ORCA

ORCA EXPLORATION GROUP INC.

2012 Annual Report

ORCA EXPLORATION GROUP INC.

is an international public company engaged in hydrocarbon exploration, development and supply of gas in Tanzania and oil appraisal and gas exploration in Italy. Orca Exploration trades on the TSXV under the trading symbols ORC.B and ORC.A.

GLOSSARY

mcf	Thousands of standard cubic feet	*1P*	Proven reserves
MMcf	Millions of standard cubic feet	*2P*	Proven and probable reserves
Bcf	Billions of standard cubic feet	*Kwh*	Kilowatt hour
Tcf	Trillions of standard cubic feet	*MW*	Megawatt
MMcfd	Millions of standard cubic feet per day	*US$*	US dollars
MMbtu	Millions of British thermal units	*CDN$*	Canadian dollars
HHV	High heat value	*bar*	Fifteen pounds pressure per square inch
LHV	Low heat value		

FINANCIAL AND OPERATING HIGHLIGHTS

	YEAR ENDED/AS AT 31 DECEMBER		
US$'000 except where otherwise stated	**2012**	2011	Change
FINANCIAL			
Revenue	**77,259**	45,893	68%
Profit before taxation	**35,454**	15,320	131%
Operating netback *(US$/mcf)*	**2.82**	2.05	38%
Cash and cash equivalents	**16,047**	34,680	(54%)
Working capital (1)	**46,820**	56,006	(16%)
Shareholders' equity	**125,935**	106,659	18%
Earnings per share - basic *(US$)*	**0.53**	0.23	130%
Earnings per share - diluted *(US$)*	**0.52**	0.22	136%
Funds flow from operating activities	**45,949**	22,658	103%
Funds per share from operating activities - basic *(US$)*	**1.33**	0.65	105%
Funds per share from operating activities - diluted *(US$)*	**1.30**	0.63	106%
Net cash flows from operating activities	**30,568**	4,577	568%
Net cash flows per share from operating activities - basic *(US$)*	**0.88**	0.13	577%
Net cash flows per share from operating activities - diluted *(US$)*	**0.86**	0.13	562%
OUTSTANDING SHARES ('000)			
Class A shares	**1,751**	1,751	0%
Class B shares	**32,892**	32,746	0%
Options	**1,922**	3,057	(37%)
OPERATING			
Additional Gas sold *(MMcf)* - industrial	**3,813**	2,742	39%
Additional Gas sold *(MMcf)* - power	**16,832**	14,722	14%
Additional Gas sold *(MMcfd)* - industrial	**10.4**	7.5	39%
Additional Gas sold *(MMcfd)* - power	**46.0**	40.3	14%
Additional Gas sold *(MMcfd)*	**56.4**	47.8	18%
Average price per mcf *(US$)* - industrial	**9.30**	10.05	(7%)
Average price per mcf *(US$)* - power	**3.18**	2.77	15%
ADDITIONAL GAS GROSS RECOVERABLE RESERVES TO END OF LICENCE *(BCF)* (2)			
Proved	**429**	469	(9%)
Probable	**60**	79	(24%)
Proved plus probable	**489**	548	(11%)
NET PRESENT VALUE, DISCOUNTED AT 10% *(US$ million)* (2)			
Proved	**354**	328	8%
Proved plus probable	**386**	351	10%

(1) *Working capital as at 31 December 2012 includes a TANESCO receivable of US$33.3 million (2011: US$24.2 million) and a net Songas receivable of US$5.9 million (2011 : US$0.7 million).*

(2) *Based on report prepared by Orca Exploration's independent reserve evaluator McDaniel & Associates Consultants Ltd. dated effective December 31, 2012, which was prepared in accordance with definitions, standards and procedures contained in the Canadian Oil and Gas Evaluation Handbook.*

HIGHLIGHTS

- Orca Exploration operated its Tanzania Songo Songo gas field at maximum plant and pipeline capacity resulting in record operating and financial results.
- Profit after tax for the year was a record US$18.3 million, or US$0.52 per share diluted, up 130% over 2011.
- An 18% increase in gas sales volumes plus a 10% increase in the average gas price, together with higher cost recoveries as a result of capital spending combined to double funds flow from operations over 2011 to a record US$45.8 million, or US$1.30 per share diluted.
- Capital spending in 2012 was US$54.7 million (2011: US$18.1 million) of which US$38 million was expended on SS-11 drilling and completion, US$7.9 million on preparation for SS-12 and Songo Songo West drilling, and US$7.5 million on the unsuccessful La Tosaca exploration well in Italy.
- Given TANESCO and Songas non-payments, record funds flow did not translate to cash -- balances at the end of 2012 were US$16.0 million, down 54% from 2011, net of US$54.7 million in capital spending during the year and including US$6.0 million in bank borrowings. Accordingly, the Company has incorporated a going concern note into its 2012 Consolidated Financial Statements.
- Working capital was US$46.8 million, which included a US$33.3 million receivable from TANESCO – at the end of the year the Company had drawn US$6.0 million of a US$10.0 million senior debt facility which was set up in Q3 to assist in financing TANESCO receivables.
- Average gas prices up 10% in 2012 to US$4.31/Mcf (2011: US$3.92/Mcf), industrial gas prices