovered from known accumulations where a significant expenditure (for example, when compared to the cost of drilling a well) is required to render them capable of production. They must fully meet the requirements of the reserves classification (proved, probable) to which they are assigned.

In multi-well pools it may be appropriate to allocate total pool reserves between the developed and undeveloped categories or to subdivide the developed reserves for the pool between developed producing and developed non-producing. This allocation should be based on the estimator's assessment as to the reserves that will be recovered from specific wells, facilities and completion intervals in the pool and their respective development and production status.

#### *Levels of Certainty for Reported Reserves*

The qualitative certainty levels referred to in the definitions above are applicable to individual reserve entities (which refers to the lowest level at which reserves calculations are performed) and to reported reserves (which refers to the highest level sum of individual entity estimates for which reserves are presented). Reported reserves should target the following levels of certainty under a specific set of economic conditions:

- at least a 90 percent probability that the quantities actually recovered will equal or exceed the estimated proved reserves; and
- at least a 50 percent probability that the quantities actually recovered will equal or exceed the sum of the estimated proved plus probable reserves.

A qualitative measure of the certainty levels pertaining to estimates prepared for the various reserves categories is desirable to provide a clearer understanding of the associated risks and uncertainties. However, the majority of reserves estimates will be prepared using deterministic methods that do not provide a mathematically derived quantitative measure of probability. In principle, there should be no difference between estimates prepared using probabilistic or deterministic methods.

**Forecast Prices and Costs**

The forecast cost and price assumptions assume increases in wellhead selling prices and take into account inflation with respect to future operating and capital costs. Crude oil and natural gas benchmark reference pricing, as at December 31, 2012, inflation and exchange rates utilized in the McDaniel Report were as follows:

SUMMARY OF PRICING AND INFLATION RATE ASSUMPTIONS  
as of December 31, 2012  
FORECAST PRICES AND COSTS

Year	WTI Cushing Oklahoma (\$US/bbl)	Edmonton Par Price 40° API (\$Cdn/bbl)	Bow River Hardisty API (\$Cdn/bbl)	Alberta Heavy 12° API (\$Cdn/bbl)	Cromer Medium 29.3° API (\$Cdn/bbl)	Natural Gas AECO Price (\$Cdn/ MMBTU)	Natural Gas Liquids FOB Field Gate (\$Cdn/bbl)	Inflation Rate <sup>(1)</sup> %/year	Exchange Rate <sup>(2)</sup> (\$US/ \$Cdn)
Forecast									
2013	92.50	87.50	75.30	65.60	83.10	3.35	57.60	2.0	1.000
2014	92.50	90.50	77.80	67.90	86.00	3.85	63.40	2.0	1.000
2015	93.60	92.60	79.60	69.50	88.00	4.35	68.70	2.0	1.000
2016	95.50	94.50	81.30	70.90	89.80	4.70	70.40	2.0	1.000
2017	97.40	96.40	82.90	72.30	91.60	5.10	72.10	2.0	1.000
2018	99.40	98.30	84.50	73.70	93.40	5.45	73.80	2.0	1.000
2019	101.40	100.30	86.30	75.20	95.30	5.55	75.30	2.0	1.000
2020	103.40	102.30	88.00	76.70	97.20	5.70	76.80	2.0	1.000
2021	105.40	104.30	89.70	78.20	99.10	5.80	78.30	2.0	1.000
2022	107.60	106.50	91.60	79.90	101.20	5.90	80.00	2.0	1.000
2023	109.70	108.50	93.30	81.40	103.10	6.00	81.50	2.0	1.000
2024	111.90	110.70	95.20	83.00	105.20	6.15	83.10	2.0	1.000
2025	114.10	112.90	97.10	84.70	107.30	6.25	84.80	2.0	1.000
2026	116.40	115.20	99.10	86.40	109.40	6.35	86.50	2.0	1.000
2027	118.80	117.50	101.10	88.10	111.60	6.50	88.30	2.0	1.000
Thereafter:	Escalate at 2.0%/year	Escalate at 2.0%/year	Escalate at 2.0%/year	Escalate at 2.0%/year	Escalate at 2.0%/year	Escalate at 2.0%/year	Escalate at 2.0%/year	2.0	1.000

## Notes:

- (1) Inflation rates for forecasting prices and costs.  
(2) Exchange rates used to generate the benchmark reference prices in this table.

Weighted average historical prices realized by us (before the impact of financial risk management contracts) for the year ended December 31, 2012, were \$2.16/Mcf for natural gas, \$72.86/bbl for crude oil, \$64.24/bbl for natural gas liquids and \$79.85/bbl for heavy oil.

**Future Development Costs**

The following tables set forth development costs deducted in the estimation of our future net revenue attributable to the reserve categories noted below.

**CANADA**

Year (\$000s)	Forecast Prices and Costs	
	Proved Reserves	Proved Plus Probable Reserves
2013	2,098	48,536
2014	3,504	19,620
2015	993	24,311
2016	-	12,780
2017	-	11,957
Thereafter	294	6,253
Total Undiscounted	6,889	123,457
Total Discounted at 10%	6,030	105,992

**UNITED STATES**

Year (\$000s)	Forecast Prices and Costs	
	Proved Reserves	Proved Plus Probable Reserves
2013	-	-
2014	-	-
2015	-	-
2016	-	-
2017	-	-
Thereafter	-	-
Total Undiscounted	-	-
Total Discounted at 10%	-	-

**AGGREGATE**

Year (\$000s)	Forecast Prices and Costs	
	Proved Reserves	Proved Plus Probable Reserves
2013	2,098	48,536
2014	3,504	19,620
2015	993	24,311
2016	-	12,780
2017	-	11,957
Thereafter	294	6,253
Total Undiscounted	6,889	123,457
Total Discounted at 10%	6,030	105,992

## Notes:

- (1) We expect to fund the development costs of our reserves through a combination of internally generated cash flow, debt and the issuance of Common Shares or other securities.
- (2) There can be no guarantee that funds will be available or that our Board of Directors will allocate funding to develop all of the reserves attributed in the McDaniel Report. Failure to develop those reserves would have a negative impact on our future cash flow.
- (3) At this time, there are no expectations that the costs of funding would make development of a property uneconomic.
- (4) The interest or other costs of external funding are not included in the reserves and future net revenue estimates. This would reduce reserves and future net revenue to some degree depending upon the funding sources utilized. We do not anticipate that interest or other funding costs would make development of any property uneconomic.

- (5) Estimated future abandonment and reclamation costs related to a property have been taken into account by McDaniel in determining reserves that should be attributed to a property. Reasonable estimated future well abandonment costs were deducted in determining the aggregate future net revenue. No allowance was made, however, for reclamation of well sites or the abandonment and reclamation of any facilities.
- (6) The forecast price and cost assumptions assume the continuance of current laws and regulations.
- (7) The extent and character of all factual data supplied to McDaniel were accepted by McDaniel as represented. No field inspection was conducted.

***Reconciliation of Changes in Reserves***

RECONCILIATION OF  
GROSS RESERVES  
BY PRINCIPAL PRODUCT TYPE  
FORECAST PRICES AND COSTS

**CANADA**

FACTORS	LIGHT AND MEDIUM OIL			HEAVY OIL			ASSOCIATED AND NON-ASSOCIATED GAS		
	Proved (Mbbbl)	Probable (Mbbbl)	Proved Plus	Proved (Mbbbl)	Probable (Mbbbl)	Proved Plus	Proved (MMcf)	Probable (MMcf)	Proved Plus
			Probable (Mbbbl)			Probable (Mbbbl)			
December 31, 2011	7,663	3,389	11,052	4,080	5,282	9,362	39,370	22,053	61,423
Extensions & Improved									
Recovery	637	267	904	330	410	740	431	189	620
Technical Revisions	305	(602)	(297)	309	462	771	336	(1,850)	(1,514)
Discoveries	-	-	-	-	-	-	-	-	-
Acquisitions	32	10	42	85	36	121	64	19	83
Dispositions	(925)	(339)	(1,264)	-	-	-	-	-	-
Economic Factors	-	(1)	(1)	-	-	-	(3,997)	(1,513)	(5,510)
Production	(1,062)	-	(1,062)	(636)	-	(636)	(6,285)	-	(6,285)
<b>December 31, 2012</b>	<b>6,650</b>	<b>2,724</b>	<b>9,374</b>	<b>4,168</b>	<b>6,190</b>	<b>10,358</b>	<b>29,919</b>	<b>18,898</b>	<b>48,817</b>



RECONCILIATION OF  
GROSS RESERVES  
BY PRINCIPAL PRODUCT TYPE  
FORECAST PRICES AND COSTS

**UNITED STATES**

FACTORS	LIGHT AND MEDIUM OIL			HEAVY OIL			ASSOCIATED AND NON-ASSOCIATED GAS		
	Proved (Mdbl)	Probable (Mdbl)	Proved Plus	Proved (Mdbl)	Probable (Mdbl)	Proved Plus	Proved (MMcf)	Probable (MMcf)	Proved Plus
			Probable (Mdbl)			Probable (MMcf)			
December 31, 2011	2,693	652	3,345	-	-	-	-	-	-
Extensions & Improved									
Recovery	-	-	-	-	-	-	-	-	-
Technical Revisions	(46)	(25)	(71)	-	-	-	-	-	-
Discoveries	-	-	-	-	-	-	-	-	-
Acquisitions	-	-	-	-	-	-	-	-	-
Dispositions	-	-	-	-	-	-	-	-	-
Economic Factors	-	-	-	-	-	-	-	-	-
Production	(183)	-	(183)	-	-	-	-	-	-
<b>December 31, 2012</b>	<b>2,464</b>	<b>627</b>	<b>3,091</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>

RECONCILIATION OF  
GROSS RESERVES  
BY PRINCIPAL PRODUCT TYPE  
FORECAST PRICES AND COSTS

**AGGREGATE**

FACTORS	LIGHT AND MEDIUM OIL			HEAVY OIL			ASSOCIATED AND NON-ASSOCIATED GAS		
	Proved (Mdbl)	Probable (Mdbl)	Proved Plus	Proved (Mdbl)	Probable (Mdbl)	Proved Plus	Proved (MMcf)	Probable (MMcf)	Proved Plus
			Probable (Mdbl)			Probable (MMcf)			
December 31, 2011	10,356	4,041	14,397	4,080	5,282	9,362	39,370	22,053	61,423
Extensions & Improved									
Recovery	637	267	904	330	410	740	431	189	620
Technical Revisions	259	(627)	(368)	309	462	771	336	(1,850)	(1,514)
Discoveries	-	-	-	-	-	-	-	-	-
Acquisitions	32	10	42	85	36	121	64	19	83
Dispositions	(925)	(339)	(1,264)	-	-	-	-	-	-
Economic Factors	-	(1)	(1)	-	-	-	(3,997)	(1,513)	(5,510)
Production	(1,245)	-	(1,245)	(636)	-	(636)	(6,285)	-	(6,285)
<b>December 31, 2012</b>	<b>9,114</b>	<b>3,351</b>	<b>12,465</b>	<b>4,168</b>	<b>6,190</b>	<b>10,358</b>	<b>29,919</b>	<b>18,898</b>	<b>48,817</b>

### ***Additional Information Relating to Reserves Data***

#### ***Undeveloped Reserves***

Undeveloped reserves are attributed by McDaniel in accordance with standards and procedures contained in the COGE Handbook. Proved undeveloped reserves are those reserves that can be estimated with a high degree of certainty and are expected to be recovered from known accumulations where a significant expenditure is required to render them capable of production. Probable undeveloped reserves are those reserves that are less certain to be recovered than proved reserves and are expected to be recovered from known accumulations where a significant expenditure is required to render them capable of production. In our practice, proved undeveloped reserves tend to be those reserves related to wells that have been tested and not yet tied-in, wells drilled near the end of the fiscal year or wells further away from our gathering systems. In addition, such reserves may relate to planned infill drilling locations. Probable undeveloped reserves may be reserves tested or indicated by analogy to be productive, infill drilling location and lands contiguous to production. In either case, the majority of undeveloped reserves are planned to be on stream within a two-year time frame. Undeveloped proved and probable reserves represent only about 17 percent of our proved and probable reserves.

There are a number of factors that could result in delayed or cancelled development, including the following: (i) changing economic conditions (due to pricing, operating and capital expenditure fluctuations); (ii) changing technical conditions (including production anomalies, such as water breakthrough or accelerated depletion); (iii) multi-zone developments (for instance, a prospective formation completion may be delayed until the initial completion is no longer economic); (iv) a larger development program may need to be spread out over several years to optimize capital allocation and facility utilization; and (v) surface access issues (including those relating to land owners, weather conditions and regulatory approvals). For more information, see "*Risk Factors – Risks Relating to Our Business and Operations*".

#### ***Proved Undeveloped Reserves***

The following table discloses, for each product type, the volumes of proved undeveloped reserves that were attributed in each of our most recent three financial years and, in the aggregate, before that time.

<b>Year</b>	<b>Light and Medium Oil (Mbbbl)</b>		<b>Heavy Oil (Mbbbl)</b>		<b>Natural Gas (MMcf)</b>		<b>NGLs (Mbbbl)</b>	
	<b>First Attributed</b>	<b>Cumulative at Year End</b>	<b>First Attributed</b>	<b>Cumulative at Year End</b>	<b>First Attributed</b>	<b>Cumulative at Year End</b>	<b>First Attributed</b>	<b>Cumulative at Year End</b>
Prior	-	181	-	45	-	317	-	-
2010	349	446	206	251	79	187	4	4
2011	77	282	55	205	186	366	-	3
2012	12	69	-	153	3	77	1	4

A total of 222 Mbbbl of oil, 77 MMcf of gas and 4 Mbbbl of NGLs were assigned as proved undeveloped reserves at December 31, 2012, representing one percent of our total proved reserves. In estimating future net revenue McDaniel reviewed our future development plans in order to estimate and deduct future development costs. Therefore the future development costs as set out under "*Future Development Costs*" are consistent with our future development plans. The proved undeveloped reserves are generally associated with infill/development drilling locations supported by recent drilling results and offset well data. The largest portion of the capital associated with developing proved undeveloped reserves is expected to be spent in 2013, with carryover into 2014. Within the McDaniel Report 81 percent of the capital is scheduled to be spent over the next two years.

### ***Probable Undeveloped Reserves***

The following table discloses, for each product type, the volumes of probable undeveloped reserves that were first attributed in each of our most recent three financial years and, in the aggregate, before that time.

Year	Light and Medium Oil (Mbbbl)		Heavy Oil (Mbbbl)		Natural Gas (MMcf)		NGLs (Mbbbl)	
	First Attributed	Cumulative at Year End	First Attributed	Cumulative at Year End	First Attributed	Cumulative at Year End	First Attributed	Cumulative at Year End
Prior	144	407	-	114	25	3,041	-	4
2010	286	385	462	481	99	698	1	1
2011	423	731	3,465	3,667	2,572	2,878	31	43
2012	4	336	502	4,465	94	2,847	1	27

A total of 4,801 Mbbbl of oil, 2,847 MMcf of gas and 27 Mbbbl of NGLs were assigned as gross probable undeveloped reserves in 2012, representing approximately 41 percent of our total probable reserves or 17 percent of our total proved plus probable reserves. The majority of the probable reserves assignment for us relates to properties which have proved producing reserves assigned. The bulk of the probable undeveloped reserves are assigned to projects which are actively underway and are contemplated in our upcoming capital programs. Of the total future development costs assigned in the McDaniel Report for probable undeveloped reserves 56 percent are forecast to be spent in 2013 and 2014.

### ***Significant Factors or Uncertainties Affecting Reserves Data***

Our reserves have been evaluated in accordance with NI 51-101 by McDaniel, an independent engineering firm, effective December 31, 2012. Our audit and reserves committee has reviewed the scope and methodology of McDaniel's evaluation; any significant new discoveries, additions, revisions and acquisitions, and reviewed the assumptions and consistency with prior years.

Our reserves are characterized by a high developed producing component. This reflects our core competencies of oil exploitation, increasing oil production and reserves from existing reservoirs. It is a technically complex business and each oil reservoir is treated differently depending on the interrelationships of the reservoir rock, fluids, pressures, wells and surface facilities. As circumstances change and additional data becomes available, our reserve estimates also change. Estimates made are reviewed and revised, either upward or downward, as warranted by the new information.

Our evaluated oil and gas properties have no material extraordinary risks or uncertainties beyond those which are inherent in an oil and gas producing company as described in our management's discussion and analysis relating to our 2012 annual audited consolidated financial statements under the heading "*Business Risks And Outlooks*", which is incorporated herein by reference. See also "*Risk Factors – Risks Relating to Our Business and Operations*" below.

### **Other Oil and Gas Information**

#### ***Oil and Gas Properties***

The following is a description of our principal oil and natural gas properties on production or under development as at December 31, 2012. The term "net", when used to describe our share of production, means the total of our working interest share before deduction of royalties owned by others. Unless otherwise specified, gross and net acres and well count information are as at December 31, 2012. **Estimates of reserves for individual properties may not reflect the same confidence level as estimates of reserves and future net revenue for all properties, due to the effects of aggregation.**

Our major properties are concentrated within the Alberta and Saskatchewan in Canada and in North Dakota in the United States. Each region offers a large undeveloped land base, a vast seismic database, and significant ownership and operatorship in production facilities.

*Williston Basin*

We have a long and profitable history in the Williston Basin core area, which encompasses a portion of southeast Saskatchewan and three counties of North Dakota. The area holds 27 percent of our proved and probable oil and liquids reserves and accounted for 28 percent of our production in 2012.

In the Williston Basin, we are working two types of oil exploitation projects. In 2012, the majority of our Williston Basin drilling locations were Midale drainage targets, which are characterized by low permeability reservoirs that are generally partially pressure supported by either weak aquifers or, in some cases, by non-operated offsetting mature waterfloods. Production from Midale type wells are characterized by relatively low rates, moderately high water cuts, but shallow production declines. Ultimately, as many as 30 of these drainage locations are expected to be drilled over the next three years at the Weyburn, Elswick, Midale, Ralph and Steelman properties. The McDaniel Report has booked only one of these undeveloped Williston Basin Midale horizontal drainage locations.

Exploiting un-drained Frobisher seismically defined targets is the second type of Williston Basin oil exploitation project that is being pursued. These Frobisher targets are characterized by higher permeability rock with full aquifer pressure support. Successful wells have high initial oil production rates, but high initial declines as the flank water encroaches on the wells. The economics of these Frobisher programs can be very robust, as demonstrated by our 17 well 2009-2010 Steelman Frobisher program where McDaniel assigned average proved and probable reserves in excess of 75 thousand barrels of oil per well. Over the next three years, we expect to drill 15 or more Frobisher locations on already identified structures at the Weyburn, Steelman and Mackabee Coulee properties. The McDaniel Report does not include any of these undeveloped Williston Basin Frobisher horizontal locations.

*Alberta Plains South*

Our Alberta Plains South core area holds 37 percent of our proved and probable oil and liquids reserves and contributed 27 percent of our 2012 production. During 2012, we continued our progress with the horizontal development of the Taber South Sunburst pool and expanded the area of the waterflood secondary recovery project. At Grand Forks, oil exploitation will include facility optimization, and modifications to enhance oil recoveries.

The largest and most important property in this core area is Little Bow with its tertiary oil recovery opportunities plus a number of waterflood and production optimization projects. Over the last few years, we have assembled assets at Little Bow through a number of property and corporate acquisitions, which also consolidated our position in the ASP project.

In 2012, we received ERCB regulatory approval and substantially completed the detailed engineering and the procurement of long-lead-time equipment for the Little Bow Upper Mannville I and P pool ASP project. This tertiary oil recovery project entails the injection of chemicals as a dilute water solution into a partially depleted reservoir to recover incremental oil reserves. The 2012 year end McDaniel Report has assigned 4.39 Mmboe of probable undeveloped reserves to our working interest in Phases 1 and 2 of the project. The management project schedule anticipates first chemical injection in January 2014, with a significant oil production response forecast to occur by mid-2014. Future costs to develop the first two phases of the project are estimated at \$103.0 million and are comprised of \$53.0 million for facilities and field development capital (2013-2015) and \$50.0 million for the cost of the chemical injection (2014-2020). Incorporating all future capital (including ASP chemical costs), the Little Bow ASP Phase 1 and 2 finding and development costs are estimated to be \$24.92 per barrel of oil equivalent. Targeted field netbacks for the Little Bow ASP Phase 1 and 2 projects are in the \$50 per barrel of oil range.

In 2013, Zargon is projecting to spend \$38.0 million of Phase 1 Little Bow ASP capital with the bulk of the expenditures occurring in the second half of the year. An additional \$4.0 million of capital expenditures is forecast to be spent in 2014 for completion of Phase 1 facilities and initiation of Phase 2 engineering. The remainder of the facility capital costs for Phase 2 is scheduled for 2015.

*Alberta Plains North*

Our Alberta Plains North core area holds 36 percent of our proved and probable oil and liquids reserves. During 2012, significant oil exploitation projects included a multi-frac horizontal drilling test program at Hamilton Lake targeting large Viking reservoirs, along with the three well step-out development drilling program in the Glauconite oil pool at Killam/Jarrow. A new stepout well drilled at Bellhill Lake will lead to further drilling in 2013, while facility and pumping optimizations at Bellshill Lake, Killam South and Provost also provided additional oil volumes in 2012.

Alberta Plains North provided 45 percent of our production in 2012, primarily from the Jarrow, Hamilton Lake, Highvale and Progress areas. In 2013, modest investments in facility optimization projects will maximize returns from these natural gas properties in a weak natural gas price environment. We will also pursue sale, farmout and swap transactions on our large undeveloped land base to maximize returns and create a more concentrated property footprint.

In the first quarter of 2012, two multi-frac horizontal locations were drilled at the 47 section wholly-owned Hamilton Lake property, followed by a three well program in the fourth quarter of the year. Unlocking the potential of Hamilton Lake's large oil-in-place resource with stimulated horizontal wells and a reactivated waterflood will be a priority in 2013. Success at Hamilton Lake could lead to more than 30 additional horizontal oil locations. The McDaniel Report has not booked any of these undeveloped Hamilton Lake Viking multi-frac horizontal locations.

In addition to Hamilton Lake, 2012 capital was directed to the Killam property, where a three well horizontal development drilling program was completed in the first quarter. A pilot waterflood project is being considered for the property, with possible implementation in mid-2013. With further derisking, the Killam property is expected to be a significant oil exploitation project that could require numerous horizontal drainage wells to optimally exploit under a waterflood scheme. The McDaniel Report has booked only one of these undeveloped Killam Glauconite horizontal locations.

Additional 2013 Alberta expenditures will be directed to oil exploitation projects at Bellshill Lake, where further infill drilling plus oil treating and water disposal upgrades are expected to deliver increased oil production and reserves.

***Oil and Gas Wells***

The following table sets forth the number and status of wells in which we had a working interest as at December 31, 2012.

	Oil Wells				Natural Gas Wells			
	Producing		Non-Producing		Producing		Non-Producing	
	Gross	Net	Gross	Net	Gross	Net	Gross	Net
Canada								
British Columbia	-	-	-	-	-	-	3.0	1.4
Alberta	472.0	263.9	410.0	233.3	393.0	221.8	447.0	286.0
Saskatchewan	249.0	194.3	30.0	24.9	79.0	39.5	35.0	19.0
United States								
North Dakota	81.0	79.4	17.0	16.7	-	-	-	-
Total	802.0	537.6	457.0	274.9	472.0	261.3	485.0	306.4

Note:

(1) Well counts are based on wellbores.

**Properties with no Attributable Reserves**

The following table sets out our undeveloped land holdings as at December 31, 2012.

(thousand acres)	Undeveloped Acres	
	Gross	Net
Alberta	422	298
British Columbia	6	4
Saskatchewan	33	24
United States	11	11
Total	472	337

When determining gross and net acreage for two or more leases covering the same lands but different rights, the acreage is reported for each lease. Where there are multiple discontinuous rights in a single lease, the acreage is reported only once

With respect to our undeveloped land inventory and farm-in agreements, we have commitments from industry participants as follows:

- one option well to be drilled prior to March 24, 2013, in the Rycroft area of Alberta; and
- one well to be drilled prior to March 31, 2013, in the Elswick area of Saskatchewan.

Rights to explore, develop and exploit 64,465 net acres of our undeveloped land holdings in Canada and 1,084 net acres of our undeveloped land holdings in the United States are scheduled to expire by December 31, 2013.

**Forward Contracts**

We are exposed to market risks resulting from fluctuations in commodity prices, foreign exchange rates, electricity rates and interest rates in the normal course of our operations. A variety of derivative instruments are used to reduce exposure to fluctuations in commodity prices and foreign exchange rates. We are exposed to losses in the event of default by the counterparties to these derivative instruments. We manage this risk by diversifying our derivative portfolio amongst a number of financially strong counterparties. For information in relation to our marketing arrangements, see "Marketing Arrangements".

For details of our material commitments to sell natural gas and crude oil that were outstanding at December 31, 2012 see Note 16 to our 2012 annual audited consolidated financial statements, which is incorporated herein by reference.

**Additional Information Concerning Abandonment and Reclamation Costs**

As at December 31, 2012, we had 1,380.2 net wells capable of production for which we expect to incur abandonment and/or reclamation costs.

The total amount of abandonment and reclamation costs, net of estimated salvage values that we expect to incur are summarized in the following table.

Period	Abandonment and Reclamation Costs Escalated at 2% Undiscounted (\$000s)	Abandonment and Reclamation Costs Escalated at 2% Discounted at 10% (\$000s)
Total liability as at December 31, 2012	54,665	15,036
Anticipated to be paid in 2013	-	-
Anticipated to be paid in 2014	526	462
Anticipated to be paid in 2015	1,015	805

We have estimated the net present value of our total asset retirement obligations to be \$112 million as at December 31, 2012 based on a total future liability of \$135 million. The future net revenues disclosed in this Annual Information Form based on the McDaniel Report do not contain an allowance for abandonment and reclamation costs for batteries and salvage values are deducted. The McDaniel Report deducted \$54.67 million (undiscounted) and \$15.04 million (10 percent discount using forecast prices and costs for proved and probable reserves) for abandonment and reclamation costs in estimating the future net revenue disclosed in this Annual Information Form.

We do not expect to pay any material amounts with respect to abandonment and reclamation costs in the next two financial years.

### ***Tax Horizon***

We did not pay Canadian income taxes in 2012. During 2012, we incurred current income taxes in the United States of \$0.57 million, compared to \$1.53 million in 2011.

We are a taxable entity under the *Income Tax Act* (Canada); however, based on the current forward commodity strip, our tax pools are expected to shelter us from paying cash taxes in Canada beyond 2016.

### ***Costs Incurred***

The following table summarizes capital expenditures related to our activities for the year ended December 31, 2012.

(\$ million)	Canada	United States	Total
Property Acquisition Costs:			
Proved Properties <sup>(1)</sup>	(34.50)	-	(34.50)
Unproved Properties	5.00	0.45	5.45
Corporate Acquisitions	-	-	-
Development Costs <sup>(2)</sup>	52.04	2.92	54.96
Exploration Costs <sup>(3)</sup>	3.46	0.82	4.28
Total	26.00	4.19	30.19

Notes:

- (1) Acquisitions are net of disposition of properties.
- (2) Development and facilities expenditures.
- (3) Cost of land acquired, geological and geophysical capital expenditures and drilling costs for 2012 exploration wells drilled.

### ***Exploration and Development Activities***

The following table sets forth the gross and net exploratory and development wells in which we participated during the year ended December 31, 2012.

CANADA	Exploratory Wells		Development Wells	
	Gross	Net	Gross	Net
Oil	-	-	30.0	23.8
Natural Gas	-	-	-	-
Service	-	-	2.0	2.0
Stratigraphic Test	-	-	-	-
Dry	1.0	1.0	-	-
Total	1.0	1.0	32.0	25.8

UNITED STATES	Exploratory Wells		Development Wells	
	Gross	Net	Gross	Net
Oil	-	-	1.0	1.0
Natural Gas	-	-	-	-
Service	-	-	-	-
Stratigraphic Test	-	-	-	-
Dry	-	-	-	-
Total	-	-	1.0	1.0

In 2013, we are budgeted to invest approximately \$78 million in our core areas, which is comprised of a net \$40 million of field capital and \$38 million of ASP related expenditures. The entire amount is dedicated to exploration, exploitation, development and optimization of our existing assets. This amount does not include any capital for acquisitions, which will be pursued on an opportunistic basis.

For most details regarding our most important current exploration and development activities for 2013 see, "- Other Oil and Gas Information – Oil and Gas Properties" above.

### *Production Estimates*

The following table sets out the volumes of gross production estimated in the McDaniel Report for the year ended December 31, 2013, which is reflected in the estimate of future net revenue disclosed in the tables contained under "Disclosure of Reserves Data and Other Oil and Natural Gas Information".

CANADA	Light and	Natural Gas	Natural Gas	Heavy Oil	BOE
	Medium Oil	Natural Gas	Liquids	Heavy Oil	BOE
	(bbl/d)	(Mcf/d)	(bbl/d)	(bbl/d)	(boe/d)
Total Proved	3,297	14,982	55	1,710	7,559
Total Probable	203	547	3	139	436
Total Proved Plus Probable	3,500	15,529	58	1,849	7,995

UNITED STATES	Light and	Natural Gas	Natural Gas	Heavy Oil	BOE
	Medium Oil	Natural Gas	Liquids	Heavy Oil	BOE
	(bbl/d)	(Mcf/d)	(bbl/d)	(bbl/d)	(boe/d)
Total Proved	480	-	-	-	480
Total Probable	9	-	-	-	9
Total Proved Plus Probable	489	-	-	-	489



**Production History and Prices Received**

The following tables summarize certain information in respect of our production, product prices received, royalties paid, production expenses and resulting netbacks for the periods indicated.

**CANADA**

	Quarter Ended			
	2012			
	Dec. 31	Sept. 30	June 30	Mar. 31
<b>Average Daily Production:</b>				
Gas (Mcf/d)	15,929	15,329	17,436	20,030
Light and Medium Crude Oil (bbl/d)	2,809	2,752	3,012	3,152
Heavy Oil (bbl/d)	1,664	1,732	1,784	1,776
Natural Gas Liquids (bbl/d)	101	83	86	77
Combined (boe/d)	7,229	7,122	7,788	8,343
<b>Average Price Received: <sup>(1)</sup></b>				
Gas (\$/Mcf)	2.93	2.08	1.68	2.01
Light and Medium Crude Oil (\$/bbl)	75.95	76.52	76.49	84.32
Heavy Oil (\$/bbl)	67.00	67.80	68.79	79.15
Natural Gas Liquids (\$/bbl)	55.03	58.16	75.89	70.15
Combined (\$/boe)	52.17	51.20	49.95	54.18
<b>Royalties Paid:</b>				
Gas (\$/Mcf)	0.46	0.32	0.37	0.19
Light and Medium Crude Oil (\$/bbl)	13.81	14.93	13.19	15.82
Heavy Oil (\$/bbl)	12.99	12.77	13.66	16.26
Natural Gas Liquids (\$/bbl)	7.15	6.79	32.35	5.92
Combined (\$/boe)	9.47	9.63	9.43	9.95
<b>Production Costs:</b>				
Gas (\$/Mcf)	2.17	1.79	2.15	1.86
Light and Medium Crude Oil (\$/bbl)	19.75	18.26	20.30	22.24
Heavy Oil (\$/bbl)	17.01	16.46	17.81	19.89
Natural Gas Liquids (\$/bbl)	13.97	14.12	19.65	17.63
Combined (\$/boe)	16.58	15.07	16.93	17.27
<b>Netback Received: <sup>(2)</sup></b>				
Gas (\$/Mcf)	0.30	(0.03)	(0.84)	(0.04)
Light and Medium Crude Oil (\$/bbl)	42.39	43.33	43.00	46.26
Heavy Oil (\$/bbl)	37.00	38.57	37.32	43.00
Natural Gas Liquids (\$/bbl)	33.91	37.25	23.89	46.60
Combined (\$/boe)	26.12	26.50	23.59	26.96

## Notes:

- (1) Average price received is calculated before the impact of realized risk management gains or losses.
- (2) Netbacks are calculated by subtracting royalties and operating costs from revenues before realized risk management gains or losses.

## UNITED STATES

	Quarter Ended			
	2012			
	Dec. 31	Sept. 30	June 30	Mar. 31
<b>Average Daily Production:</b>				
Gas (Mcf/d)	-	-	-	-
Light and Medium Crude Oil (bbl/d)	491	512	502	491
Heavy Oil (bbl/d)	-	-	-	-
Natural Gas Liquids (bbl/d)	-	-	-	-
Combined (boe/d)	491	512	502	491
<b>Average Price Received: <sup>(1)</sup></b>				
Gas (\$/Mcf)	-	-	-	-
Light and Medium Crude Oil (\$/bbl)	70.48	71.24	68.32	78.42
Heavy Oil (\$/bbl)	-	-	-	-
Natural Gas Liquids (\$/bbl)	-	-	-	-
Combined (\$/boe)	70.48	71.24	68.32	78.42
<b>Royalties Paid:</b>				
Gas (\$/Mcf)	-	-	-	-
Light and Medium Crude Oil (\$/bbl)	16.82	18.00	17.30	19.95
Heavy Oil (\$/bbl)	-	-	-	-
Natural Gas Liquids (\$/bbl)	-	-	-	-
Combined (\$/boe)	16.82	18.00	17.30	19.95
<b>Production Costs:</b>				
Gas (\$/Mcf)	-	-	-	-
Light and Medium Crude Oil (\$/bbl)	15.24	19.03	14.72	12.94
Heavy Oil (\$/bbl)	-	-	-	-
Natural Gas Liquids (\$/bbl)	-	-	-	-
Combined (\$/boe)	15.24	19.03	14.72	12.94
<b>Netback Received: <sup>(2)</sup></b>				
Gas (\$/Mcf)	-	-	-	-
Light and Medium Crude Oil (\$/bbl)	38.42	34.21	36.30	45.53
Heavy Oil (\$/bbl)	-	-	-	-
Natural Gas Liquids (\$/bbl)	-	-	-	-
Combined (\$/boe)	38.42	34.21	36.30	45.53

## Notes:

- (1) Average price received is calculated before the impact of realized risk management gains or losses.
- (2) Netbacks are calculated by subtracting royalties and operating costs from revenues before realized risk management gains or losses.

## AGGREGATE

	Quarter Ended			
	2012			
	Dec. 31	Sept. 30	June 30	Mar. 31
<b>Average Daily Production:</b>				
Gas (Mcf/d)	15,929	15,329	17,436	20,030
Light and Medium Crude Oil (bbl/d)	3,300	3,264	3,514	3,643
Heavy Oil (bbl/d)	1,664	1,732	1,784	1,776
Natural Gas Liquids (bbl/d)	101	83	86	77
Combined (boe/d)	7,720	7,634	8,290	8,834
<b>Average Price Received: <sup>(1)</sup></b>				
Gas (\$/Mcf)	2.93	2.08	1.68	2.01
Light and Medium Crude Oil (\$/bbl)	75.14	75.69	75.33	83.52
Heavy Oil (\$/bbl)	67.00	67.80	68.79	79.15
Natural Gas Liquids (\$/bbl)	55.03	58.16	75.89	70.15
Combined (\$/boe)	53.33	52.55	51.06	55.53
<b>Royalties Paid:</b>				
Gas (\$/Mcf)	0.46	0.32	0.37	0.19
Light and Medium Crude Oil (\$/bbl)	14.26	15.41	13.78	16.37
Heavy Oil (\$/bbl)	12.99	12.77	13.66	16.26
Natural Gas Liquids (\$/bbl)	7.15	6.79	32.35	5.92
Combined (\$/boe)	9.94	10.19	9.90	10.51
<b>Production Costs:</b>				
Gas (\$/Mcf)	2.17	1.79	2.15	1.86
Light and Medium Crude Oil (\$/bbl)	19.08	18.38	19.51	20.99
Heavy Oil (\$/bbl)	17.01	16.46	17.81	19.89
Natural Gas Liquids (\$/bbl)	13.97	14.12	19.65	17.63
Combined (\$/boe)	16.49	15.34	16.80	17.03
<b>Netback Received: <sup>(2)</sup></b>				
Gas (\$/Mcf)	0.30	(0.03)	(0.84)	(0.04)
Light and Medium Crude Oil (\$/bbl)	41.80	41.90	42.04	46.16
Heavy Oil (\$/bbl)	37.00	38.57	37.32	43.00
Natural Gas Liquids (\$/bbl)	33.91	37.25	23.89	46.60
Combined (\$/boe)	26.90	27.02	24.36	27.99

Notes:

- (1) Average price received is calculated before the impact of realized risk management gains or losses.  
(2) Netbacks are calculated by subtracting royalties and operating costs from revenues before realized risk management gains or losses.

The following table indicates our average daily production from our core areas for the year ended December 31, 2012.

	Natural Gas	Light and Medium Crude Oil	Heavy Oil	NGLs	BOE
	(Mcf/d)	(bbl/d)	(bbl/d)	(bbl/d)	(boe/d)
Alberta Plains North	13,867	1,237	61	58	3,667
Alberta Plains South	2,860	11	1,676	29	2,193
Williston Basin	444	2,183	-	-	2,257
Total	17,171	3,431	1,737	87	8,117

## ***Marketing Arrangements***

### *Natural Gas*

Most of our natural gas production was sold by spot sale contracts and Alberta index prices were received. In order to control and manage credit risk and ensure competitive bids, we engage with a number of reputable counterparties for our natural gas transactions. The integration and application of these strategies resulted in an average realized price (after realized risk management gains/losses) of \$2.18 per Mcf in 2012 compared to \$3.45 per Mcf in 2011.

### *Oil and Natural Gas Liquids*

We sell our oil and natural gas liquids production to a variety of customers. This allows us to benefit from specific regional advantages while maintaining pricing and delivery flexibility. In general, we market our oil production with various purchasers under one month renewable contracts and receive posted reference prices with adjustments for quality and transportation. In 2012, our average realized oil and liquids price (after realized risk management gains/losses) was \$75.02 per bbl compared to \$76.19 per bbl in 2011.

### *Risk Management Activities*

Our commodity price risk management policy, which is approved by the Board of Directors, allows the sale of up to a 60 percent maximum of its estimated oil production for up to a 30 month period in order to meet capital program and dividend obligations in the event of significant commodity price declines. Because our risk management strategy is protective in nature and is designed to guard us against extreme effects on funds flow from sudden falls in prices and revenue, upward price spikes tend to produce overall losses. For details of our risk management activities in 2012 see our management's discussion and analysis relating to our 2012 annual audited consolidated financial statements under the heading "*Risk Management Activities*", which is incorporated herein by reference.

### ***Acquisitions and Dispositions***

During 2012, we completed several property transactions including the acquisition and disposition of oil and natural gas properties. In aggregate, we recorded \$34.50 million on net property dispositions in the year.

### ***Environmental Policies***

We have an environmental policy in place as part of our commitment to protecting the environment while conducting our operations. Our environmental policy states that:

- Operating in an environmentally responsible manner is key to insuring our continued growth and the industry.
- Sound environmental management is an integral component of a good business plan. Environmental stewardship reduces costs and corporate liability. It enhances shareholder value, boosts employee morale and enhances our image in the eyes of regulators and the public.
- Managing our environmental responsibilities is a team effort requiring the commitment of management, employees and contractors.
- Preventing environmental damage is cheaper than repairing damage.
- An effective environmental program helps operations staff to understand and comply with environmental laws and regulations and to minimize the costs and liabilities associated with environmental damage. It helps meet the concerns of investors, analysts, bankers, partners and the public that environmental issues are being managed properly and will provide a due-diligence defence in the event of an environmental incident.

Our management also monitors developments related to the climate change and other environmental laws and regulations.

We are not currently impacted by proposed environmental laws and regulations relating to the control of greenhouse gases (see "*Industry Conditions – Climate Change Regulation*") as none of our facilities qualify and currently, no facility production qualifies under the criteria described in the Updated Action Plan (as defined therein). We will continue to monitor the regulatory developments and any impact that they may have on our future compliance costs.

### Finding, Development and Acquisition Costs <sup>(1)</sup>

The following table sets forth our finding and development costs ("F&D") and our finding, development and acquisition costs ("FD&A") for the periods indicated. We have presented finding and development costs below both including and excluding acquisitions and dispositions. While NI 51-101 requires that the effects of acquisitions and dispositions be excluded, we have included these items because we believe that acquisitions and dispositions can have a significant impact on our ongoing reserve replacement costs and that excluding these amounts could result in an inaccurate portrayal of our cost structure.

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Total net capital expenditures (\$ millions) <sup>(2)</sup> - unaudited	30.19	48.29	71.38
Total net capital expenditures plus change in forecast proved plus probable future development costs (\$ millions) <sup>(2)</sup>	24.85	144.52	79.62
Proved plus probable reserves (Mmboe)			
Open	34.29	32.39	32.24
Discoveries and extensions	1.53	5.77	3.07
Acquisitions and dispositions	(1.09)	0.06	1.53
Revisions	(0.57)	(0.59)	(0.84)
Production	(2.97)	(3.34)	(3.61)
Close	<u>31.19</u>	<u>34.29</u>	<u>32.39</u>
Proved FD&A costs (\$/boe) <sup>(3)</sup>	111.86	21.11	24.60
Proved three-year average FD&A costs (\$/boe) <sup>(3)</sup>	26.64	21.30	21.13
Proved plus probable FD&A costs (\$/boe) <sup>(4)</sup>	-	27.58	21.18
Proved plus probable three-year average FD&A costs (\$/boe) <sup>(4)</sup>	28.07	21.48	18.83
Proved F&D costs (\$/boe) <sup>(3)</sup>	57.42	33.48	32.84
Proved three-year average F&D costs (\$/boe) <sup>(3)</sup>	37.88	27.50	22.18
Proved plus probable F&D costs (\$/boe) <sup>(4)</sup>	61.82	32.41	30.79
Proved plus probable three-year average F&D costs (\$/boe) <sup>(4)</sup>	35.35	30.06	24.80

Notes:

- (1) The aggregate of the exploration and development costs incurred in the most recent financial year and the change during that year in estimated future development costs generally will not reflect total finding and development costs related to reserves additions for that year.
- (2) Amounts exclude additions for administrative assets.
- (3) Amounts are calculated including the change in proved future development costs (2012 - \$(6.70) million; 2011 - \$(6.71) million; 2010 - \$12.49 million).
- (4) Amounts are calculated including the change in proved plus probable future development costs.

## OUR CAPITAL STRUCTURE

### Share Capital

Our authorized share capital consists of an unlimited number of Common Shares without nominal or par value and 10,000,000 preferred shares without nominal or par value issuable in series (the "**Preferred Shares**"). The following is a summary of the rights, privileges, restrictions and conditions which attach to our securities. The inclusion of Preferred Shares in our authorized share capital is intended to provide us with the flexibility to raise a limited amount of future capital in the form of preferred shares. At the present time, our management is not aware of any financing structures for oil and gas companies that involve the issuance of preferred shares. The Preferred Shares will not be utilized as a defence to any take-over bid.

### *Common Shares*

Holders of our Common Shares are entitled to notice of, to attend and to one vote per share held at any meeting of our Shareholders (other than meetings of a class or series of our shares other than the Common Shares).

Holders of our Common Shares will be entitled to receive dividends as and when declared by our Board of Directors on the Common Shares as a class, subject to prior satisfaction of all preferential rights to dividends attached to shares of other classes of our shares ranking in priority to the Common Shares in respect of dividends.

Holders of our Common Shares will be entitled in the event of our liquidation, dissolution or winding-up, whether voluntary or involuntary, or any other distribution of our assets among our Shareholders for the purpose of winding-up our affairs, and subject to prior satisfaction of all preferential rights to return of capital on dissolution attached to all shares of other classes ranking in priority to the Common Shares in respect of a return of capital on dissolution, to share rateably, together with the holders of shares of any other class of our shares ranking equally with the Common Shares in respect of a return of capital on dissolution, in such of our assets as are available for distribution.

### *Preferred Shares*

The Preferred Shares may be issued in one or more series, at any time or from time to time. Before any shares of a particular series are issued, our Board of Directors will fix the number of shares that will form such series and will, subject to the limitations set out in the preferred share terms described below, fix the designation, rights, privileges, restrictions and conditions to be attached to the Preferred Shares of such series, including, but without in any way limiting or restricting the generality of the foregoing, the rate, amount or method of calculation of dividends thereon, the time and place of payment of dividends, the consideration for and the terms and conditions of any purchase for cancellation, retraction or redemption thereof, conversion or exchange rights (if any), and whether into or for our securities or otherwise, voting rights attached thereto (if any), the terms and conditions of any share purchase or retirement plan or sinking fund, and restrictions on the payment of dividends on any shares other than Preferred Shares or payment in respect of capital on any shares in our capital or creation or issue of debt or equity securities; the whole subject to filing of Articles of Amendment setting forth a description of such series including the designation, rights, privileges, restrictions and conditions attached to the shares of such series. Notwithstanding the foregoing: (a) our Board of Directors may at any time or from time to time change the rights, privileges, restrictions and conditions attached to unissued shares of any series of Preferred Shares; and (b) other than in the case of a failure to declare or pay dividends specified in any series of the Preferred Share, the voting rights attached to the Preferred Shares will be limited to one vote per Preferred Share at any meeting where the Preferred Shares and Common Shares vote together.

### Credit Facility

We have a syndicated credit facility with a \$165 million borrowing base. A \$300 million demand debenture on our assets has been provided as security for these facilities. The facilities are fully revolving for a 377 day period with the provision for an annual extension at the option of the lenders and upon notice from us. The next renewal date is June 26, 2013. Should the facilities not be renewed, they convert to one year non-revolving term facilities at the end of the revolving 365 day period. Repayment would not be required until the end of the non-revolving term.

Interest rates fluctuate under the syndicated facilities with Canadian prime, US prime and US base rates plus an applicable margin between 50 basis points and 200 basis points as well as with Canadian banker's acceptance and LIBOR rates plus an applicable margin between 200 basis points and 350 basis points. Unused amounts under the facility are subject to standby fees. In the normal course of operations we enter into various letters of credit. The letters of credit reduce the amount of our available credit facilities.

### **Convertible Debentures**

The Convertible Debentures were issued under and pursuant to the provisions of the Debenture Indenture. The following description of the Convertible Debentures is a summary of their material attributes and characteristics and is subject to the detailed provisions of the Debenture Indenture and is qualified in its entirety by reference to the Debenture Indenture which has been filed and is available on SEDAR at [www.sedar.com](http://www.sedar.com).

#### ***General***

The Convertible Debentures mature on June 30, 2017 and bear interest at an annual rate of 6.00% payable semi-annually in arrears on June 30 and December 31 in each year commencing on December 31, 2012.

#### ***Conversion Privilege***

Each Convertible Debenture is convertible at the option of the holder into fully paid and non-assessable Common Shares at any time prior to 5:00 p.m. (Calgary time) on the earliest of: (i) the last business day immediately preceding their maturity and (ii) the last business day immediately preceding the date specified by us for redemption, in each case, at a conversion price of \$18.80 per Common Share, representing a conversion rate of approximately 53.1915 Common Shares per \$1,000 principal amount of Convertible Debentures. The conversion price may be adjusted in certain circumstances as described in the Debenture Indenture.

Interest will be paid on conversion from up to, but not including, the date of conversion. The Convertible Debentures may not be converted on June 30 or December 31 or during the five business days preceding June 30 and December 31 in each year, as the registers of the Debenture Trustee will be closed during such periods. No fractional Common Shares will be issued on any conversion of the Convertible Debenture but in lieu thereof we will satisfy fractional interests by a cash payment equal to the current market price of any fractional interest.

#### ***Redemption and Purchase***

The Convertible Debentures may not be redeemed by us before June 30, 2015, except in certain limited circumstances following a change of control. On or after June 30, 2015 and prior to their maturity, the Convertible Debentures may be redeemed by us, in whole or in part from time to time, at our option on not more than 60 days' and not less than 30 days' prior written notice at a redemption price equal to the principal amount plus accrued and unpaid interest thereon, if any, provided that the current market price of the Common Shares on the date on which notice of redemption is given is not less than 125% of the conversion price. In the event that a holder of Convertible Debentures exercises their conversion right following a notice of redemption by us, the holder will be entitled to receive accrued and unpaid interest, in addition to the applicable number of Common Shares to be received on conversion, for the period from the last interest payment date up to, but not including, the date of conversion.

In the case of redemption of less than all of the Convertible Debentures, the Convertible Debentures to be redeemed will be selected by the Debenture Trustee on a *pro rata* basis or in such other manner as the Debenture Trustee deems equitable, subject to regulatory approvals.

We have the right to purchase Convertible Debentures for cancellation in the market, by tender or by private contract, at any time, subject to regulatory requirements.

### ***Payment upon Redemption or at Maturity***

On redemption or at maturity, as applicable, we are required to repay the indebtedness represented by the Convertible Debentures by paying to the Debenture Trustee an amount equal to the principal amount of the outstanding Convertible Debentures, together with accrued and unpaid interest thereon, if any, up to but not including the redemption date or the maturity date, as applicable. On redemption or at maturity, as applicable, we may, at our option, on not more than 60 days' and not less than 40 days' prior notice and subject to any required regulatory approvals, and provided that no event of default has occurred and is continuing, elect to satisfy our obligation to repay, in whole or in part, the principal amount of the Convertible Debentures which are to be redeemed or which have matured by issuing and delivering Common Shares to the holders of the Convertible Debentures in an amount equal to the principal amount of the Convertible Debentures divided by 95% of the current market price of the Common Shares. Any accrued and unpaid interest thereon will be paid in cash. In the event a holder of Convertible Debentures exercises its conversion rights following delivery of a notice of redemption by us, such holder shall be entitled to receive the applicable number of Common Shares to be received on conversion on the last business day immediately preceding the redemption.

No fractional Common Shares will be issued upon redemption or at maturity of the Convertible Debenture but in lieu thereof we will satisfy fractional interests by a cash payment equal to the current market price of any fractional interest.

### ***Rank***

The Convertible Debentures are subordinate to all Senior Indebtedness as more particularly described below under "*Subordination*". In the event of our insolvency, bankruptcy, liquidation, reorganization, dissolution or winding up, our assets would be made available to satisfy the obligations of the creditors of such Senior Indebtedness before being available to pay our obligations to the holders of Convertible Debentures. Accordingly, all or a substantial portion of our assets could be unavailable to satisfy the claims of the holders of Convertible Debentures.

### ***Subordination***

The payment of the principal and premium, if any, of, and interest on, the Convertible Debentures is subordinated and postponed, and subject in right of payment, to the full and final payment of all of our Senior Indebtedness. "**Senior Indebtedness**" is defined in the Debenture Indenture as all of our obligations, liabilities and indebtedness which would, in accordance with generally accepted accounting principles, be classified upon our consolidated balance sheet as our liabilities and, whether or not so classified, includes (without duplication): (a) our indebtedness for borrowed money; (b) our obligations evidenced by bonds, debentures, notes or other similar instruments; (c) our obligations arising pursuant or in relation to bankers' acceptances, letters of credit, letters of guarantee, performance bonds and surety bonds (including payment and reimbursement obligations in respect thereof) or indemnities issued in connection therewith; (d) our obligations under any swap, hedging or other similar contracts or arrangements; (e) our obligations under guarantees, indemnities, assurances, legally binding comfort letters or other contingent obligations relating to the Senior Indebtedness or other obligations of any other person which would otherwise constitute Senior Indebtedness within the meaning of this definition; (f) all of our indebtedness representing the deferred purchase price of any property including, without limitation, purchase money mortgages; (g) accounts payable to trade creditors; (h) all renewals, extensions and refinancing of any of the foregoing; (i) all declared but unpaid dividends or distributions; and (j) all costs and expenses incurred by or on behalf of any senior creditor in enforcing payment or collection of any such Senior Indebtedness, including enforcing any security interest securing the same but "**Senior Indebtedness**" does not include any indebtedness that would otherwise be Senior Indebtedness if it is expressly stated to be subordinate to or rank *pari passu* with the Convertible Debentures.

The Debenture Indenture provides that in the event of any insolvency or bankruptcy proceedings, or any receivership, liquidation, reorganization or other similar proceedings relative to us, or to our property or assets, or in the event of any proceedings for voluntary liquidation, dissolution or other winding-up of us, whether or not involving insolvency or bankruptcy, or any marshalling of our assets and liabilities, then holders of Senior Indebtedness will receive payment in full before the holders of Convertible Debentures will be entitled to receive any payment or distribution of any kind or character, whether in cash, property or securities, which may be payable



or deliverable in any such event in respect of any of the Convertible Debentures or any unpaid interest accrued thereon. The Debenture Indenture also provides that we will not make any payment, and the holders of the Convertible Debentures will not be entitled to demand, institute proceedings for the collection of, or receive any payment or benefit (including, without any limitation, by set-off, combination of accounts or realization of security or otherwise in any manner whatsoever) on account of indebtedness represented by the Convertible Debentures: (a) in a manner inconsistent with the terms (as they exist on the date of issue) of the Convertible Debentures; or (b) at any time when a default or an event of default has occurred under the Senior Indebtedness and is continuing or upon the acceleration of Senior Indebtedness, unless the Senior Indebtedness has been repaid in full.

### ***Repurchase upon a Change of Control***

Within 30 days following the occurrence of a Change of Control, we are required to make a cash offer to purchase all of the Convertible Debentures at a price equal to 100% of the principal amount thereof plus accrued and unpaid interest thereon. A "**Change of Control**" is defined in the Debenture Indenture to include: (i) an acquisition by a person or group of persons acting jointly or in concert (within the meaning of Multilateral Instrument 62-104 – *Take-Over Bids and Issuer Bids* ("**MI 62-104**") and in Ontario, the *Securities Act* (Ontario) and Ontario Securities Commission Rule 62-504 – *Take-Over Bids and Issuer Bids*) of ownership of, or voting control or direction over, more than 50% of the issued and outstanding Common Shares; or (ii) the sale or other transfer of all or substantially all of our consolidated assets, excluding a sale, merger, reorganization or other similar transaction if the previous holders of the Common Shares hold at least 50% of the voting control in such merged, reorganized or other continuing entity.

If Convertible Debentures representing 90% or more of the aggregate principal amount of the Convertible Debentures outstanding on the date of the giving of notice of the Change of Control are tendered for purchase following a Change of Control (other than Convertible Debentures held at the date of the take-over bid by or on behalf of the offeror, associates or affiliates of the offeror or any one acting jointly or in concert with the offeror), we have the right to redeem all of the remaining Convertible Debentures at the same price.

### ***Cash Change of Control***

In addition to the requirement for us to make a cash offer to purchase all of the Convertible Debentures in the event of a Change of Control, if a Change of Control occurs on or before maturity in which 10% or more of the consideration for the Common Shares in the transaction or transactions constituting a Change of Control consists of: (i) cash (other than cash payments for fractional Common Shares and cash payments made in respect of dissenters' appraisal rights); (ii) equity securities (including trust units, limited partnership units or other participating securities of a trust, limited partnership or similar entity) that are not traded or intended to be traded immediately following such transactions on a recognized stock exchange; or (iii) other property that is not traded or intended to be traded immediately following such transactions on a recognized stock exchange, then subject to regulatory approvals, holders of Convertible Debentures will be entitled to convert their Debentures, subject to certain limitations, and receive, subject to and upon completion of the Change of Control, in addition to the number of Common Shares they would otherwise be entitled to receive on conversion, an additional number of Common Shares per \$1,000 principal amount of Convertible Debentures. The number of such additional Common Shares per \$1,000 principal amount of Debentures will be determined by reference to the provisions of the Debenture Indenture based on the date on which the Change of Control becomes effective and the price paid per Common Share in the transaction constituting the Change of Control.

### ***Interest Payment Election***

Unless an Event of Default (as defined below) under the Debenture Indenture has occurred and is continuing, we may elect, from time to time, subject to applicable regulatory approval, to satisfy our obligation to pay all or any portion of the interest on the Convertible Debentures by delivering sufficient Common Shares to the Debenture Trustee for sale, to satisfy such obligation, and holders of the Convertible Debentures will be entitled to receive a cash payment equal to the interest payable from the proceeds of the sale of such Common Shares. The Debenture Indenture sets out the procedures to be followed by us and the Debenture Trustee in order to effect this election.

### ***Events of Default***

The Debenture Indenture provides that an event of default ("**Event of Default**") in respect of the Convertible Debentures will occur if certain events described in the Debenture Indenture occur, including if any one or more of the following described events has occurred and is continuing with respect to such Convertible Debentures: (i) failure for 30 days to pay interest on the Convertible Debentures when due; (ii) failure to pay principal or premium, if any (whether by payment in cash or delivery of Common Shares), on the Convertible Debentures when due, whether at maturity, upon redemption, on a change of control, by declaration or otherwise; (iii) default in the delivery, when due, of any Common Shares or other consideration, including any Make-Whole Premium (as defined below), payable upon conversion with respect to the Convertible Debentures, which default continues for 15 days; (iv) default in the observance or performance of any other covenant or condition of the Debenture Indenture and the failure to cure (or obtain a waiver for) such default for a period of 30 days after notice in writing has been given by the Debenture Trustee or from holders of not less than 25% of the aggregate principal amount of the Convertible Debentures specifying such default and requiring us to rectify or obtain a waiver for same; (v) certain events of bankruptcy, insolvency or reorganization of us under bankruptcy or insolvency laws; and (vi) if an event of default occurs or exists under any agreement evidencing indebtedness for borrowed money (other than non-recourse debt) of us and as a result of such event of default (a) indebtedness for borrowed money thereunder in excess of \$10,000,000 has become due and payable before the date it would otherwise have been due and payable, and (b) the holders of such indebtedness are entitled to commence, and have commenced, the enforcement of security they hold for such indebtedness (if any) or the exercise of any other creditors' remedies to collect such indebtedness.

If an Event of Default has occurred and is continuing, the Debenture Trustee may, in its discretion, and will, upon the request of holders of not less than 25% in principal amount of the then-outstanding Convertible Debentures declare the principal of (and premium, if any) and interest on all outstanding Convertible Debentures to be immediately due and payable. In certain cases, the holders of more than 50% of the principal amount of the Convertible Debentures then-outstanding may, on behalf of the holders of all Convertible Debentures, waive any Event of Default and/or cancel any such declaration upon such terms and conditions as such holders shall prescribe.

### ***Offers for Convertible Debentures***

The Debenture Indenture contains provisions to the effect that if an offer is made for the Convertible Debentures which is a take-over bid for the Convertible Debentures within the meaning of MI 62-104 and in Ontario, the *Securities Act* (Ontario) and Ontario Securities Commission Rule 62-504 if the Convertible Debentures were considered equity securities, and not less than 90% of the principal amount of the then-outstanding Convertible Debentures (other than Convertible Debentures held at the date of the take-over bid by or on behalf of the offeror or associates or affiliates of the offeror) are taken up and paid for by the offeror, the offeror will be entitled to acquire the Convertible Debentures held by those who did not accept the offer on the terms offered by the offeror.

### ***Modification***

The rights of the holders of Convertible Debentures may be modified in accordance with the terms of the Debenture Indenture. For that purpose, among others, the Debenture Indenture will contain certain provisions which make binding on all holders of outstanding Convertible Debentures, resolutions passed at meetings of the holders of outstanding Convertible Debentures by votes cast thereat by holders of not less than 66⅔% of the principal amount of the then-outstanding Convertible Debentures present at the meeting or represented by proxy, or rendered by instruments in writing signed by the holders of not less than 66⅔% of the principal amount of the then-outstanding Convertible Debentures. Under the Debenture Indenture, certain amendments of a technical nature or which are not prejudicial to the rights of the holders of the Convertible Debentures may be made to the Debenture Indenture without the consent of the holders of the Convertible Debentures.

## DIRECTORS AND OFFICERS

### *Directors*

The name, municipality of residence, principal occupation for the prior five years and position (including with a predecessor of us), of each of our directors is as follows:

<b>Name and Municipality of Residence</b>	<b>Director Since</b>	<b>Principal Occupation</b>
<b>Craig H. Hansen</b> Calgary, Alberta	1992	Our President & Chief Executive Officer since 1993.
<b>K. James Harrison</b> <sup>(2)</sup> Oakville, Ontario	1995	Mr. Harrison is our Chairman. He is the founder of K.J. Harrison & Partners Inc., a private client investment management firm in Toronto, Ontario. Prior to 2000, he was the Vice-Chairman and Chief Executive Officer of Connor Clark Ltd.
<b>Kyle D. Kitagawa</b> <sup>(1)</sup> Calgary, Alberta	2001	Mr. Kitagawa brings over 25 years experience in commodity trading, equity investing, and structured finance in energy and energy intensive industries. Prior to April 2003, he held senior executive positions in a global energy trading and capital corporation. Mr. Kitagawa has been an independent businessman since 2003. In addition, Mr. Kitagawa serves as Chairman of both Canadian Energy Services & Technology Corp. and Coral Hill Energy Ltd. Prior directorships included Advanced Mobile Power Systems, LLC., Esprit Exploration Ltd., Ferus Trust, Independent Energy Ltd., Invasion Energy Inc., Livingston Energy Ltd., Papier Masson Ltee., ProspEx Resources Ltd. and Wave Energy Ltd.
<b>Margaret A. McKenzie</b> <sup>(1)</sup> Calgary, Alberta	2007	Ms. McKenzie is the Chief Financial Officer of Range Royalty Management Ltd., general partner of Range Royalty Limited Partnership, a private royalty partnership. She was previously Vice President Finance and Chief Financial Officer of Profico Energy Management Ltd., a private oil and gas company, and Manager, Treasury and Administration with Renaissance Energy Ltd., a public oil and gas company.
<b>Geoffrey C. Merritt</b> <sup>(1)</sup> Calgary, Alberta	2009	Mr. Merritt has been an independent businessman since April, 2009. Mr. Merritt was the founder of Masters Energy Inc., a public exploration and production company, incorporated in 2003 and acquired by us in April 2009. From 1998 to 2003, Mr. Merritt was the President and CEO of Sunfire Energy Corporation, a public oil and gas company. Prior to 1998, Geoff was the Vice President and General Manager of the oil and gas division of Pembina Corporation. Mr. Merritt currently sits on the board of Perpetual Energy Inc.

<b>Name and Municipality of Residence</b>	<b>Director Since</b>	<b>Principal Occupation</b>
<b>Jim Peplinski</b> <sup>(2)</sup> Calgary, Alberta	1997	Mr. Peplinski is the founder of Jim Peplinski Leasing Inc., a commercial vehicle lessor. Mr. Peplinski is also the VP Business Development, Calgary Flames Hockey Club as well as an investor in real estate and oil and gas. Mr. Peplinski currently sits on the board of directors of Wrangler West Energy Corp.
<b>J. Graham Weir</b> <sup>(1)</sup> Calgary, Alberta	2004	Mr. Weir is an independent businessman. From September 1990 to December 2000, he was Vice President and Director of Corporate Finance for Goepel McDermid Inc., an investment bank, where he initiated and completed acquisition, financing, financial advisory, merger and valuation assignments for mid-market public and private companies generally headquartered in Calgary and active in the oil and gas producer and service sectors. Mr. Weir chairs the boards of Graymont Limited and Pulse Seismic Inc. and serves as a director of other companies including: Coral Hill Energy Ltd., Flagstone Energy Inc., Grupo Calidra, S.A. de C.V. and Joss Windpower Inc.
<b>Grant A. Zawalsky</b> <sup>(2)</sup> Calgary, Alberta	2000	Mr. Zawalsky is a Partner of Burnet, Duckworth & Palmer LLP, Barristers and Solicitors. Mr. Zawalsky has been a Partner of Burnet, Duckworth & Palmer LLP since 1994. Mr. Zawalsky currently sits on the board of directors of a number of public and private companies including Endurance Energy Ltd., Flagstone Energy Inc., Home Quarter Resources Ltd., NuVista Energy Ltd., Range Royalty Management Ltd. (general partner of Range Royalty Limited Partnership), Spur Resources Ltd., Whitecap Resources Inc. and is Corporate Secretary of Bonavista Energy Corporation, Northpoint Energy Ltd., RMP Energy Inc. and Rock Energy Ltd.

## Notes:

- (1) Member of our audit and reserves committee.
- (2) Member of our governance and compensation committee.
- (3) We do not have an executive committee.
- (4) Directors hold office until the next annual meeting of Shareholders or until their successors are duly elected or appointed.

**Officers**

The name, municipality of residence, principal occupation for the prior five years and position (including with a predecessor of us), of each of our officers is as follows:

<b><u>Name and Municipality of Residence</u></b>	<b><u>Officer Since</u></b>	<b><u>Office</u></b>
<b>Craig H. Hansen</b> Calgary, Alberta	1992	President & Chief Executive Officer.
<b>Leslie E. Burden</b> Calgary, Alberta	2013	Vice President, Land since February 2013; prior thereto our Manager, Land Negotiations and Manager, Land since 2010 and prior thereto Manager, Land at Masters Energy Inc. from 2005.
<b>Randolph J. Doetzel</b> Calgary, Alberta	2011	Vice President, Operations since June, 2011; prior thereto, our Production Manager, Williston Basin since January, 2009. Prior thereto, Randy held various executive, management and engineering positions at Cobalt International Energy Inc., Harvest Operations Corp., Apache Canada Ltd., and Samson Canada Ltd.
<b>Jason B. Dranchuk</b> Calgary, Alberta	2006	Vice President, Finance and Chief Financial Officer; prior thereto, our Vice President, Finance and Controller and before that Corporate Controller for Enserco Energy Service Company Inc. and Calfrac Well Services Ltd.
<b>Tracy L. Howard</b> Calgary, Alberta	2007	Corporate Secretary; prior thereto, our Manager, Administration.
<b>Christopher M. Hustad</b> Calgary, Alberta	2013	Vice President, Alberta Plains South since February, 2013; prior thereto, our Manager Exploitation, Alberta Plains South since August, 2008. Prior thereto, various management and engineering positions at Talisman Energy Inc.
<b>Pete H.S. Janjua</b> Calgary, Alberta	2013	Vice President, Williston Basin since February 2013; prior thereto, our Manager Exploitation Williston Basin, Senior Technical position since 2006.
<b>Brian G. Kergan</b> Calgary, Alberta	2007	Vice President, Corporate Development since August, 2007.
<b>Kevin C.Y. Lee</b> Calgary, Alberta	2009	Vice President, Alberta Plains North since September, 2009; prior thereto, Vice President, Engineering of Trafalgar Energy Ltd., a public energy company.
<b>Robert T. Moriyama</b> Calgary, Alberta	2011	Vice President, Enhanced Recovery since January, 2011; prior thereto, he held various management and reservoir & exploitation engineering roles with Legacy Oil & Gas Ltd., CanEra Resources Inc., Pengrowth Corporation and Imperial Oil.

As at March 12, 2013, our directors and officers, as a group, beneficially owned, controlled or directed, directly or indirectly, 2,245,108 Common Shares or approximately 7.5 percent of our issued and outstanding Common Shares.

**Corporate Cease Trade Orders, Bankruptcies or Penalties or Sanctions**

None of our directors or executive officers (nor any personal holding company of any of such persons) is, as of the date of this Annual Information Form, or was within ten years before the date of this Annual Information Form, a director, chief executive officer or chief financial officer of any company (including us), that was subject to a cease trade order (including a management cease trade order), an order similar to a cease trade order or an order that

denied the relevant company access to any exemption under securities legislation, in each case that was in effect for a period of more than 30 consecutive days (collectively, an "**Order**") that was issued while the director or executive officer was acting in the capacity as director, chief executive officer or chief financial officer or was subject to an Order that was issued after the director or executive officer ceased to be a director, chief executive officer or chief financial officer and which resulted from an event that occurred while that person was acting in the capacity as director, chief executive officer or chief financial officer.

Except as otherwise disclosed herein, none of our directors or executive officers (nor any personal holding company of any of such persons), or shareholder holding a sufficient number of our securities to affect materially our control is, as of the date of this Annual Information Form, or has been, within the ten years before the date of this Annual Information Form, a director or executive officer of any company (including us) that, while that person was acting in that capacity, or within a year of that person ceasing to act in that capacity, became bankrupt, made a proposal under any legislation relating to bankruptcy or insolvency or was subject to or instituted any proceedings, arrangement or compromise with creditors or had a receiver, receiver manager or trustee appointed to hold its assets, other than Mr. Zawalsky who was a director of Efficient Energy Resources Ltd. (a private electrical generation company), which agreed to the voluntary appointment of a receiver in 2005. In addition, none of our directors or executive officers (nor any personal holding company of any such persons), or shareholder holding a sufficient number of our securities to materially affect the control of us has, within the ten years before the date of this Annual Information Form, become bankrupt, made a proposal under any legislation relating to bankruptcy or insolvency, or become subject to or instituted any proceedings, arrangement or compromise with creditors, or had a receiver, receiver manager or trustee appointed to hold the assets of the director, executive officer or shareholder.

In addition, none of our directors or executive officers (nor any personal holding company of any of such persons), or shareholder holding a sufficient number of our securities to affect materially the control of us, has been subject to any penalties or sanctions imposed by a court relating to securities legislation or by a securities regulatory authority or has entered into a settlement agreement with a securities regulatory authority or any other penalties or sanctions imposed by a court or regulatory body that would likely be considered important to a reasonable investor in making an investment decision.

### **Conflicts of Interest**

Circumstances may arise where members of our Board of Directors serve as directors or officers of corporations that are in competition to our interests. No assurances can be given that opportunities identified by such board members will be provided to us.

The *Business Corporations Act* (Alberta) provides that in the event that a director has an interest in a contract or proposed contract or agreement, the director shall disclose his interest in such contract or agreement and shall refrain from voting on any matter in respect of such contract or agreement unless otherwise provided under the *Business Corporations Act* (Alberta). To the extent that conflicts of interest arise, such conflicts will be resolved in accordance with the provisions of the *Business Corporations Act* (Alberta).

## **AUDIT AND RESERVES COMMITTEE INFORMATION**

### **Audit and Reserves Committee Mandate and Terms of Reference**

The Mandate of our audit and reserves committee is attached hereto as Schedule "C". The members of our audit and reserves committee are Kyle D. Kitagawa, Margaret A. McKenzie, Geoffrey C. Merritt and J. Graham Weir.

### **Composition of the Audit and Reserves Committee**

The members of our audit and reserves committee are independent (in accordance with National Instrument 52-110 – *Audit Committees*) and are financially literate.

***Relevant Education and Experience***

<b>Name</b>	<b>Relevant Education and Experience</b>
<p>Kyle D. Kitagawa <i>(Audit and Reserves Committee Chairman)</i></p>	<p>Mr. Kitagawa brings over 25 years experience in commodity trading, equity investing, and structured finance in energy and energy intensive industries. Prior to April 2003, he held senior executive positions in a global energy trading and capital corporation. Mr. Kitagawa has been an independent businessman since 2003. In addition, Mr. Kitagawa serves as Chairman of both Canadian Energy Services &amp; Technology Corp. and Coral Hill Energy Ltd. Prior directorships included Advanced Mobile Power Systems, LLC., Esprit Exploration Ltd., Ferus Trust, Independent Energy Ltd., Invasion Energy Inc., Livingston Energy Ltd., Papier Masson Ltee., ProspEx Resources Ltd. and Wave Energy Ltd.</p> <p>He holds a Master of Business Administration degree from Queen's University, a Bachelor of Commerce from the University of Calgary and is a Chartered Accountant.</p>
<p>Margaret A. McKenzie</p>	<p>Ms. McKenzie is the Chief Financial Officer, Range Royalty Management Ltd., general partner of Range Royalty Limited Partnership, a private royalty partnership. She was previously Vice President Finance and Chief Financial Officer of Profico Energy Management Ltd., a private oil and gas company and Manager, Treasury and Administration with Renaissance Energy Ltd., a public oil and gas company.</p> <p>Ms. McKenzie holds a Bachelor of Commerce with Distinction degree from the University of Saskatchewan and has been a member of the Institute of Chartered Accountants of Alberta since 1985. Ms. McKenzie is on the board of directors of Bonavista Energy Corporation and three private oil and natural gas exploration and development companies (Spur Resources Ltd., Endurance Energy Ltd. and Home Quarter Resources Ltd.).</p>
<p>Geoffrey C. Merritt</p>	<p>Mr. Merritt has over 30 years of experience in the upstream oil and gas sector. In 2003, he founded Masters Energy Inc., a public exploration and production company, which was acquired by Zargon in April 2009. From 1998 to 2003, Mr. Merritt was the President and Chief Executive Officer of Sunfire Energy. Prior to 1998, he was the Vice President and General Manager of the oil and gas division of Pembina Corporation. He currently sits on the board of Perpetual Energy Inc.</p> <p>Mr. Merritt received a Bachelor of Science in Chemical Engineering from the University of Alberta in 1978 and is a graduate of the Harvard Business School.</p>
<p>J. Graham Weir</p>	<p>Mr. Weir is an independent businessman. From September 1990 to December 2000, he was Vice President and Director of Corporate Finance for Goepel McDermid Inc. (an investment bank), where he initiated and completed acquisition, financing, financial advisory, merger and valuation assignments for mid-market public and private companies generally headquartered in Calgary and active in the oil and gas producer and service sectors. Mr. Weir chairs the boards of Graymont Limited and Pulse Seismic Inc. and serves as a director of other companies including: Coral Hill Energy Ltd., Flagstone Energy Inc., Grupo Calidra, S.A. de C.V. and Joss Windpower Inc.</p> <p>Mr. Weir graduated from Trent University in 1974 with a Bachelors Degree in Mathematics and the University of Manitoba in 1977 with a Masters Degree in Actuarial Mathematics. Mr. Weir received the designation Chartered Business Valuator in 1994 and completed a Masters Degree in Mathematical Finance at the University of Oxford in 2005.</p>

**Pre-Approval Policies and Procedures**

Our audit and reserves committee must pre-approve all non-audit services to be provided to us or our subsidiaries by our external auditors. Our audit and reserves committee may delegate to one or more members the authority to pre-approve non-audit services, provided that the member reports to our audit and reserves committee at the next

scheduled meeting and that such pre-approval and the member comply with such other procedures as may be established by our audit and reserves committee from time to time.

### **External Auditor Service Fees**

#### ***Audit Fees***

The aggregate fees billed by our external auditors, including expenses, in each of the last two fiscal years for audit services were \$220,659 in 2012 and \$206,275 in 2011.

#### ***Tax Fees***

The aggregate fees billed in each of the last two fiscal years for professional services rendered by our external auditors, including expenses for tax compliance, tax advice and tax planning were \$106,893 in 2012 and \$213,452 in 2011.

#### ***All Other Fees***

The aggregate fees billed in each of the last two fiscal years for products and services provided by our auditors other than services reported above were \$105,925 in 2012 and \$54,078 in 2011.

## **DIVIDENDS**

We currently make monthly dividend payments to our Shareholders on the 15th day of each month or the first business day following the 15th day. The record date for any dividend is the last business day of the month preceding the dividend date or such other date as may be determined by our Board of Directors. In accordance with stock exchange rules, an ex-dividend date occurs two trading days prior to the record date to permit time for settlement of trades of securities and dividends must be declared a minimum of seven trading days before the record date. Unless otherwise indicated, all dividends paid or to be paid on our Common Shares are designated as "eligible dividends" for Canadian income tax purposes.

In connection with the Arrangement, our prior Distribution Reinvestment Plan was amended and restated as a Dividend Reinvestment Plan. Canadian Shareholders who participate in the Dividend Reinvestment Plan are entitled to reinvest monthly cash dividends in additional Common Shares. At our discretion, the additional Common Shares will be issued from treasury at a 95 percent of the weighted average trading price of our Common Shares for the five days prior to the dividend payment date or acquired at prevailing market rates with no discount.

Dividends can and may fluctuate in the future. Actual future cash dividends, if any, will be subject to the discretion of our Board of Directors and may vary depending on a variety of factors and conditions existing from time to time, including fluctuations in commodity prices, production levels, capital expenditure requirements, debt service requirements, operating costs, royalty burdens, foreign exchange rates and the satisfaction of the liquidity and solvency tests imposed by the *Business Corporations Act* (Alberta) for the declaration and payment of dividends. Our Board of Directors cannot provide assurance that cash flow will be available for distribution to Shareholders in the amounts anticipated or at all. See "*Risk Factors*".

The payment of dividends by a corporation is governed by the liquidity and insolvency tests described in the *Business Corporations Act* (Alberta). Pursuant to the *Business Corporations Act* (Alberta), after the payment of a dividend, we must be able to pay our liabilities as they become due and the realizable value of our assets must be greater than our liabilities and the legal stated capital of our outstanding securities.

Our ability to make cash dividends to Shareholders may be directly or indirectly affected in certain events as a result of certain restrictions, including restrictions set forth in our Credit Facility and the solvency tests in the *Business Corporations Act* (Alberta). In particular, dividends may be only declared and paid to Shareholders if: (i) no default or event of default shall have occurred or shall occur as a result of making any such dividends; and (ii) no borrowing base shortfall shall have occurred that is continuing.



The following monthly cash dividends have been declared by us or the Trust for each of the three most recently completed financial years:

<b>For the Month Ended</b>	<b>Dividends per Common Share</b>	<b>Payment Date</b>
January 31, 2012	\$0.10	February 15, 2012
February 29, 2012	\$0.10	March 15, 2012
March 31, 2012	\$0.10	April 16, 2012
April 30, 2012	\$0.10	May 15, 2012
May 31, 2012	\$0.10	June 15, 2012
June 30, 2012	\$0.10	July 16, 2012
July 31, 2012	\$0.10	August 15, 2012
August 31, 2012	\$0.10	September 17, 2012
September 30, 2012	\$0.10	October 15, 2012
October 31, 2012	\$0.06	November 15, 2012
November 30, 2012	\$0.06	December 17, 2012
December 31, 2012	\$0.06	January 15, 2013
Total	\$1.08	

<b>For the Month Ended</b>	<b>Dividends per Common Share</b>	<b>Payment Date</b>
January 31, 2011	\$0.14	February 15, 2011
February 28, 2011	\$0.14	March 15, 2011
March 31, 2011	\$0.14	April 15, 2011
April 30, 2011	\$0.14	May 16, 2011
May 31, 2011	\$0.14	June 15, 2011
June 30, 2011	\$0.14	July 15, 2011
July 31, 2011	\$0.14	August 15, 2011
August 31, 2011	\$0.14	September 15, 2011
September 30, 2011	\$0.14	October 17, 2011
October 31, 2011	\$0.10	November 15, 2011
November 30, 2011	\$0.10	December 15, 2011
December 31, 2011	\$0.10	January 16, 2012
Total	\$1.56	

<b>For the Month Ended</b>	<b>Distributions per Trust Unit</b>	<b>Payment Date</b>
January 31, 2010	\$0.18	February 15, 2010
February 28, 2010	\$0.18	March 15, 2010
March 31, 2010	\$0.18	April 15, 2010
April 30, 2010	\$0.18	May 17, 2010
May 31, 2010	\$0.18	June 15, 2010
June 30, 2010	\$0.18	July 15, 2010
July 31, 2010	\$0.18	August 16, 2010
August 31, 2010	\$0.18	September 15, 2010
September 30, 2010	\$0.18	October 15, 2010
October 31, 2010	\$0.18	November 15, 2010
November 30, 2010	\$0.18	December 15, 2010
December 31, 2010	\$0.18	January 17, 2011
Total	\$2.16	

## MARKET FOR SECURITIES

### Common Shares

The Common Shares are listed and posted for trading on the TSX under the trading symbol "ZAR". The Common Shares commenced trading on the TSX on January 7, 2011 following completion of the Arrangement. The following table sets forth the high and low trading prices and the aggregate volume of trading of the Common Shares, as reported by the TSX for the periods indicated.

<u>Period</u>	<u>High</u>	<u>Low</u>	<u>Volume</u>
<b><u>2012</u></b>			
January	15.16	13.64	1,308,826
February	15.99	14.50	1,266,529
March	15.24	13.76	946,826
April	14.40	11.74	1,338,902
May	13.30	9.71	1,332,816
June	10.86	8.15	1,349,049
July	8.89	7.32	1,905,680
August	9.58	7.25	1,617,604
September	9.43	8.40	878,401
October	9.21	8.25	904,125
November	8.88	7.62	890,794
December	8.40	7.66	1,180,223
<b><u>2013</u></b>			
January	8.59	7.74	1,012,319
February	7.96	6.36	1,194,450
March (1 – 12)	7.21	6.66	410,048

In connection with the Arrangement, holders of Trust Units and Exchangeable Shares exchanged their Trust Units and Exchangeable Shares for Common Shares. Prior to the Arrangement, the Trust Units and Exchangeable Shares were listed and traded on the TSX. The trading symbol for the Trust Units was ZAR.UN and for the Exchangeable Shares was ZOG.B.

### Convertible Debentures

The Convertible Debentures are listed and posted for trading on the TSX under the trading symbol "ZAR.DB". The Convertible Debentures commenced trading on the TSX on May 1, 2012. The following table sets forth the high and low trading prices and the aggregate volume of trading of the Convertible Debentures, as reported by the TSX for the periods indicated.

<u>Period</u>	<u>High</u>	<u>Low</u>	<u>Volume</u>
<b><u>2012</u></b>			
May	101.20	98.50	71,060
June	99.70	96.00	18,680
July	100.27	98.00	13,970
August	100.50	99.15	12,940
September	100.00	98.75	8,120
October	100.49	99.75	13,100
November	100.60	99.55	10,530
December	100.40	98.14	8,010
<b><u>2013</u></b>			
January	103.74	99.00	8,630
February	101.11	99.21	11,350
March (1 – 12)	99.50	99.04	3,550

## INDUSTRY CONDITIONS

Companies operating in the oil and natural gas industry are subject to extensive regulation and control of operations (including land tenure, exploration, development, production, refining and upgrading, transportation, and marketing) as a result of legislation enacted by various levels of government and with respect to the pricing and taxation of oil and natural gas through agreements among the governments of Canada, Alberta and Saskatchewan, all of which should be carefully considered by investors in the oil and gas industry. It is not expected that any of these regulations or controls will affect our operations in a manner materially different than they will affect other oil and natural gas companies of similar size. All current legislation is a matter of public record and we are unable to predict what additional legislation or amendments may be enacted. Outlined below are some of the principal aspects of legislation, regulations and agreements governing the oil and gas industry in western Canada.

### Pricing and Marketing

#### *Oil*

The producers of oil are entitled to negotiate sales contracts directly with oil purchasers, with the result that the market determines the price of oil. Worldwide supply and demand primarily determines oil prices. The specific price depends in part on oil quality, prices of competing fuels, distance to market, the availability of transportation, value of refined products, the supply/demand balance and contractual terms of sale. Oil exporters are also entitled to enter into export contracts with terms not exceeding one year in the case of light crude oil and two years in the case of heavy crude oil, provided that an order approving such export has been obtained from the National Energy Board of Canada (the "**NEB**"). Any oil export to be made pursuant to a contract of longer duration (to a maximum of 25 years) requires an exporter to obtain an export licence from the NEB. The NEB is currently undergoing a consultation process to update the current regulations governing the issuance of export licences. The updating process is necessary to meet the criteria set out in the federal *Jobs, Growth and Long-term Prosperity Act* which received Royal Assent on June 29, 2012 (the "**Prosperity Act**"). In this transitory period, the NEB has issued, and is currently following an "Interim Memorandum of Guidance concerning Oil and Gas Export Applications and Gas Import Applications under Part VI of the *National Energy Board Act*".

#### *Natural Gas*

Alberta's natural gas market has been deregulated since 1985. Supply and demand determine the price of natural gas and price is calculated at the sale point, being the wellhead, the outlet of a gas processing plant, on a gas transmission system such as the Alberta "NIT" (Nova Inventory Transfer), at a storage facility, at the inlet to a utility system or at the point of receipt by the consumer. Accordingly, the price for natural gas is dependent upon such producer's own arrangements (whether long or short term contracts and the specific point of sale). As natural gas is also traded on trading platforms such as the Natural Gas Exchange (NGX) or the New York Mercantile Exchange (NYMEX) in the United States, spot and future prices can be set by such supply and demand. Natural gas exported from Canada is subject to regulation by the NEB and the Government of Canada. Exporters are free to negotiate prices and other terms with purchasers, provided that the export contracts must continue to meet certain other criteria prescribed by the NEB and the Government of Canada. Natural gas (other than propane, butane and ethane) exports for a term of less than two years or for a term of two to 20 years (in quantities of not more than 30,000 m<sup>3</sup>/day) must be made pursuant to an NEB order. Any natural gas export to be made pursuant to a contract of longer duration (to a maximum of 25 years) or for a larger quantity requires an exporter to obtain an export licence from the NEB.

The governments of Alberta and Saskatchewan also regulate the volume of natural gas that may be removed from those provinces for consumption elsewhere based on such factors as reserve availability, transportation arrangements and market considerations.

## **Pipeline Capacity**

From time to time, pipeline operators will limit the amount of product shipped. A typical reason may be limited ability for purchasers to accept product or there have been limitations imposed due to a pipeline taken out of service for planned or unplanned outages.

## **The North American Free Trade Agreement**

The North American Free Trade Agreement ("**NAFTA**") among the governments of Canada, the United States and Mexico became effective on January 1, 1994. In the context of energy resources, Canada continues to remain free to determine whether exports of energy resources to the United States or Mexico will be allowed, provided that any export restrictions do not: (i) reduce the proportion of energy resources exported relative to the total supply of goods of the party maintaining the restriction as compared to the proportion prevailing in the most recent 36 month period; (ii) impose an export price higher than the domestic price (subject to an exception with respect to certain measures which only restrict the volume of exports); and (iii) disrupt normal channels of supply.

All three signatory countries are prohibited from imposing a minimum or maximum export price requirement in any circumstance where any other form of quantitative restriction is prohibited. The signatory countries are also prohibited from imposing a minimum or maximum import price requirement except as permitted in enforcement of countervailing and anti-dumping orders and undertakings. NAFTA requires energy regulators to ensure the orderly and equitable implementation of any regulatory changes and to ensure that the application of those changes will cause minimal disruption to contractual arrangements and avoid undue interference with pricing, marketing and distribution arrangements, all of which are important for Canadian oil and natural gas exports. NAFTA contemplates the reduction of Mexican restrictive trade practices in the energy sector and prohibits discriminatory border restrictions and export taxes.

## **Royalties and Incentives**

### ***General***

In addition to federal regulation, each province has legislation and regulations which govern royalties, production rates and other matters. The royalty regime in a given province is a significant factor in the profitability of oil sands projects, crude oil, natural gas liquids, sulphur and natural gas production. Royalties payable on production from lands other than Crown lands are determined by negotiation between the mineral freehold owner and the lessee, although production from such lands is subject to certain provincial taxes and royalties. Royalties from production on Crown lands are determined by governmental regulation and are generally calculated as a percentage of the value of gross production. The rate of royalties payable generally depends in part on prescribed reference prices, well productivity, geographical location, field discovery date, method of recovery and the type or quality of the petroleum product produced. Other royalties and royalty-like interests are, from time to time, carved out of the working interest owner's interest through non-public transactions. These are often referred to as overriding royalties, gross overriding royalties, net profits interests, or net carried interests.

Occasionally the governments of the western Canadian provinces create incentive programs for exploration and development. Such programs often provide for royalty rate reductions, royalty holidays or royalty tax credits and are generally introduced when commodity prices are low to encourage exploration and development activity by improving earnings and cash flow within the industry.

### ***Alberta***

Producers of oil and natural gas from Crown lands in Alberta are required to pay annual rental payments, currently at a rate of \$3.50 per hectare, and make monthly royalty payments in respect of oil and natural gas produced.

Royalties are currently paid pursuant to "The New Royalty Framework" (implemented by the *Mines and Minerals (New Royalty Framework) Amendment Act, 2008*) and the "Alberta Royalty Framework", which was implemented in 2010.

Royalty rates for conventional oil are set by a single sliding rate formula, which is applied monthly and incorporates separate variables to account for production rates and market prices. Effective January 1, 2011, the maximum royalty payable under the royalty regime was set at 40%. The royalty curve for conventional oil announced on May 27, 2010 amends the price component of the conventional oil royalty formula to moderate the increase in the royalty rate at prices higher than \$535/m<sup>3</sup> compared to the previous royalty curve.

Royalty rates for natural gas under the royalty regime are similarly determined using a single sliding rate formula incorporating separate variables to account for production rates and market prices. Effective January 1, 2011, the maximum royalty payable under the royalty regime was set at 36%. The royalty curve for natural gas announced on May 27, 2010 amends the price component of the natural gas royalty formula to moderate the increase in the royalty rate at prices higher than \$5.25/GJ compared to the previous royalty curve.

Oil sands projects are also subject to the Alberta's royalty regime. Prior to payout of an oil sands project, the royalty is payable on gross revenues of an oil sands project. Gross revenue royalty rates range between 1-9% depending on the market price of oil, determined using the average monthly price, expressed in Canadian dollars, for WTI crude oil and Cushing, Oklahoma: rates are 1% when the market price of oil is less than or equal to \$55 per barrel and increase for every dollar of market price of oil increase to a maximum of 9% when oil is priced at \$120 or higher. After payout, the royalty payable is the greater of the gross revenue royalty based on the gross revenue royalty rate of 1-9% and the net revenue royalty based on the net revenue royalty rate. Net revenue royalty rates start at 25% and increase for every dollar of market price of oil increase above \$55 up to 40% when oil is priced at \$120 or higher. In addition, concurrently with the implementation of the New Royalty Framework, the Government of Alberta renegotiated existing contracts with certain oil sands producers that were not compatible with the current royalty regime.

Producers of oil and natural gas from freehold lands in Alberta are required to pay annual freehold production taxes. The level of the freehold production tax is based on the volume of monthly production and a specified rate of tax for both oil and gas.

The Innovative Energy Technologies Program (the "**IETP**"), which is currently in place, has the stated objectives of increasing recovery from oil and gas deposits, finding technical solutions to the gas over bitumen issue, improving the recovery of bitumen by in-situ and mining techniques and improving the recovery of natural gas from coal seams. The IETP provides royalty adjustments to specific pilot and demonstration projects that utilize new or innovative technologies to increase recovery from existing reserves.

The Government of Alberta currently has in place two royalty programs, both of which commenced in 2008 with the intention to encourage the development of deeper, higher cost oil and gas reserves. A five-year program for conventional oil exploration wells over 2,000 metres provides qualifying wells with up to a \$1 million or 12 months of royalty relief, whichever comes first, and a five-year program for natural gas wells deeper than 2,500 metres provides a sliding scale royalty credit based on depth of up to \$3,750 per metre. On May 27, 2010, the natural gas deep drilling program was amended, retroactive to May 1, 2010, by reducing the minimum qualifying depth to 2,000 metres, removing a supplemental benefit of \$875,000 for wells exceeding 4,000 metres that are spudded subsequent to that date, and including wells drilled into pools drilled prior to 1985, among other changes.

On November 19, 2008, the Government of Alberta announced the introduction of a five-year program of transitional royalty rates with the intent of promoting new drilling. The five-year transition option is designed to provide lower royalties at certain price levels in the initial years of a well's life when production rates are expected to be the highest. Under this program, companies drilling new natural gas or conventional deep oil wells between 1,000 and 3,500 metres receive a one-time option, on a well-by-well basis, to adopt either the new transitional royalty rates or those outlined in the royalty regime. These options expired on February 15, 2011 and on January 1, 2014, all producers operating under the transitional royalty rates will automatically become subject to the royalty regime. Production from wells operating under the transitional royalty rates will not be subject to the royalty curves for conventional oil and natural gas.

On March 17, 2011, the Government of Alberta approved the *New Well Royalty Regulation* providing for the permanent implementation of a formerly temporary royalty program which provides for a maximum 5% royalty rate for eligible new wells for the first 12 productive months or until the regulated "volume cap" is reached.

In addition to the foregoing, the Government of Alberta has implemented certain initiatives intended to accelerate technological development and facilitate the development of unconventional resources (the "**Emerging Resource and Technologies Initiative**"). Specifically:

- Coalbed methane wells will receive a maximum royalty rate of 5% for 36 producing months on up to 750 MMcf of production, retroactive to wells that began producing on or after May 1, 2010;
- Shale gas wells will receive a maximum royalty rate of 5% for 36 producing months with no limitation on production volume, retroactive to wells that began producing on or after May 1, 2010;
- Horizontal gas wells will receive a maximum royalty rate of 5% for 18 producing months on up to 500 MMcf of production, retroactive to wells that commenced drilling on or after May 1, 2010; and
- Horizontal oil wells and horizontal non-project oil sands wells will receive a maximum royalty rate of 5% with volume and production month limits set according to the depth of the well (including the horizontal distance), retroactive to wells that commenced drilling on or after May 1, 2010.

The Emerging Resource and Technologies Initiative will be reviewed in 2014, and the Government of Alberta has committed to providing industry with three years notice at that time if it decides to discontinue the program.

### **Saskatchewan**

In Saskatchewan, the amount payable as Crown royalty or freehold production tax in respect of oil depends on the type and vintage of oil, the quantity of oil produced in a month, the value of the oil produced and specified adjustment factors determined monthly by the provincial government. For Crown royalty and freehold production tax purposes, conventional oil is divided into "types", being "heavy oil", "southwest designated oil" or "non-heavy oil other than southwest designated oil". The conventional royalty and production tax classifications ("fourth tier oil", "third tier oil", "new oil" and "old oil") depend on the finished drilling date of a well and are applied to each of the three crude oil types slightly differently. Heavy oil is classified as third tier oil (having a finished drilling date on or after January 1, 1994 and before October 1, 2004), fourth tier oil (having a finished drilling date on or after October 1, 2002 or incremental oil from new or expanded waterflood projects) or new oil (oil from wells drilled on or after January 1, 1994). Southwest designated oil uses the same definitions of third and fourth tier oil but new oil is defined as conventional oil produced from a horizontal well having a finished drilling date on or after February 9, 1998 and before October 1, 2002. For non-heavy oil other than southwest designated oil, the same classification is used but new oil is defined as conventional oil produced from a vertical well completed after 1973 and having a finished drilling date prior to 1994, whereas old oil is defined as conventional oil not classified as third or fourth tier oil or new oil. Production tax rates for freehold production are determined by first determining the Crown royalty rate and then subtracting the "Production Tax Factor" ("**PTF**") applicable to that classification of oil. Currently the PTF is 6.9 for "old oil", 10.0 for "new oil" and "third tier oil" and 12.5 for "fourth tier oil". The minimum rate for freehold production tax is zero.

Base prices are used to establish lower limits in the price-sensitive royalty structure for conventional oil and apply at a reference well production rate of 100 m<sup>3</sup> for "old oil", "new oil" and "third tier oil", and 250 m<sup>3</sup> per month for "fourth tier oil". Where average wellhead prices are below the established base prices of \$100 per m<sup>3</sup> for third and fourth tier oil and \$50 per m<sup>3</sup> for new oil and old oil, base royalty rates are applied. Base royalty rates are 5% for all fourth tier oil, 10% for heavy oil that is third tier oil or new oil, 12.5% for southwest designated oil that is third tier oil or new oil, 15% for non-heavy oil other than southwest designated oil that is third tier or new oil, and 20% for old oil. Where average wellhead prices are above base prices, marginal royalty rates are applied to the proportion of production that is above the base oil price. Marginal royalty rates are 30% for all fourth tier oil, 25% for heavy oil that is third tier oil or new oil, 35% for southwest designated oil that is third tier oil or new oil, 35% for non-heavy oil other than southwest designated oil that is third tier or new oil, and 45% for old oil.

The amount payable as Crown royalty or freehold production tax in respect of natural gas production is determined by a sliding scale based on the actual price received, the quantity produced in a given month, the type of natural gas, and the classification of the natural gas. Like conventional oil, natural gas may be classified as "non-associated gas" (gas produced from gas wells) or "associated gas" (gas produced from oil wells) and royalty rates are determined according to the finished drilling date of the respective well. Non-associated gas is classified as new gas (having a finished drilling date before February 9, 1998 with a first production date on or after October 1, 1976), third tier gas (having a finished drilling date on or after February 9, 1998 and before October 1, 2002), fourth tier gas (having a finished drilling date on or after October 1, 2002) and old gas (not classified as either third tier, fourth tier or new gas). A similar classification is used for associated gas except that the classification of old gas is not used, the definition of fourth tier gas also includes production from oil wells with a finished drilling date prior to October 1, 2002, where the individual oil well has a gas-oil production ratio in any month of more than 3,500 m<sup>3</sup> of gas for every m<sup>3</sup> of oil, and new gas is defined as oil produced from a well with a finished drilling date before February 9, 1998 that received special approval, prior to October 1, 2002, to produce oil and gas concurrently without gas-oil ratio penalties. Natural gas liquids and by-products recovered at gas processing plants are not subject to a royalty. Gas liquids which are produced and measured at the wellhead are treated as crude oil for royalty purposes.

On December 9, 2010, the Government of Saskatchewan enacted the *Freehold Oil and Gas Production Tax Act, 2010* with the intention to facilitate the efficient payment of freehold production taxes by industry. Two new regulations with respect to this legislation are: (i) *The Freehold Oil and Gas Production Tax Regulations, 2012* which sets out the terms and conditions under which the taxes are calculated and paid; and (ii) *The Recovered Crude Oil Tax Regulations, 2012* which sets out the terms and conditions under which taxes on recovered crude oil that was delivered from a crude oil recovery facility on or after March 1, 2012 are to be calculated and paid.

As with conventional oil production, base prices based on a well reference rate of 250 10<sup>3</sup> m<sup>3</sup>/month are used to establish lower limits in the price-sensitive royalty structure for natural gas. Where average field-gate prices are below the established base prices of \$50 per thousand m<sup>3</sup> for third and fourth tier gas and \$35 per thousand m<sup>3</sup> for new gas and old gas, base royalty rates are applied. Base royalty rates are 5% for all fourth tier gas, 15% for third tier or new gas, and 20% for old gas. Where average well-head prices are above base prices, marginal royalty rates are applied to the proportion of production that is above the base gas price. Marginal royalty rates are 30% for all fourth tier gas, 35% for third tier and new gas, and 45% for old gas. The current regulatory scheme provides for certain differences with respect to the administration of "fourth tier gas" which is associated gas.

The Government of Saskatchewan currently provides a number of targeted incentive programs. These include both royalty reduction and incentive volume programs, including the following:

- *Royalty/Tax Incentive Volumes for Vertical Oil Wells Drilled on or after October 1, 2002* providing reduced Crown royalty (a Crown royalty rate of the lesser of "fourth tier oil" Crown royalty rate and 2.5%) and freehold tax rates (a freehold production tax rate of 0%) on incentive volumes of 8,000 m<sup>3</sup> for deep development vertical oil wells, 4,000 m<sup>3</sup> for non-deep exploratory vertical oil wells and 16,000 m<sup>3</sup> for deep exploratory vertical oil wells (more than 1,700 metres or within certain formations) and after the incentive volume is produced, the oil produced will be subject to the "fourth tier" royalty tax rate;
- *Royalty/Tax Incentive Volumes for Exploratory Gas Wells Drilled on or after October 1, 2002* providing reduced Crown royalty (a Crown royalty rate of the lesser of "fourth tier oil" Crown royalty rate and 2.5%) and freehold tax rates (a freehold production tax rate of 0%) on incentive volumes of 25,000,000 m<sup>3</sup> for qualifying exploratory gas wells;
- *Royalty/Tax Incentive Volumes for Horizontal Oil Wells Drilled on or after October 1, 2002* providing reduced Crown royalty (a Crown royalty rate of the lesser of "fourth tier oil" Crown royalty rate and 2.5%) and freehold tax rates on incentive volumes of 6,000 m<sup>3</sup> for non-deep horizontal oil wells and 16,000 m<sup>3</sup> for deep horizontal oil wells (more than 1,700 metres or within certain formations) and after the incentive volume is produced, the oil produced will be subject to the "fourth tier" royalty tax rate;

- *Royalty/Tax Incentive Volumes for Horizontal Gas Wells drilled on or after June 1, 2010 and before April 1, 2013* providing for a classification of the well as a qualifying exploratory gas well and resulting in a reduced Crown royalty (a Crown royalty rate of the lesser of "fourth tier oil" Crown royalty rate and 2.5%) and freehold tax rates (a freehold production tax rate of 0%) on incentive volumes of 25,000,000 m<sup>3</sup> for horizontal gas wells and after the incentive volume is produced, the gas produced will be subject to the "fourth tier" royalty tax rate;
- *Royalty/Tax Regime for Incremental Oil Produced from New or Expanded Waterflood Projects Implemented on or after October 1, 2002* whereby incremental production from approved waterflood projects is treated as fourth tier oil for the purposes of Crown royalty and freehold tax calculations;
- *Royalty/Tax Regime for Enhanced Oil Recovery Projects (Excluding Waterflood Projects) Commencing prior to April 1, 2005* providing lower Crown royalty and freehold tax determinations based in part on the profitability of EOR projects during and subsequent to the payout of the EOR operations;
- *Royalty/Tax Regime for Enhanced Oil Recovery Projects (Excluding Waterflood Projects) Commencing on or after April 1, 2005* providing a Crown royalty of 1% of gross revenues on enhanced oil recovery projects pre-payout and 20% of EOR operating income post-payout and a freehold production tax of 0% pre-payout and 8% post-payout on operating income from EOR projects; and
- *Royalty/Tax Regime for High Water-Cut Oil Wells* designed to extend the product lives and improve the recovery rates of high water-cut oil wells and granting "third tier oil" royalty/tax rates to incremental high water-cut oil production resulting from qualifying investments made to rejuvenate eligible oil wells and/or associated facilities.

In 1975, the Government of Saskatchewan introduced a Royalty Tax Rebate ("**RTR**") as a response to the Government of Canada disallowing Crown royalties and similar taxes as a deductible business expense for income tax purposes. As of January 1, 2007, the remaining balance of any unused RTR is limited in its carry forward to seven years because of the Government of Canada's initiative to reintroduce the full deduction of provincial resource royalties from federal and provincial taxable income.

On June 22, 2011, the Government of Saskatchewan released the Upstream Petroleum Industry Associated Gas Conservation Standards, which are designed to reduce emissions resulting from the flaring and venting of associated gas (the "**Associated Natural Gas Standards**"). The Associated Natural Gas Standards were jointly developed with industry and the implementation of such standards commenced on July 1, 2012 for new wells and facilities licensed on or after such date. These will apply to existing licensed wells and facilities on July 1, 2015.

## **Land Tenure**

The respective provincial governments predominantly own crude oil and natural gas located in the western provinces. Provincial governments grant rights to explore for and produce oil and natural gas pursuant to leases, licences, and permits for varying terms, and on conditions set forth in provincial legislation including requirements to perform specific work or make payments. Private ownership of oil and natural gas also exists in such provinces and rights to explore for and produce such oil and natural gas are granted by lease on such terms and conditions as may be negotiated.

Each of the provinces of Alberta and Saskatchewan has implemented legislation providing for the reversion to the Crown of mineral rights to deep, non-productive geological formations at the conclusion of the primary term of a lease or license.

Alberta also has a policy of "shallow rights reversion" which provides for the reversion to the Crown of mineral rights to shallow, non-productive geological formations for all leases and licenses. For leases and licenses issued subsequent to January 1, 2009, shallow rights reversion will be applied at the conclusion of the primary term of the



lease or license. Holders of leases or licences that have been continued indefinitely prior to January 1, 2009 will receive a notice regarding the reversion of the shallow rights, which will be implemented three years from the date of the notice. Leases and licences granted prior to January 1, 2009, but continued after that date, are not subject to shallow rights reversion until they continue past their primary term (at which time the application of deep rights reversion occurs). Afterwards, the holders of such agreements will be served with shallow rights reversion notices based on vintage and location similar to leases and licences that were already continued as of January 1, 2009. The order in which these agreements will receive reversion notices will depend on their vintage and location.

### **Environmental Regulation**

The oil and natural gas industry is currently subject to environmental regulations pursuant to a variety of provincial and federal legislation, all of which is subject to governmental review and revision from time to time. Such legislation provides for restrictions and prohibitions on the release or emission of various substances produced in association with certain oil and gas industry operations, such as sulphur dioxide and nitrous oxide. In addition, such legislation sets out the requirements for the satisfactory abandonment and reclamation of well and facility sites. Compliance with such legislation can require significant expenditures and a breach of such requirements may result in suspension or revocation of necessary licenses and authorizations, civil liability for pollution damage, and the imposition of material fines and penalties.

On a Federal level and pursuant to the *Prosperity Act*, the Government of Canada amended or appealed several pieces of federal environmental legislation and in addition, created a new federal environment assessment regime. The changes to the environmental legislation under the *Prosperity Act* are intended to provide for more efficient and timely environmental assessments of projects that previously had been subject to overlapping legislative jurisdiction.

In December 2008, the Government of Alberta released a new land use policy for surface land in Alberta, the Alberta Land Use Framework (the "**ALUF**"). The ALUF sets out an approach to manage public and private land use and natural resource development in a manner that is consistent with the long-term economic, environmental and social goals of the province. It calls for the development of region-specific land use plans in order to manage the combined impacts of existing and future land use within a specific region and the incorporation of a cumulative effects management approach into such plans.

The *Alberta Land Stewardship Act* (the "**ALSA**") was proclaimed in force in Alberta on October 1, 2009 and provides the legislative authority for the Government of Alberta to implement the policies contained in the ALUF. Regional plans established pursuant to the ALSA will be deemed to be legislative instruments equivalent to regulations and will be binding on the Government of Alberta and provincial regulators, including those governing the oil and gas industry. In the event of a conflict or inconsistency between a regional plan and another regulation, regulatory instrument or statutory consent, the regional plan will prevail. Further, the ALSA requires local governments, provincial departments, agencies and administrative bodies or tribunals to review their regulatory instruments and make any appropriate changes to ensure that they comply with an adopted regional plan. The ALSA also contemplates the amendment or extinguishment of previously issued statutory consents such as regulatory permits, leases, licenses, approvals and authorizations for the purpose of achieving or maintaining an objective or policy resulting from the implementation of a regional plan. Among the measures to support the goals of the regional plans contained in the ALSA are conservation easements, which can be granted for the protection, conservation and enhancement of land; and conservation directives, which are explicit declarations contained in a regional plan to set aside specified lands in order to protect, conserve, manage and enhance the environment.

On August 22, 2012, the Government of Alberta approved the Lower Athabasca Regional Plan ("**LARP**") which came into effect on September 1, 2012. The LARP covers approximately 93,212 square kilometres and is in the northeast corner of Alberta. The region includes a substantial portion of the Athabasca oilsands area, which contains approximately 82% of the province's oilsands resource and much of the Cold Lake oilsands area. LARP establishes six new conservation areas, bringing the total conserved land in the region to two million hectares, or 22%—an area three times the size of Banff National Park. The Alberta government plans to pay \$30 million to producers whose leases will be cancelled in areas set aside for conservation. Oil and gas companies will be allowed to continue to operate in conservation and recreation areas while oilsands companies' tenures will be cancelled. New petroleum and gas tenure sold in conservation areas will include a restriction that prohibits surface access. Application procedures for activities and facilities in the LARP, regulated by the Energy Resources Conservation Board and the

Alberta Utilities Commission, respectively, have been changed to accommodate the new restrictions set out in the LARP. The LARP is the first of seven regions to get a land use plan. The next will be the South Saskatchewan region.

In May of 2011, Saskatchewan passed changes to *The Oil and Gas Conservation Act* ("**SKOGCA**"), the act governing the regulation of resource development operations in the province. Although the associated Bill received Royal Assent on May 18, 2011, it was not proclaimed into force until April 1, 2012, in conjunction with the release of *The Oil and Gas Conservation Regulations, 2012* ("**OGCR**") and *The Petroleum Registry and Electronic Documents Regulations* ("**Registry Regulations**"). The aim of the amendments to the SKOGCA, and associated regulations, is to provide resource companies investing in Saskatchewan's energy and resource industries with the best support services and business and regulatory systems available. With the enactment of the Registry Regulations and the OGCR, Saskatchewan has implemented a number of operational aspects, including the increased demand for record-keeping, increased testing requirements for injection wells and increased investigation and enforcement powers; and, procedural aspects including those related to Saskatchewan's participation as partner in the Petroleum Registry of Alberta.

## **Climate Change Regulation**

### *Federal*

On April 26, 2007, the Government of Canada released "Turning the Corner: An Action Plan to Reduce Greenhouse Gases and Air Pollution" (the "**Action Plan**") which set forth a plan for regulations to address both green house gases ("**GHGs**") and air pollution. An update to the Action Plan, "Turning the Corner: Regulatory Framework for Industrial Greenhouse Gas Emissions" was released on March 10, 2008 (the "**Updated Action Plan**"). The Updated Action Plan outlines emissions intensity-based targets, which will be applied to regulated sectors on either a facility-specific, sector-wide or company-by-company basis. Facility-specific targets apply to the upstream oil and gas, oil sands, petroleum refining and natural gas pipelines sectors. Unless a minimum regulatory threshold applies, all facilities within a regulated sector will be subject to the emissions intensity targets. Although the intention was for draft regulations for the implementation of the Updated Action Plan to become binding on January 1, 2010, the only regulations announced pertain to carbon dioxide emissions from coal-fired generation of electricity (finalized in summer 2012). Further, representatives of the Government of Canada have indicated that the proposals contained in the Updated Action Plan will be modified to ensure consistency with the direction ultimately taken by the United States with respect to GHG emissions regulation. As a result, it is unclear to what extent implementation of the proposals contained in the Updated Action Plan will occur.

The United States Environmental Protection Agency (the "**EPA**") has indicated its intention to impose GHG emissions standards for fossil fuel-fired power plants by specifying that it would issue final regulations by May 26, 2012, and with respect to refineries, specifying that it will issue proposed regulations by December 10, 2011 and finalized regulations by November 10, 2012. The EPA did not meet the December 10, 2011 deadline and it is unclear whether the EPA will also miss the finalized regulations deadline. However, in March 2012, the EPA proposed a strict GHG standard on new power plants only. While it is expected that this rule could encourage building new natural gas power plants rather than coal plants, the actual effect of the new rule will not be able to be quantified for some time.

### *Alberta*

Alberta enacted the *Climate Change and Emissions Management Act* (the "**CCEMA**") on December 4, 2003, amending it through the *Climate Change and Emissions Management Amendment Act*, which received royal assent on November 4, 2008. The CCEMA is based on an emissions intensity approach similar to the Updated Action Plan and aims for a 50% reduction from 1990 emissions relative to GDP by 2020.

Alberta facilities emitting more than 100,000 tonnes of GHGs a year are subject to compliance with the CCEMA. Similar to the Updated Action Plan, the CCEMA and the associated *Specified Gas Emitters Regulation* make a distinction between "Established Facilities" and "New Facilities". Established Facilities are defined as facilities that completed their first year of commercial operation prior to January 1, 2000 or that have completed eight or more

years of commercial operation. Established Facilities are required to reduce their emissions intensity to 88% of their baseline for 2008 and subsequent years, with their baseline being established by the average of the ratio of the total annual emissions to production for the years 2003 to 2005. New Facilities are defined as facilities that completed their first year of commercial operation on December 31, 2000, or a subsequent year, and have completed less than eight years of commercial operation, or are designated as New Facilities in accordance with the *Specified Gas Emitters Regulation*. New Facilities are required to reduce their emissions intensity by 2% from baseline in the fourth year of commercial operation, 4% of baseline in the fifth year, 6% of baseline in the sixth year, 8% of baseline in the seventh year, and 10% of baseline in the eighth year. Unlike the Updated Action Plan, the CCEMA does not contain any provision for continuous annual improvements in emissions intensity reductions beyond those stated above.

The CCEMA contains compliance mechanisms that are similar to the Updated Action Plan. Regulated emitters can meet their emissions intensity targets by contributing to the Climate Change and Emissions Management Fund (the "**Fund**") at a rate of \$15 per tonne of CO<sub>2</sub> equivalent. Unlike the Updated Action Plan, CCEMA contains no provisions for an increase to this contribution rate. Emissions credits can be purchased from regulated emitters that have reduced their emissions below the 100,000 tonne threshold or non-regulated emitters that have generated emissions offsets through activities that result in emissions reductions in accordance with established protocols published by the Government of Alberta.

We do not own or have a working interest in facilities that meet or are expected to exceed these emissions thresholds.

On December 2, 2010, the Government of Alberta passed the *Carbon Capture and Storage Statutes Amendment Act, 2010*. It deemed the pore space underlying all land in Alberta to be, and to have always been, the property of the Crown and provided for the assumption of long-term liability for carbon sequestration projects by the Crown, subject to the satisfaction of certain conditions.

### ***Saskatchewan***

On May 11, 2009, the Government of Saskatchewan announced *The Management and Reduction of Greenhouse Gases Act* (the "**MRGGA**") to regulate GHG emissions in the province. The MRGGA received Royal Assent on May 20, 2010 and will come into force on proclamation. Regulations under the MRGGA have also yet to be proclaimed, but draft versions indicate that Saskatchewan will adopt the goal of a 20% reduction in GHG emissions from 2006 levels by 2020.

## **RISK FACTORS**

An investment in our Common Shares is subject to various risks including those risks inherent to the industry in which we operate. If any of these risks occur, our production, revenues and financial condition could be materially harmed, with a resulting decrease in dividends on, and the market price of, the Common Shares. As a result, the trading price of our Common Shares could decline, and you could lose all or part of your investment. Cash dividends to Shareholders are not assured or guaranteed.

You should carefully consider the following risk factors, as well as the other information contained in this Annual Information Form and our other public filings before making an investment decision. If any of the risks described below materialize, our business, financial condition or results of operations could be materially and adversely affected. Additional risks and uncertainties not currently known to us that we currently view as immaterial may also materially and adversely affect our business, financial condition or results of operations. Residents of the United States and other non-residents of Canada should have additional regard to the risk factors under the heading "*Certain Risks for United States and Other Non-Resident Shareholders*".

The information set forth below contains "forward-looking statements", which are qualified by the information contained in the section of this Annual Information Form entitled "*Notice to Reader – Special Note Regarding Forward-Looking Statements*".

## **Risks Relating to Our Business and Operations**

### ***Declines in oil and natural gas prices will adversely affect our financial condition***

Our operational results and financial condition, and therefore the amounts we pay to Shareholders as dividends, will be dependent on the prices received for our oil and natural gas production. Declines in oil and natural gas prices may result in declines in, or the elimination of, dividends to Shareholders.

Prices for oil and natural gas are subject to large fluctuations in response to relatively minor changes in the supply of and demand for oil and natural gas, market uncertainty and a variety of additional factors beyond our control. These factors include economic conditions, in the United States, Canada and Europe, the actions of OPEC, governmental regulation, political stability in the Middle East, Northern Africa and elsewhere, weather conditions including weather-related disruptions to the North American natural gas supply, the foreign supply of oil and natural gas, risks of supply disruption, the price of foreign imports and the availability of alternative fuel sources. Prices for oil and natural gas are also subject to the availability of foreign markets and our ability to access such markets. Any substantial and extended decline in the price of oil and natural gas would have an adverse effect on the carrying value of our proved and probable reserves, net asset value, borrowing capacity, revenues, profitability and funds from operations and ultimately on our financial condition and may, therefore, affect the amount of dividends that we pay to our Shareholders.

Oil and natural gas prices are expected to remain volatile for the near future because of market uncertainties over the supply and the demand of these commodities due to the current state of the world economies, OPEC actions, and sanctions imposed on certain oil producing nations by other countries and the ongoing credit and liquidity concerns.

The economics of producing from some wells may change as a result of lower commodity prices, which could result in reduced production of oil or natural gas and a reduction in the volumes of our reserves. We might also elect not to produce from certain wells at lower prices. Volatile oil and natural gas prices also make it difficult to estimate the value of producing properties for acquisitions and often cause disruption in the market for oil and natural gas producing properties, as buyers and sellers have difficulty agreeing on such value. Price volatility also makes it difficult to budget for and project the return on acquisitions and development and exploitation projects.

### ***Our ASP project will require substantial capital investment over the coming years***

In addition, there are certain additional risk factors associated with the development of our ASP project. These include the following:

#### ***Execution Risks***

There is a risk that construction of the facilities and infrastructure to support our ASP project will not be completed on time on budget. Additionally, there is a risk that the project may have delays, interruptions of operations or increased costs due to many factors, including, without limitation:

- inability to attract or retain sufficient numbers of qualified workers;
- breakdown or failure of equipment or processes;
- construction performance falling below expected levels of output or efficiency;
- design errors;
- non-performance by, or financial failure of, third-party contractors;
- labour disputes, disruptions or declines in productivity;
- increases in materials or labour costs;
- conditions imposed by regulatory approvals;
- delays induced by weather;
- errors in construction;
- changes in project scope;
- unforeseen site surface or subsurface conditions;
- transportation or construction accidents;

- permit requirement violation; and
- reservoir performance.

The information contained herein related to the ASP project, including, without limitation, reserve and economic evaluations, assumes receipt of all regulatory approvals and no material changes being made to the project or its scope.

The industry is in a period of substantial industrial activity. We will need to compete for equipment, supplies, services, and labour in this environment which could result in increased costs, shortages of goods and services that delay progress, or both. Increased competition for equipment, materials and labour may result in increased costs that could have a material adverse effect on our business, financial condition or results of operations. As such, there are risks associated with project cost estimates provided by us. Cost estimates are provided prior to completion of detailed engineering needed to reduce the margin of error. Accordingly, actual costs may vary from estimates and these differences may be material.

### *Operating Costs*

The operating costs of the project have the potential to vary considerably throughout the operating period and will be significant components of the cost of production of any petroleum products produced by the project. Project economics and our overall earnings may be reduced if increases in operating costs are incurred. Factors which could affect operating costs include, without limitation;

- the amount and cost of labour to operate the project;
- the cost of chemicals;
- the cost of electricity;
- power outages, particularly in winter when freeze-ups could occur;
- reliability of the facilities;
- the maintenance cost of the facilities;
- the cost of insurance; and
- catastrophic events such as fires, earthquakes, storms or explosions.

The market for heavy oil is more limited than for light and medium grades of oil, making it more susceptible to supply and demand fundamentals. Future price differentials are uncertain and any increase in heavy oil differentials could have an adverse effect on the anticipated returns from the project as well as our overall business, financial condition, results of operations and cash flows.

### ***The amount of oil and natural gas that we can produce and sell is subject to the accessibility, availability, proximity and capacity of gathering, processing and pipeline systems***

We deliver our products through gathering, processing and pipeline systems some of which we do not own. Access to the pipeline capacity for the transport of crude oil into the United States has become inadequate for the amount of Canadian production being exported to the United States and has recently resulted in significantly lower amounts being realized by Canadian producers compared with the WTI price for crude oil. Although opportunities to move oil by rail continue to grow and will provide new outlets for access to North American refineries otherwise not reachable via existing pipeline infrastructure, supply in excess of current pipeline and refining capacity is expected to continue to exist. Although Zargon currently does not directly transport oil by rail, we could be affected by both positive and negative impacts (i.e. pricing of our oil sales from supply/demand issues) that could result from significant fluctuations to this transport method. Material structural changes are required to reduce these bottlenecks and the resulting steep price discounts. A variety of new pipeline expansion projects to provide increased access to eastern Canadian and Gulf Coast refineries, as well as new off-shore markets, have been announced and are in various stages of review and approval. There can be no assurance that such regulatory approvals will be secured on a timely basis or at all. The lack of firm pipeline capacity continues to affect the oil and natural gas industry and limit the ability to produce and to market oil and natural gas production. In addition, the pro-rationing of capacity on inter-provincial pipeline systems also continues to affect the ability to export oil and natural gas.

The lack of access to capacity in any of the gathering, processing and pipeline systems, and in particular the processing facilities, could result in our inability to realize the full economic potential of our production or in a reduction of the price offered for our production. Any significant change in market factors or other conditions affecting these infrastructure systems and facilities, as well as any delays in constructing new infrastructure systems and facilities could harm our business and, in turn, our financial condition.

A portion of our production may, from time to time, be processed through facilities owned by third parties and which we do not have control of. From time to time, these facilities may discontinue or decrease operations either as a result of normal servicing requirements or as a result of unexpected events. A discontinuance or decrease of operations could materially adversely affect our ability to process our production and to deliver the same for sale.

Certain pipeline leaks have gained media and other stakeholder attention and may result in additional regulation or changes in law which could impede the conduct of our business or make our operations more expensive.

***Our ability to maintain dividends is dependent on a number of factors, including volatility of prices for oil and natural gas, interest rates, sources of capital, changes in legislation and those set forth below***

Our ability to add to our petroleum and natural gas reserves is highly dependent on our success in exploiting existing properties and acquiring additional reserves. Our long-term commercial success depends on our ability to find, acquire, develop and commercially produce petroleum and natural gas reserves. Future oil and natural gas exploration may involve unprofitable efforts, not only from unsuccessful wells, but also from wells that are productive but do not produce sufficient petroleum substances to return a profit after drilling, completion (including hydraulic fracturing), operating and other costs. Completion of a well does not assure a profit on the investment or recovery of drilling, completion, operating and other costs. Drilling hazards or environmental damage could greatly increase the cost of operations (including hydraulic fracturing), and various field operating conditions may adversely affect the production from successful wells. These conditions include delays in obtaining governmental approvals or consents, shut-ins of connected wells resulting from extreme weather conditions, insufficient storage or transportation capacity or other geological and mechanical conditions. While diligent well supervision and effective maintenance operations can contribute to maximizing production rates over time, production delays and declines from normal field operating conditions cannot be eliminated and can be expected to adversely affect revenue and cash flow levels to varying degrees. New wells we drill or participate in may not become productive and we may not recover all or any portion of our investment in wells we drill or participate in. The cost of drilling, completing and operating a well is often uncertain, and cost factors can adversely affect the economics of a project.

Higher operating costs for our underlying properties will directly decrease the amount of cash flow received by us and, therefore, may reduce dividends to Shareholders. Labour costs, electricity, gas processing, well servicing and chemicals are a few of our operating costs that are susceptible to material fluctuation. There is no assurance that further commercial quantities of petroleum and natural gas will be discovered or acquired by us.

The level of production from our existing properties may decline at rates greater than anticipated due to unforeseen circumstances, many of which are beyond our control. A significant decline in production could result in materially lower revenues and cash flow and, therefore, may reduce dividends to Shareholders.

There is no assurance we will be successful in developing additional reserves or acquiring additional reserves on terms that meet our investment objectives. Without these reserves additions, our reserves will deplete and consequently, either production from, or the average reserves life of, our properties will decline, which will result in a reduction in the value of Common Shares and in a reduction in funds from operations available for dividends to Shareholders.

***Variations in interest rates and foreign exchange rates could affect our financial condition***

There is a risk that interest rates will increase given the current historical low level of interest rates. An increase in interest rates could result in a significant increase in the amount we pay to service debt and affect our ability to fund ongoing operations, resulting in a decrease in dividends to Shareholders, and could impact the market price of the Common Shares.

World oil and natural gas prices are quoted in United States dollars. The Canadian/U.S. dollar exchange rate, which fluctuates over time, consequently affects the price received by Canadian producers of oil and natural gas. Recently, the Canadian dollar has increased materially in value against the United States dollar. Material increases in the value of the Canadian dollar negatively affect our production revenue and our ability to maintain dividends to Shareholders in the future. Future Canadian/United States exchange rates could accordingly affect the future value of our as determined by our independent evaluator.

A decline in the value of the Canadian dollar relative to the United States dollar provides a competitive advantage to United States companies in acquiring Canadian oil and gas properties and may make it more difficult for us to replace reserves through acquisitions.

To the extent that we engage in risk management activities related to foreign exchange rates, there is a credit risk associated with counterparties with which we may contract.

***Continued uncertainty in the credit markets may restrict the availability or increase the cost of borrowing required for future development and acquisitions***

Recent market events and conditions, including disruptions in the international credit markets and other financial systems and the American and European sovereign debt levels have caused significant volatility in commodity prices. These events and conditions have caused a decrease in confidence in the broader U.S. and global credit and financial markets and have created a climate of greater volatility, less liquidity, widening of credit spreads, a lack of price transparency, increased credit losses and tighter credit conditions. Notwithstanding various actions by governments, concerns about the general condition of the capital markets, financial instruments, banks, investment banks, insurers and other financial institutions caused the broader credit markets to further deteriorate and stock markets to decline substantially. While there are signs of economic recovery, these factors have negatively impacted company valuations and are likely to continue to impact the performance of the global economy going forward. Petroleum prices are expected to remain volatile for the near future as a result of market uncertainties over the supply and demand of these commodities due to the current state of the world economies, actions taken by OPEC and the ongoing global credit and liquidity concerns. This volatility could materially affect our ability to access sufficient capital for our capital expenditures and acquisitions and, as a result, may have a material adverse effect on our ability to execute our business strategy and on our financial condition. There can be no assurance that financing will be available or sufficient to meet these requirements or for other corporate purposes or, if financing is available, that it will be on terms appropriate and acceptable to us. Should the lack of financing and uncertainty in the capital markets adversely impact our ability to refinance debt, additional equity may be issued resulting in a dilutive effect on current and future Shareholders.

***We have been historically reliant on external sources of capital, borrowings and equity sales and, if unavailable, our financial condition will be adversely affected***

Amounts paid in respect of interest and principal on debt may reduce dividends to Shareholders. Variations in interest rates and scheduled principal repayments could result in significant changes in the amount required to be applied to debt service before payment of dividends. Certain covenants in our Credit Agreement may also limit dividends. Although we believe the Credit Agreement will be sufficient for our immediate requirements, there can be no assurance that the amount will be adequate for our future financial obligations including our future capital expenditure program, or that we will be able to obtain additional funds.

As future capital expenditures will be financed out of funds flow from operating activities, borrowings and possible future security issuances, our ability to do so is dependent on, among other factors, the overall state of capital markets and investor appetite for investments in the energy industry and our securities in particular.

From time to time we may enter into transactions which may be financed in whole or in part with debt. The level of our indebtedness from time to time could impair our ability to obtain additional financing on a timely basis to take advantage of business opportunities that may arise. To the extent that external sources of capital become limited or unavailable or available on onerous terms, our ability to make capital investments and maintain or expand existing

assets and reserves may be impaired, and our assets, liabilities, business, financial condition, results of operations and dividends to Shareholders may be materially and adversely affected as a result.

Shareholders may suffer dilution in connection with future issuances of Common Shares. In the normal course of making capital investments to maintain and expand our oil and gas reserves additional Common Shares may be issued. Additionally, from time to time we may issue Common Shares in order to finance significant acquisitions or development projects or to reduce debt and maintain a more optimal capital structure. Our success is, in part, dependent on our ability to raise capital from time to time by issuing additional Common Shares. Shareholders may suffer dilution as a result of these offerings if, for example, the cash flow, production or reserves from the acquired assets do not reflect the additional number of Common Shares issued to acquire those assets. Shareholders may also suffer dilution in connection with future issuances of Common Shares to complete acquisitions.

We believe that estimated funds from operations, together with our Credit Agreement, will be sufficient to substantially finance our current operations, dividends to Shareholders and planned capital expenditures for the ensuing year. The timing of most of our capital expenditures is discretionary and there are no material long-term capital expenditure commitments. The level of dividends is also discretionary, and we have the ability to modify dividend levels should funds from operations be negatively impacted by a reduction in commodity prices or other factors. However, if funds from operations are lower than expected or capital costs for these projects exceed current estimates, or if we incur major unanticipated expenses related to development or maintenance of our existing properties, we may be required to seek additional capital to maintain our capital expenditures at planned levels. Failure to obtain any financing necessary for our capital expenditure plans may result in a delay in development or production on our properties or a decrease in dividends to Shareholders.

***Our hedging activities may negatively impact our income and our financial condition***

We may manage the risk associated with changes in commodity prices by entering into petroleum or natural gas price hedges. If we hedge our commodity price exposure, we may forego some of the benefits we would otherwise experience if commodity prices were to increase. As at December 31, 2012, our income statement reflected \$0.8 million of unrealized losses resulting from hedges to protect our commodity risk exposure. For more information in relation to our commodity hedging program, see "*Description of our Business – Disclosure of Reserves Data and Other Oil and Natural Gas Information – Other Oil and Gas Information – Forward Contracts*". We may initiate certain hedges to attempt to mitigate the risk of the Canadian dollar appreciating against the U.S. dollar. An increase in the Canada/U.S. foreign exchange rate will impact future dividends and the future value of our reserves as determined by independent evaluators. These hedging activities could expose us to losses and to credit risk associated with counterparties with which we contract.

***Failure of third parties to meet their contractual obligations to us may have a material adverse affect on our financial condition***

We are exposed to third party credit risk through our contractual arrangements with our current or future joint venture partners, third party operators, marketers of our petroleum and natural gas production, hedge counterparties and other parties. We manage this credit risk by entering into sales contracts with creditworthy entities and reviewing our exposure to individual entities on a regular basis. However, in the event such parties fail to meet their contractual obligations to us, such failures may have a material adverse effect on our business, financial condition, results of operations and prospects. In addition, poor credit conditions in the industry and of joint venture partners may impact a joint venture partner's willingness to participate in our ongoing capital program, potentially delaying the program and the results of such program until we find a suitable alternative partner.

***Our business is heavily regulated and such regulation increases our costs and may adversely affect our financial condition***

The oil and natural gas industry in Canada is subject to federal, provincial and municipal legislation and regulation governing such matters as land tenure, prices, royalties, production rates, environmental protection controls, the exportation of crude oil, natural gas and other products, as well as other matters. The industry is also subject to regulation by governments in such matters as the awarding or acquisition of exploration and production rights, oil



sands or other interests, the imposition of specific drilling obligations, environmental protection controls, control over the development and abandonment of fields and sites (including restrictions on production) and possibly the expropriation or cancellation of contract rights. Governments may regulate or intervene with respect to prices, taxes, royalties and the exportation of oil and natural gas and such regulations may be amended from time to time. Regulation increases our costs which will result in a reduction in funds from operations available for dividends to Shareholders.

In order to conduct oil and gas operations, we require licenses from various governmental authorities. There can be no assurance that we will be able to obtain all of the licenses and permits that may be required to conduct operations that we may wish to undertake. See "*Industry Conditions*".

In addition to regulatory requirements pertaining to the production, marketing and sale of oil and natural gas mentioned above, our business and financial condition could be influenced by federal legislation affecting, in particular, foreign investment, through legislation such as the *Competition Act* (Canada) and the *Investment Canada Act* (Canada).

***There are numerous uncertainties inherent in estimating quantities of recoverable petroleum and natural gas reserves, including many factors beyond our control***

Although we, together with McDaniel, have carefully prepared the reserves figures included in this Annual Information Form and believe that the methods of estimating reserves have been verified by operating experience, such figures are estimates and no assurance can be given that the indicated levels of reserves will be produced.

In general, estimates of economically recoverable petroleum and natural gas reserves and the future net revenues therefrom are based upon a number of variable factors and assumptions, such as historical production from the properties, production rates, ultimate reserve recovery, timing and amount of capital expenditures, marketability of petroleum and natural gas, royalty rates, the assumed effects of regulation by governmental agencies and future operating costs, all of which may vary materially from actual results. All such estimates are based on professional judgment and classifications of reserves, which, by their nature have a high degree of subjectivity. For those reasons, estimates of the economically recoverable petroleum and natural gas reserves attributable to any particular group of properties, classification of such reserves based on risk of recovery and estimates of future net revenues associated with reserves prepared by different engineers, or by the same engineers at different times may vary.

The reserves and recovery information contained in the McDaniel Report is only an estimate and the actual production and ultimate reserves from the properties may be greater or less than the estimates prepared by McDaniel and such variations could be material. The McDaniel Report has been prepared using certain commodity price assumptions which are described in the notes to the reserves tables. If we realize lower prices for crude oil, NGLs and natural gas and they are substituted for the price assumptions utilized in the McDaniel Report, the present value of estimated future net revenues for our reserves and our net asset value would be reduced and the reduction could be significant. The estimates in the McDaniel Report are based, in part, on the timing and success of activities we intend to undertake in future years. The reserves and estimated cash flows to be derived therefrom contained in the McDaniel Report will be reduced, in future years, to the extent that such activities do not achieve the level of success assumed in the McDaniel Report.

Estimates of proved and probable oil and gas reserves include undeveloped reserves that are expected to be recovered from new wells on undrilled acreage or from existing wells where a relatively major expenditure is still required before such wells begin production. Reserves may be recognized when plans are in place to make the required investments to convert these undeveloped reserves to producing. Circumstances such as a sustained decline in commodity prices or poorer than expected results from initial activities could cause a change in the investment or development plans which could result in a material change in our reserves estimates.

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poorer than expected results from initial activities could cause a change in the investment or development plans which could result in a material change in our reserves estimates.

Estimates of proved undeveloped reserves are sometimes based upon volumetric calculations and upon analogy to similar types of reserves rather than actual production history. Recovery factors and drainage areas are estimated by experience and analogy to similar producing pools. Estimates based on these methods are generally less reliable than those based on actual production history. Subsequent evaluation of the same reserves based upon production history and production practices will result in variations in the estimated reserves and such variations could be material.

***Acquiring, developing and exploring for oil and natural gas involves many risks, which even a combination of experience, knowledge and careful evaluation may not be able to overcome***

These risks include, but are not limited to, encountering unexpected formations or pressures, premature declines of reservoirs, blow-outs, craterings, equipment failures and other accidents, sour gas releases, oil and natural gas spills, uncontrollable flows of oil, natural gas or well fluids, the invasion of water into producing formations, adverse weather conditions, pollution, other environmental hazards, fires, spills, transport accidents and spills and delays in payments between parties caused by operation or economic matters which could result in substantial damage to oil and natural gas wells, production facilities, other property and the environment, personal injuries, loss of life and other hazards, all of which could result in liability. These risks will increase as we undertake more exploratory activity. Drilling hazards or environmental damage could greatly increase the cost of operations, and various field operating conditions may adversely affect the production from successful wells. These conditions include delays in obtaining governmental approvals or consents, the shut-ins of connected wells resulting from extreme weather conditions, insufficient storage or transportation capacity or other geological and mechanical conditions. Although we maintain insurance in accordance with customary industry practice, we are not fully insured against all of these risks nor are all such risks insurable and in certain circumstances we may elect not to obtain insurance to deal with specific risks due to the high premiums associated with such insurance or other reasons. In addition, the nature of these risks is such that liabilities could exceed policy limits, in which event we could incur significant costs that could have a material adverse effect upon our financial condition.

Exploration and development risks arise due to the uncertain results of searching for and producing petroleum and natural gas using imperfect scientific methods. These risks are mitigated by using highly skilled staff, focusing exploration efforts in areas in which we have existing knowledge and expertise or access to such expertise, using up-to-date technology to enhance methods and controlling costs to maximize returns.

Losses resulting from the occurrence of any of these risks may have a material adverse effect on our business, financial condition, results of operations, prospects and our ability to maintain dividends to Shareholders.

***The operation of a portion of our properties is largely dependent on the ability of third party operators, and harm to their business could cause delays and additional expenses in our receiving revenues***

The continuing production from a property, and to some extent the marketing of production, is dependent upon the ability of the operators of our properties. Approximately 14.6 percent of our properties are operated by third parties, based on daily production. Our return on assets operated by others depends upon a number of factors that may be outside of our control, including the timing and amount of capital expenditures, the operator's expertise and financial resources, the approval of other participants, the selection of technology and risk management practices. If, in situations where we are not the operator, the operator fails to perform these functions properly or becomes insolvent, revenues may be reduced. Revenues from production generally flow through the operator and, where we are not the operator; there is a risk of delay and additional expense in receiving such revenues.

In addition to the usual delays in payment by purchasers of oil and natural gas to the operators of the properties, and by the operator to our operating entities, payments between any of such parties may also be delayed by restrictions imposed by lenders, delays in the sale or delivery of products, delays in the connection of wells to a gathering system, blowouts or other accidents, recovery by the operator of expenses incurred in the operation of properties or the establishment by the operator of reserves for such expenses. Our return on assets operated by others therefore will depend upon a number of factors that may be outside of our control, including the timing and amount of capital

expenditures, the operator's expertise and financial resources, the approval of other participants, the selection of technology and risk management practices. Losses resulting from the occurrence of any of these risks may have a material adverse effect on our business, financial condition, results of operations and prospects and our ability to maintain dividends to Shareholders.

***Delays in business operations could adversely affect dividends to Shareholders and the market price of the Common Shares***

Delays in business operations could adversely affect dividends to Shareholders and the market price of our Common Shares. In addition to the usual delays in payment by purchasers of oil and natural gas to the operators of our properties, and the delays of those operators in remitting payment to us, payments between any of these parties may also be delayed by:

- restrictions imposed by lenders;
- accounting delays;
- delays in the sale or delivery of products;
- delays in the connection of wells to a gathering system;
- restrictions due to limited pipeline or processing capacity;
- operational problems affecting pipelines and facilities;
- blowouts or other accidents;
- adjustments for prior periods;
- recovery by the operator of expenses incurred in the operation of the properties; or
- the establishment by the operator of reserves for these expenses.

Any of these delays could reduce the amount of cash available for dividends to Shareholders in a given period and expose us to additional third party credit risks.

***The marketability of petroleum and natural gas that may be acquired or discovered by us will be affected by numerous factors beyond our control***

These factors include demand for petroleum and natural gas, market fluctuations, the availability, proximity and capacity of oil and natural gas pipelines and processing and storage facilities and government regulations, including regulations relating to environmental protection, royalties, allowable production, pricing, taxes, importing and exporting of oil and natural gas and political events throughout the world that cause disruptions in the supply of oil and affect the marketability and price of oil and natural gas acquired or discovered by us. Any particular event could result in a material decline in prices and, therefore, result in a reduction of our net production revenue. The availability of markets is beyond our control. In addition, our oil and natural gas properties, wells and facilities could be subject to a terrorist attack. If any of our properties, wells or facilities are the subject of terrorist attack it could have a material adverse effect on our financial condition. We do not have insurance to protect against the risk from terrorism.

***Our Credit Agreement may be extended prior to June 26, 2013 and failure to extend may, and higher rates will, adversely affect our financial condition***

Our existing Credit Agreement and any replacement credit facilities may not provide sufficient liquidity. The amounts available under our existing Credit Agreement may not be sufficient for future operations, or we may not be able to obtain additional financing on economic terms attractive to us, if at all. Our current Credit Agreement includes credit facilities in the maximum principal amount of \$165 million. Our current Credit Agreement has a term date of June 26, 2013 and may be extended for a further 364-day period at our request. If the credit facilities are not extended, they convert to a 365-day term loan and are repayable in full at the end of such term. Repayment of all outstanding amounts under the Credit Agreement may be demanded on relatively short notice if an event of default occurs, which is continuing. If this occurs, we may need to obtain alternate financing. Any failure to obtain suitable replacement financing may have a material adverse effect on our business, and dividends to Shareholders may be materially reduced. There is also a risk that the Credit Agreement will not be extended for the same amount or on the same terms.

We are required to comply with covenants under the Credit Agreement. In the event that we do not comply with these covenants, which may be affected by events beyond our control, our access to capital could be restricted or repayment could be required on an accelerated basis by our lenders, and the ability to pay dividends to our Shareholders may be restricted. The lenders under the Credit Agreement have security over all of our assets. If we become unable to pay our debt service charges or otherwise commit an event of default, such as breach of our financial covenants, the lenders under the Credit Agreement may foreclose on or sell our working interests in our properties.

Our borrowing base is determined and re-determined by our lenders based on our reserves, commodity prices, applicable discount rate and other factors as determined by our lenders. A material decline in commodity prices could reduce our borrowing base, thereby reducing the funds available to us under our credit facilities which could result in a portion, or all, of our bank indebtedness being required to be repaid.

***Hydraulic fracturing is subject to certain risks***

Hydraulic fracturing involves the injection of water, sand and small amounts of additives under pressure into rock formations to stimulate hydrocarbon (natural gas and oil) production. Specifically, hydraulic fracturing is used to produce commercial quantities of natural gas and oil from reservoirs that were previously unproductive. We use hydraulic fracturing extensively in our operations. With the increase in the use of fracture stimulations in horizontal wells there is increased communication between the oil and natural gas industry and a wider variety of stakeholders regarding the responsible use of this technology as it relates to the environment. This increased attention to fracture stimulations may result in increased regulation or changes of law which may make the conduct of our business more expensive or prevent us from conducting our business as currently conducted. Any new laws, regulation or permitting requirements regarding hydraulic fracturing could lead to operational delays or increased operating costs, third party or governmental claims, and could increase our costs of compliance and doing business as well as delay the development of oil and natural gas resources from shale formations which are not commercial without the use of hydraulic fracturing. Restrictions on hydraulic fracturing could also reduce the amount of oil and natural gas that we are ultimately able to produce from our reserves.

***Changes in government regulations that affect the oil and natural gas industry could adversely affect us and reduce our dividends to our Shareholders***

Government regulations may change from time to time in response to economic or political conditions. The exercise of discretion by governmental authorities under existing regulations, the implementation of new regulations or the modification of existing regulations affecting the oil and gas industry could reduce demand for crude oil and natural gas, increase our costs, or delay or restrict our operations, all of which would have a material adverse impact on us.

There can be no assurance that the federal government and the provincial governments of the western provinces will not adopt a new or modify the royalty regime which may have an impact on the economics of our projects. An increase in royalties would reduce our earnings and could make future capital investments, or our operations, less economic. See "*Industry Conditions*".

***Income tax laws or other laws or government incentive programs or regulations relating to our industry may in the future be changed or interpreted in a manner that adversely affects us and our Shareholders***

Changes in tax and other laws may adversely affect Shareholders. Income tax laws, other laws or government incentive programs relating to the oil and natural gas industry, such as resource allowance, may in the future be changed or interpreted in a manner that adversely affects us and our Shareholders. Tax authorities having jurisdiction over us or our Shareholders may disagree with the manner in which we calculate our income for tax purposes or could change their administrative practices to our detriment or the detriment of Shareholders.

The oil and natural gas industry is subject to extensive controls and regulations governing its operations (including land tenure, exploration, development, production, refining, transportation, and marketing) imposed by legislation enacted by various levels of government and with respect to pricing and taxation of oil and natural gas by agreements among the governments of Canada, Alberta, Saskatchewan and the United States, all of which should be

carefully considered by investors in the oil and natural gas industry. All of such controls, regulations and legislation are subject to revocation, amendment or administrative change, some of which have historically been material and in some cases materially adverse and there can be no assurance that there will not be further revocation, amendment or administrative change which will be materially adverse to our assets, reserves, financial condition or results of operations or prospects and our ability to maintain dividends to Shareholders.

We cannot assure you that income tax laws and government incentive programs relating to the oil and natural gas industry will not change in a manner that adversely affects the market price of the Common Shares.

We file all required income tax returns and believe that we are in full compliance with the provisions of the Income Tax Act (Canada) and all other applicable provincial tax legislation. However, such returns are subject to reassessment by the applicable taxation authority. In the event of a successful reassessment of us, whether by re-characterization of exploration and development expenditures or otherwise, such reassessment may have an impact on current and future taxes payable.

***Climate change laws and related environmental, health and safety regulation may impose restrictions or costs on our business which may adversely affect our financial condition and our ability to maintain dividends***

Our exploration and production facilities and other operations and activities emit greenhouse gases and which may require us to comply with greenhouse gas emissions legislation in Alberta or that may be enacted in other provinces. Climate change policy is evolving at regional, national and international levels, and political and economic events may significantly affect the scope and timing of climate change measures that are ultimately put in place. As a signatory to the *United Nations Framework Convention on Climate Change* (the "UNFCCC") and as a participant to the Copenhagen Agreement (a non-binding agreement created by the UNFCCC), the Government of Canada announced on January 29, 2010 that it will seek a 17% reduction in greenhouse gas ("GHG") emissions from 2005 levels by 2020. These GHG emission reduction targets are not binding, however. Although it is not the case today, some of our significant facilities may ultimately be subject to future regional, provincial and/or federal climate change regulations to manage GHG emissions. The direct or indirect costs of compliance with these regulations may have a material adverse effect on our business, financial condition, results of operations and prospects. Given the evolving nature of the debate related to climate change and the control of greenhouse gases and resulting requirements, it is not possible to predict the impact on us and our operations and financial condition.

Although we believe that we are in material compliance with current applicable environmental, health and safety regulations, no assurance can be given that such regulations will not result in a curtailment of production, a reduction of product demand, a material increase in the costs of production, development or exploration activities or otherwise adversely affect our business, financial condition, results of operations or prospects. Future changes in other environmental, health and safety legislation could occur and result in stricter standards and enforcement, larger fines and liability, and increased capital expenditures and operating costs, which could have a material adverse effect on our financial condition or results of operations and prospects. See "*Industry Conditions – Environmental Regulation*".

***We may not be able to realize the anticipated benefits of acquisitions and dispositions or to manage growth***

We make acquisitions and dispositions of businesses and assets in the ordinary course of our business. Achieving the benefits of acquisitions depends on successfully consolidating functions and integrating operations and procedures in a timely and efficient manner and our ability to realize the anticipated growth opportunities and synergies from combining the acquired businesses and operations with our operations. The integration of acquired business may require substantial management effort, time and resources diverting management's focus from other strategic opportunities and operational matters. Management continually assesses the value and contribution of services provided and assets required to provide such services. There is no assurance that we will be able to continue to complete acquisitions or dispositions of oil and natural gas properties which realize all the synergistic benefits.

We periodically dispose of non-core assets so that we can focus our efforts and resources more efficiently. Depending on the state of the market for such non-core assets, certain of our non-core assets, if disposed of, may realize less than their carrying value on our financial statements.

The price we pay for the purchase of any material properties is based on several criteria, including engineering and economic assessments made by independent engineers modified to reflect our technical and economic views. These assessments include a series of assumptions regarding such factors as recoverability and marketability of petroleum and natural gas, future prices of petroleum and natural gas and operating costs, future capital expenditures and royalties and other government levies which will be imposed over the producing life of the reserves. Many of these factors are subject to change and are beyond our control. All such assessments involve a measure of geologic and engineering uncertainty which could result in lower than anticipated production and reserves. Consequently, the reserves acquired may be less than expected, which could adversely impact cash flow from operating activities and dividends to Shareholders.

We may be subject to growth-related risks including capacity constraints and pressure on our internal systems and controls. Our ability to manage growth effectively will require us to continue to implement and improve our operational and financial systems and to expand, train and manage our employee base. Our inability to deal with this growth could have a material adverse effect on our business, financial condition, results of operations and prospects.

***There is strong competition relating to all aspects of the oil and natural gas industry***

There are numerous companies in the oil and natural gas industry, who are competing with us for the acquisitions of properties with longer life reserves, properties with exploitation and development opportunities and undeveloped land. As a result of such competition, it may be more difficult for us to acquire reserves on beneficial terms. Many of these other organizations have significantly greater technical, financial and operational resources than us.

We compete with other oil and gas companies to hire and retain skilled personnel necessary for running our daily operations, including planning, capitalizing on available technical advances and the execution of our exploration and development program. The inability to hire and retain skilled personnel could adversely impact certain of our operational and financial results.

Oil and natural gas exploration and development activities are dependent on the availability of drilling and related equipment (typically leased from third parties) in the particular areas where such activities will be conducted. Demand for such limited equipment or access restrictions may affect the availability of such equipment to us and may delay exploration and development activities.

The oil industry is characterized by rapid and significant technological advancements and introductions of new products and services utilizing new technologies. Other oil companies may have greater financial, technical and personnel resources that allow them to enjoy technological advantages and may in the future allow them to implement new technologies before us. There can be no assurance that we will be able to respond to such competitive pressures and implement such technologies on a timely basis or at an acceptable cost. One or more of the technologies currently utilized by us or implemented in the future may become obsolete. In such case, our business, financial condition and results of operations could be materially adversely affected. If we are unable to utilize the most advanced commercially available technology, our business, financial condition and results of operations could be materially adversely affected.

Full conservation measures, alternative fuel requirements, increasing consumer demand for alternatives to oil and natural gas, and technological advances in fuel economy and energy generation devices could reduce the demand for oil and other liquid hydrocarbons. We cannot predict the impact of changing demand for oil and natural gas products, and any major changes may have a material adverse effect on our business, financial condition, results of operations and cash flows.

***Our petroleum and natural gas reserves are a depleting resource and decline as such reserves are produced***

Absent commodity price increases or cost effective acquisition and development activities, our funds from operations will decline over time in a manner consistent with declining production from typical petroleum and natural gas reserves. Our future petroleum and natural gas reserves and production, and therefore our funds from operations, will be highly dependent on our success in exploiting our reserves base and acquiring additional

reserves. Without reserves additions through acquisition or development activities, our reserves and production may decline over time as reserves are produced.

We also distribute a significant proportion of our funds from operations to Shareholders rather than reinvesting it in reserves additions. Accordingly, if external sources of capital, including the issuance of additional Common Shares, become limited or unavailable on commercially reasonable terms, our ability to make the necessary capital investments to maintain or expand our petroleum and natural gas reserves may be impaired. To the extent that we use funds from operations to finance capital expenditures or property acquisitions, the level of funds from operations available for distribution to Shareholders will be reduced. There can be no assurance that we will be successful in developing or acquiring additional reserves on terms that meet our investment objectives.

***We may participate in larger projects and may have more concentrated risk in certain areas of our operations***

We manage a variety of small and large projects in the conduct of our business. Project delays may impact expected revenues from operations. Significant project cost over-runs could make a project uneconomic. Our ability to execute projects and market oil and natural gas depends upon numerous factors beyond our control, including:

- the availability of processing capacity;
- the availability and proximity of pipeline capacity;
- the availability of storage capacity;
- the availability of, and the ability to acquire, water supplies needed for drilling and hydraulic fracturing, or our ability to dispose of water used or removed from strata at a reasonable cost and within applicable environmental regulations;
- the supply of and demand for oil and natural gas;
- the availability of alternative fuel sources;
- the effects of inclement weather;
- the availability of drilling and related equipment;
- unexpected cost increases;
- accidental events;
- currency fluctuations;
- changes in regulations;
- the availability and productivity of skilled labour; and
- the regulation of the oil and natural gas industry by various levels of government and governmental agencies.

Because of these factors, we could be unable to execute projects on time, on budget or at all, and may be unable to effectively market the oil and natural gas that we produce effectively.

***We only operate in western Canada and the United States and expansion outside of these areas may increase our risk exposure***

Our operations and expertise are currently primarily focused on oil and gas production and development in the Western Canadian Sedimentary Basin and the United States. In the future we may acquire or move into new industry related activities or new geographical areas, may acquire different energy related assets, and as a result may face unexpected risks or alternatively, significantly increase our exposure to one or more existing risk factors, which may in turn result in our future operational and financial conditions being adversely affected.

***Our success depends in large measure on the activities of our key personnel***

Our Shareholders are entirely dependent on our management with respect to the acquisition of oil and gas properties, the development and acquisition of additional reserves, the management and administration of all matters relating to our properties, including the safekeeping of our primary workspace and computer systems. The loss of the services of key personnel may have a material adverse effect on our business, financial condition, results of operations and prospects. The contributions of the existing management team to our immediate and near term operations are likely

to be of central importance. In addition, the competition for qualified personnel in the oil and natural gas industry is intense and there can be no assurance that we will be able to continue to attract and retain all personnel necessary for the development and operation of our business. Investors must rely upon the ability, expertise, judgment, discretion, integrity and good faith of our management.

***Securing and maintaining title to our properties is subject to certain risks***

Our properties are held in the form of licenses and leases and working interests in licenses and leases. If we or the holder of the license or lease fails to meet the specific requirement of a license or lease, the license or lease may terminate or expire. There can be no assurance that any of the obligations required to maintain each license or lease will be met. The termination or expiration of a license or lease or the working interest relating to a license or lease may have a material adverse affect on our results of operations and business. In addition title to the properties can become subject to dispute and defeat our claim to title over certain of our properties.

Aboriginal peoples have claimed aboriginal title and rights to portions of western Canada and have also made claims that certain developments, including oil and gas exploration and development, may have been proceeding without the Crown carrying out appropriate consultations in the course of allowing such developments to proceed. We are not aware of any material claims having been made in respect of our properties and assets; however, if a claim arose and was successful this may have a material adverse affect on our results of operations and business.

Although title reviews are conducted prior to any purchase of significant resource assets, such reviews cannot guarantee that an unforeseen defect in the chain of title will not arise to defeat our title to certain assets. Our actual interest in properties may, therefore, vary from our records. If a title defect does exist, it is possible that we may lose all or a portion of the properties to which the title defect relates, which may have a material adverse effect on our business, financial condition, results of operations and prospects. There may be valid challenges to title, or proposed legislative changes which affect title, to the oil and natural gas properties that we control that, if successful or made into law, could impair our activities on them and result in a reduction in the amount of funds from operations, possibly resulting in lower dividends to our Shareholders which could result in a lower market price of the Common Shares.

***We are affected by seasonality***

The level of activity in the Canadian oil and natural gas industry is influenced by seasonal weather patterns. Wet weather and spring thaw may make the ground unstable. Consequently, municipalities and provincial transportation departments enforce road bans that restrict the movement of rigs and other heavy equipment, thereby reducing activity levels. Also, certain oil and natural gas producing areas are located in areas that are inaccessible other than during the winter months because the ground surrounding the sites in these areas consists of swampy terrain. Seasonal factors and unexpected weather patterns may lead to declines in exploration and production activity and corresponding declines in the demand for crude oil and natural gas.

***Our permitted investments may be risky***

An investment in us should be made with the understanding that the value of any of our investments may fluctuate in accordance with changes in the financial condition of such investments, the value of similar securities, and other factors. For example, the prices of Canadian government securities, bankers' acceptances and commercial paper react to economic developments and changes in interest rates. Commercial paper is also subject to issuer credit risk. Investments in energy-related companies and partnerships will be subject to the general risks of investing in equity securities. These include the risk that the financial condition of issuers may become impaired, or that the energy sector may suffer a market downturn. Securities markets in general are affected by a variety of factors, including governmental, environmental and regulatory policies, inflation and interest rates, economic cycles, and global, regional and national events. The value of our Common Shares could be affected by adverse changes in the market values of such investments.



***A shortfall in the supply of diluent may cause increase our costs***

Heavy oil and bitumen are characterized by high specific gravity or weight and high viscosity or resistance to flow. Diluent is required to facilitate the transportation of heavy oil and bitumen. A shortfall in the supply of diluent may cause its price to increase thereby increasing the cost to transport heavy oil and bitumen to market and correspondingly increasing our overall operating cost, decreasing our net revenues and negatively impacting the overall profitability of our heavy oil and bitumen projects.

***We may become involved in, named as a party to, or be the subject of, various legal proceedings***

In the normal course of our operations, we may become involved in, named as a party to, or be the subject of, various legal proceedings, including regulatory proceedings, tax proceedings and legal actions, related to personal injuries, property damage, property tax, land rights, the environment and contract disputes. The outcome of outstanding, pending or future proceedings cannot be predicted with certainty and may be determined adversely to us and as a result, could have a material adverse effect on our assets, liabilities, business, financial condition and results of operations.

In addition, due to the rapid development of oil and gas technology, in the normal course of our operations, we may become involved in, named as a party to, or be the subject of, various legal proceedings in which it is alleged that we have infringed the intellectual property rights of others or commence lawsuits against others who we believe are infringing upon our rights. Our involvement in intellectual property litigation could result in significant expense, adversely affecting the development of our assets or intellectual property or diverting the efforts of our technical and management personnel, whether or not such litigation is resolved in our favour. In the event of an adverse outcome as a defendant in any such litigation, we may, among other things, be required to: (a) pay substantial damages; cease the development, use, sale or importation of process that infringe upon other patented intellectual property; (b) expend significant resources to develop or acquire non-infringing intellectual property; (c) discontinue processes incorporating infringing technology; or (d) obtain licences to the infringing intellectual property. We may not be successful in such development or acquisition or that such licences would be available on reasonable terms. Any such development, acquisition or licence could require the expenditure of substantial time and other/ resources and could have a material adverse effect on our business and financial results.

While discussing potential business relationships or other transactions with third parties, we may disclose confidential information relating to our business, operations or affairs. Although confidentiality agreements are signed by third parties prior to the disclosure of any confidential information, a breach could put us at competitive risk and may cause significant damage to our business. The harm to our business from a breach of confidentiality cannot presently be quantified, but may be material and may not be compensable in damages. There is no assurance that, in the event of a breach of confidentiality, we will be able to obtain equitable remedies, such as injunctive relief, from a court of competent jurisdiction in a timely manner, if at all, in order to prevent or mitigate any damage to its business that such a breach of confidentiality may cause.

**Risks Relating to Ownership of Common Shares**

***Our Board of Directors has discretion in the payment of dividends and may choose not to maintain dividends in certain circumstances***

The amount of future cash dividends, if any, will be subject to the discretion of our Board of Directors and may vary depending on a variety of factors and conditions existing from time to time, including fluctuations in commodity prices, production levels, capital expenditure requirements, debt service requirements, operating costs, royalty burdens, foreign exchange rates and the satisfaction of the liquidity and solvency tests imposed by the *Business Corporations Act* (Alberta) for the declaration and payment of dividends. Depending on these and various other factors, many of which will be beyond the control of our Board of Directors and management team, we will change our dividend policy from time to time and, as a result, future cash dividends could be reduced or suspended entirely. The market value of the Common Shares may deteriorate if we reduce or suspend the amount of the cash dividends that we pay in the future and such deterioration may be material. Furthermore, the future treatment of dividends for

tax purposes will be subject to the nature and composition of our dividends and potential legislative and regulatory changes.

Dividends may be reduced during periods of lower funds from operations, which result from lower commodity prices and the decision by us to finance capital expenditures using funds from operations. A reduction in dividends could also negatively affect the market price of the Common Shares.

Production and development costs incurred with respect to properties, including power costs and the costs of injection fluids associated with tertiary recovery operations, reduce the income that we receive and, consequently, the amounts we can distribute to our Shareholders.

The timing and amount of capital expenditures will directly affect the amount of income available for dividends to our Shareholders. Dividends may be reduced, or even eliminated, at times when significant capital or other expenditures are planned. To the extent that external sources of capital, including the issuance of additional Common Shares, become limited or unavailable, our ability to make the necessary capital investments to maintain or expand petroleum and natural gas reserves and to invest in assets, as the case may be, will be impaired. To the extent that we are required to use funds from operations to finance capital expenditures or property acquisitions, the cash we receive will be reduced, resulting in reductions to the amount of cash we are able to distribute to our Shareholders. A reduction in the amount of cash distributed to Shareholders may negatively affect the market price of the Common Shares.

***Changes in market-based factors may adversely affect the trading price of the Common Shares***

The trading price of securities of oil and natural gas issuers is subject to substantial volatility often based on factors related and unrelated to the financial performance or prospects of the issuers involved. Factors unrelated to our performance could include macroeconomic developments nationally, within North America or globally, domestic and global commodity prices or current perceptions of the oil and gas market. Similarly, the market price of our Common Shares could be subject to significant fluctuations in response to variations in our operating results, financial condition, liquidity and other internal factors. The price at which our Common Shares will trade cannot be accurately predicted.

**Certain Risks for United States and Other Non-Resident Shareholders**

***The ability of investors resident in the United States to enforce civil remedies is limited***

We are a corporation incorporated under the laws of the Province of Alberta, Canada and our principal office is located in Calgary, Alberta. All of our directors and officers and the representatives of the experts who provide services to us (such as our auditors and our independent reserve engineers), and all or a substantial portion of our assets and the assets of such persons are located outside the United States. As a result, it may be difficult for investors in the United States to effect service of process within the United States upon such directors, officers and representatives of experts who are not residents of the United States or to enforce against them judgements of the United States courts based upon civil liability under the United States federal securities laws or the securities laws of any state within the United States. There is doubt as to the enforceability in Canada against us or any of our directors, officers or representatives of experts who are not residents of the United States, in original actions or in actions for enforcement of judgements of United States courts of liabilities based solely upon the United States federal securities laws or securities laws of any state within the United States.

***Canadian and United States practices differ in reporting reserves and production and our estimates may not be comparable to those of companies in the United States***

We report our production and reserve quantities in accordance with Canadian practices and specifically in accordance with NI 51-101. These practices are different from the practices used to report production and to estimate reserves in reports and other materials filed with the SEC by companies in the United States.

We incorporate additional information with respect to production and reserves which is either not required to be included or prohibited under rules of the SEC and practices in the United States. We follow the Canadian practice of reporting gross production and reserve volumes (before deduction of Crown and other royalties); however, we also follow the United States practice of separately reporting reserve volumes on a net basis (after the deduction of royalties and similar payments). We also follow the Canadian practice of using forecast prices and costs when we estimate our reserves; whereas the SEC rules require that a 12-month average price, calculated as the unweighted arithmetic average of the first-day-of-the-month price for each month within the 12-month period prior to the end of the reporting period, be utilized.

We included in this Annual Information Form estimates of proved and proved plus probable reserves. Probable reserves have a lower certainty of recovery than proved reserves. The SEC requires oil and gas issuers in their filings with the SEC to disclose only proved reserves but permits the optional disclosure of probable reserves. The SEC definitions of proved reserves and probable reserves are different than NI 51-101; therefore, proved, probable and proved plus probable reserves disclosed in this Annual Information Form may not be comparable to United States standards.

As a consequence of the foregoing, our reserve estimates and production volumes in this Annual Information Form may not be comparable to those made by companies utilizing United States reporting and disclosure standards.

***There is additional taxation applicable to non-residents***

The *Income Tax Act* (Canada) imposes a withholding tax at the rate of 25% on the dividends paid by us to Shareholders who are non-residents of Canada, unless the rate is reduced under the provisions of a tax treaty between Canada and the non-resident Shareholder's jurisdiction of residence. These taxes may change from time to time. Where the non-resident Shareholder is a United States resident entitled to benefits under the Canada-United States Income Tax Convention, 1980 and is the beneficial owner of the dividends, the rate of Canadian withholding tax applicable to dividends is generally reduced to 15%. Additionally, the reduced rates of taxation on qualified dividend income under current U.S. tax laws are scheduled to expire at the end of 2012 and there is no assurance that the reduced tax rates will be re-enacted in the future.

***There is a foreign exchange risk for non-resident Shareholders***

Our dividends are declared in Canadian dollars and converted to foreign denominated currencies at the spot exchange rate at the time of payment. As a consequence, investors are subject to foreign exchange risk. To the extent that the Canadian dollar strengthens with respect to their currency, the amount of the dividend will be reduced when converted to their home currency.

## **MATERIAL CONTRACTS**

Except for contracts entered into in the ordinary course of business, the only material contract entered into by us within the most recently completed financial year, or before the most recently completed financial year but which is still material and is in effect, are as follows:

1. our Credit Agreement in respect of our \$165 million syndicated credit facilities, which agreement is described in Note 10 to our annual audited consolidated financial statements for the year ended December 31, 2012, which note is incorporated by reference herein; and
2. the Debenture Indenture.

Copies of each of these documents have been filed on SEDAR at [www.sedar.com](http://www.sedar.com).

## **LEGAL PROCEEDINGS AND REGULATORY ACTIONS**

There are no legal proceedings that we are or were a party to, or that any of our property is or was the subject of, during the most recently completed financial year, that were or are material to us, and there are no such material legal proceedings that we are currently aware of that are contemplated.

There were no: (i) penalties or sanctions imposed against us by a court relating to securities legislation or by a securities regulatory authority during our most recently completed financial year; (ii) other penalties or sanctions imposed by a court or regulatory body against us that would likely be considered important to a reasonable investor in making an investment decision; or (iii) settlement agreements we entered into with a court relating to securities legislation or with a securities regulatory authority during our most recently completed financial year.

## **TRANSFER AGENT AND REGISTRAR**

The transfer agent and registrar for our Common Shares is Valiant Trust Company at its principal offices in Calgary, Alberta and Toronto, Ontario.

## **INTEREST OF MANAGEMENT AND OTHERS IN MATERIAL TRANSACTIONS**

There were no material interests, direct or indirect, of our directors and senior officers, any holder of Common Shares who beneficially owns, or controls or directs, directly or indirectly, more than 10 percent of the outstanding Common Shares, or any known associate or affiliate of such persons, in any transaction within the last three financial years or during the current financial year which has materially affected or would materially affect us.

## **INTERESTS OF EXPERTS**

There is no person or company whose profession or business gives authority to a statement made by such person or company and who is named as having prepared or certified a report, valuation, statement or opinion described or included in a filing, or referred to in a filing, made under National Instrument 51-102 – *Continuous Disclosure Obligations* by us during, or related to, our most recently completed financial year other than McDaniel, our independent engineering evaluator, and Ernst & Young LLP, our auditors.

None of the "designated professionals" (as that term is defined in National Instrument 51-102) of McDaniel had any registered or beneficial interests, direct or indirect, in any of our securities or other property or of our associates or affiliates either at the time they prepared the report, valuation, statement or opinion prepared by it, at any time thereafter or to be received by them.

Ernst & Young LLP is independent in accordance with the Rules of Professional Conduct as outlined by the Institute of Chartered Accountants of Alberta.

In addition, none of the aforementioned persons or companies, nor any director, officer or employee of any of the aforementioned persons or companies, is or is expected to be elected, appointed or employed as a director, officer or employee of us or of any of our associate or affiliate entities, except that Grant A. Zawalsky, one of our directors, is a partner at Burnet, Duckworth & Palmer LLP, which is a law firm that renders legal services to us.

#### **ADDITIONAL INFORMATION**

Additional information relating to us can be found on SEDAR at [www.sedar.com](http://www.sedar.com) and on our website at [www.zargon.ca](http://www.zargon.ca). Additional information, including directors' and officers' remuneration and indebtedness, principal holders of our securities and securities issued and authorized for issuance under our equity compensation plans are contained in our information circular – proxy statement dated April 10, 2013 relating to our annual and special Shareholders meeting to be held on May 15, 2013. Additional financial information is contained in our consolidated financial statements for the year ended December 31, 2012 and the related management's discussion and analysis.

For additional copies of the Annual Information Form and the materials listed in the preceding paragraphs please contact:

Zargon Oil & Gas Ltd.  
700, 333 – 5<sup>th</sup> Avenue S.W.  
Calgary, Alberta, T2P 3B6  
Tel: (403) 264-9992  
Fax: (403) 265-3026

## APPENDIX A

### REPORT OF MANAGEMENT AND DIRECTORS ON OIL AND GAS DISCLOSURE

(Form 51-101F3)

Management of Zargon Oil & Gas Ltd. ("**Zargon**") is responsible for the preparation and disclosure of information with respect to Zargon's oil and gas activities in accordance with securities regulatory requirements. This information includes reserves data which are estimates of proved reserves and probable reserves and related future net revenue as at December 31, 2012, estimated using forecast prices and costs.

An independent qualified reserves evaluator has evaluated Zargon's reserves data. The report of the independent qualified reserves evaluator is presented below.

The Reserves Committee of the board of directors of Zargon has

- (a) reviewed Zargon's procedures for providing information to the independent qualified reserves evaluator;
- (b) met with the independent qualified reserves evaluator to determine whether any restrictions affected the ability of the independent qualified reserves evaluator to report without reservation; and
- (c) reviewed the reserves data with management and the independent qualified reserves evaluator.

The Reserves Committee of the board of directors has reviewed Zargon's procedures for assembling and reporting other information associated with oil and gas activities and has reviewed that information with management. The board of directors has, on the recommendation of the Reserves Committee, approved

- (d) the content and filing with securities regulatory authorities of Form 51-101F1 containing reserves data and other oil and gas information;
- (e) the filing of Form 51-101F2 which is the report of the independent qualified reserves evaluator on the reserves data; and
- (f) the content and filing of this report.

Because the reserves data are based on judgments regarding future events, actual results will vary and the variations may be material.

(signed) C.H. Hansen  
President and Chief Executive Officer

(signed) B.G. Kergan  
Vice President, Corporate Development

(signed) J.G. Weir  
Director and Chairman of the Audit and Reserves  
Committee

(signed) M. McKenzie  
Director and Member of the Audit and Reserves  
Committee

(signed) K.D. Kitagawa  
Director and Member of the Audit and Reserves  
Committee

(signed) G.C. Merritt  
Director and Member of the Audit and Reserves  
Committee

February 20, 2013

## APPENDIX B

### REPORT ON RESERVES DATA BY MCDANIEL

(Form 51-101F2)

To the board of directors of Zargon Oil & Gas Ltd. ("Zargon"):

1. We have evaluated Zargon's reserves data as at December 31, 2012. The reserves data are estimates of proved reserves and probable reserves and related future net revenue as at December 31, 2012, estimated using forecast prices and costs.
2. The reserves data are the responsibility of Zargon's management. Our responsibility is to express an opinion on the reserves data based on our evaluation.

We carried out our evaluation in accordance with standards set out in the Canadian Oil and Gas Evaluation Handbook (the "**COGE Handbook**") prepared jointly by the Society of Petroleum Evaluation Engineers (Calgary Chapter) and the Canadian Institute of Mining, Metallurgy & Petroleum (Petroleum Society).

3. Those standards require that we plan and perform an evaluation to obtain reasonable assurance as to whether the reserves data are free of material misstatement. An evaluation also includes assessing whether the reserves data are in accordance with principles and definitions presented in the COGE Handbook.
4. The following table sets forth the estimated future net revenue (before deduction of income taxes) attributed to proved plus probable reserves, estimated using forecast prices and costs and calculated using a discount rate of 10 percent, included in the reserves data of Zargon evaluated by us for the year ended December 31, 2012, and identifies the respective portions thereof that we have evaluated and reported on to Zargon's board of directors:

Independent Qualified Reserves Evaluator or Auditor	Description and Preparation Date of Evaluation Report	Location of Reserves	Net Present Value of Future Net Revenue (thousands before income taxes, 10% discount rate)			
			Audited	Evaluated	Reviewed	Total
McDaniel & Associates Consultants Ltd.	February 20, 2013	Canada	\$nil	\$429,742	\$nil	\$429,742
		United States	\$nil	\$43,765	\$nil	\$43,765

5. In our opinion, the reserves data respectively evaluated by us have, in all material respects, been determined and are in accordance with the COGE Handbook, consistently applied. We express no opinion on the reserves data that we reviewed but did not audit or evaluate.
6. We have no responsibility to update our report referred to in paragraph 4 for events and circumstances occurring after their respective preparation date.
7. Because the reserves data are based on judgements regarding future events, actual results will vary and the variations may be material.

Executed as to our report referred to above:

(signed) McDaniel & Associates Consultants Ltd.  
Calgary, Alberta  
February 20, 2013

## APPENDIX C

### MANDATE & TERMS OF REFERENCE OF THE AUDIT AND RESERVES COMMITTEE

#### Role and Objective

The Audit and Reserves Committee (the "Committee") is appointed by the Board of Directors (the "Board") of Zargon Oil & Gas Ltd. ("Zargon" or the "Corporation"), to which the Board has delegated its responsibility for oversight of the nature and scope of the annual audit, management's reporting on internal accounting standards and practices, financial information and accounting systems and procedures, financial reporting and statements, the audited financial statements and other mandatory disclosure releases containing financial information, and reviewing the annual independent report of the Corporation's petroleum and natural gas reserves and recommending all, for board of director approval.

#### Membership of Committee

1. The Committee shall be comprised of at least three (3) directors of Zargon, none of whom are members of management of Zargon and all of whom are "independent" (as such term is used in Multilateral Instrument 52-110 - Audit Committees "MI 52-110" and National Instrument 51-101 - Standards of Disclosure for Oil and Gas Activities "NI 51-101"). Committee members shall also meet the independence requirements of the regulatory bodies to which the Corporation may be subject to.
2. All of the members of the Committee shall be "financially literate". The Board has adopted the definition for "financial literacy" used in MI 52-110.
3. The Board may from time to time designate one of the members of the Committee to be the Chair of the Committee.

#### Mandate and Responsibilities of Committee

1. The Committee shall, in addition to any other duties and responsibilities specifically delegated to it by the Board, generally assume responsibility for developing the approach of the Corporation to matters concerning all financial information and disclosure and all petroleum and natural gas reserves information and disclosure and, from time to time, shall review and make recommendations to the Board as to such matters. Specifically, the Committee will have the authority and responsibility for:
  - a) Audit Matters:
    - (i) To assist directors meet their responsibilities (especially for accountability) in respect of the preparation and disclosure of the financial statements of Zargon and related matters;
    - (ii) To provide better communication between directors and external auditors;
    - (iii) To enhance the external auditor's independence;
    - (iv) To increase the credibility and objectivity of financial reports;
    - (v) To strengthen the role of the outside directors by facilitating in depth discussions between directors on the Committee, management and external auditors;



- (vi) It is the responsibility of the Committee to oversee the work of the external auditors, including resolution of disagreements between management and the external auditors regarding financial reporting;
- (vii) It is the responsibility of the Committee to satisfy itself on behalf of the board with respect to Zargon's Internal Control Systems:
  - A. Identifying, monitoring and mitigating business risks; and
  - B. Ensuring compliance with legal, ethical and regulatory requirements.
- (viii) It is a primary responsibility of the Committee to review the annual financial statements of Zargon prior to their submission to the board of directors for approval. The process should include but not be limited to:
  - A. Reviewing changes in accounting principles, or in their application, which may have a material impact on the current or future years' financial statements;
  - B. Reviewing significant accruals, reserves or other estimates such as the impairment test calculation;
  - C. Reviewing accounting treatment of unusual or non-recurring transactions;
  - D. Ascertaining compliance with covenants under loan agreements;
  - E. Reviewing disclosure requirements for commitments and contingencies;
  - F. Reviewing adjustments raised by the external auditors, whether or not included in the financial statements;
  - G. Reviewing unresolved differences between management and the external auditors; and
  - H. Obtain explanations of significant variances with comparative reporting periods.
- (ix) The Committee is to review the financial statements, prospectuses, management discussion and analysis ("MD&A"), annual information forms ("AIF") and all public disclosure containing audited or unaudited financial information before release and prior to board approval. The Committee must be satisfied that adequate procedures are in place for the review of Zargon's disclosure of all other financial information and shall periodically access the accuracy of those procedures.
- (x) With respect to the appointment of external auditors by the board, the Committee shall:
  - A. Recommend to the board the appointment of the external auditors;
  - B. Recommend to the board the terms of engagement of the external auditor, including the compensation of the auditors and a confirmation that the external auditors shall report directly to the Committee;

- C. When there is to be a change in auditors, review the issues related to the change and the information to be included in the required notice to securities regulators of such change; and
  - D. Review and approve any non-audit services to be provided by the external auditors' firm and consider the impact on the independence of the auditors.
- (xi) Review with external auditors (and internal auditor if one is appointed by Zargon) their assessment of the internal controls of Zargon, their written reports containing recommendations for improvement, and management's response and follow-up to any identified weaknesses. The Committee shall also review annually with the external auditors their plan for their audit and, upon completion of the audit, their reports upon the financial statements of Zargon and its subsidiaries.
  - (xii) The Committee must pre-approve all non-audit services to be provided to Zargon or its subsidiaries by the external auditors. The Committee may delegate to one or more members the authority to pre-approve non-audit services, provided that the member report to the Committee at the next scheduled meeting such pre-approval and the member comply with such other procedures as may be established by the Committee from time to time.
  - (xiii) The Committee shall review risk management policies and procedures of Zargon (i.e. hedging, litigation and insurance).
  - (xiv) The Committee shall establish a procedure for:
    - A. The receipt, retention and treatment of complaints received by Zargon regarding accounting, internal accounting controls or auditing matters; and
    - B. The confidential, anonymous submission by employees of Zargon of concerns regarding questionable accounting or auditing matters.
  - (xv) The Committee shall review and approve Zargon's hiring policies regarding employees and former employees of the present and former external auditors of Zargon.
  - (xvi) The Committee shall have the authority to investigate any financial activity of Zargon. All employees of Zargon are to cooperate as requested by the Committee.
  - (xvii) The Committee may retain persons having special expertise and/or obtain independent professional advice to assist in filling their responsibilities at the expense of Zargon without any further approval of the board.
- b) Reserves Matters:
- (i) In conjunction with the Corporation's senior engineering management, meet with the independent evaluating engineers being considered for appointment to review their qualifications and independence to ensure the independent evaluating engineers being considered for appointment are technically qualified and competent, are independent of management and to establish the terms of their engagement;

- (ii) After consultation with the Corporation's senior engineering management recommend to the Board the appointment of the independent evaluating engineers to assist the Corporation in the annual review of its petroleum and natural gas reserves;
- (iii) In consultation with the Corporation's senior engineering management determine the scope of the annual review of the petroleum and natural gas reserves by the independent evaluating engineers, having regard to regulatory reporting requirements;
- (iv) Review both the procedures for providing petroleum and natural gas reserves information to the independent evaluating engineers and the information used by the independent evaluating engineers to enable the independent evaluating engineers to provide a report that will meet regulatory reporting requirements;
- (v) In consultation with the Corporation's senior engineering management and the independent evaluating engineers:
  - A. Determine whether any restrictions affect the ability of the independent evaluating engineers to report on reserves data without reservations; and
  - B. Review the reserves data and the report of the independent evaluating engineers.
- (vi) Recommend to the Board for filing, the report from the independent evaluating engineers and/or senior engineering management on the Corporation's petroleum and natural gas reserves data;
- (vii) Ensure the disclosure to the public on the Corporation's petroleum and natural gas reserves is in compliance with regulatory requirements;
- (viii) Review any proposals to change the independent evaluating engineers and/or resolve any differences between the independent evaluating engineers and management;
- (ix) Meet on an annual basis with the Corporation's senior engineering management and/or the independent evaluating engineers of the Corporation to review and consider the evaluation of the Corporation's petroleum and natural gas reserves;
- (x) Meet separately with the independent evaluating engineers and/or senior engineering management when the Committee deems it desirable and advise the Board on the results of such meeting; and
- (xi) Co-ordinate meetings with the Corporation's senior engineering management, independent evaluating engineers and auditors as required to address matters of mutual concern in respect of the Corporation's evaluation of petroleum and natural gas reserves.

### **Meeting and Administrative Matters**

1. Meetings of the Committee should be scheduled to take place at least four (4) times per year. Special meetings may be convened as required upon the request of the Committee Chairman or the CEO. The President and Chief Executive Officer and the Vice President, Finance and Chief Financial Officer shall

attend meetings of the Committee, unless otherwise excused from all or part of any such meeting by the Chairman.

2. A majority of the members of the Committee shall constitute a quorum. No business may be transacted by the Committee except at a meeting of its members at which a quorum of the Committee is present or by a resolution in writing signed by all the members of the Committee. Meetings may occur via telephone or teleconference.
3. Any members of the Committee may be removed or replaced at any time by the Board and shall cease to be a member of the Committee as soon as such member ceases to be a director. The Board of directors may fill vacancies on the Committee by appointment from among its members. If and whenever a vacancy shall exist on the Committee, the remaining members may exercise all its powers so long as a quorum remains. Subject to the foregoing, each member of the Committee shall hold such office until the close of the next annual meeting of shareholders following appointment as a member of the Committee.
4. The Committee may invite such officers, directors and employees of the Corporation as it may see fit from time to time to attend at meetings of the Committee and assist thereat in the discussion and consideration of the matters being considered by the Committee.
5. The time at which and place where the meetings of the Committee shall be held and the calling of meetings and the procedure in all respects at such meetings shall be determined by the Committee, unless otherwise determined by the by-laws of the Corporation or by resolution of the Board.
6. Unless otherwise designated by the Board, the members of the Committee shall elect a Chairman from among the members and the Chairman shall preside at all meetings of the Committee. The Chairman of the Committee shall have a second and deciding vote in the event of a tie. In the absence of the Chairman, the members of the Committee shall appoint one of their members to act as Chairman. Notwithstanding the foregoing, in all circumstances the Chairman must be an outside director, unrelated to the Corporation.
7. Minutes of the Committee will be recorded and maintained and circulated to directors who are not members of the Committee or otherwise made available at a subsequent meeting of the Board.
8. Agendas, approved by the Chair, will be circulated to Committee members along with background information on a timely basis prior to the Committee meetings.
9. The Committee may obtain information from any employee of the Corporation and the Corporation's agents that it may require to carry out this mandate. The Committee may retain persons having special expertise and may obtain independent professional advice to assist in fulfilling its responsibilities at the expense of the Corporation, as determined by the Committee.
10. Any issues arising from these meetings that bear on the relationship between the Board and management should be communicated to the Chairman of the Board by the Committee Chair.
11. The Committee shall meet with the external auditor at least once per year (in connection with the preparation of the year end financial statements) and at such other times as the external auditor and the Committee consider appropriate.
12. Review annually the Committee mandate and terms of reference and recommend any changes to the Board.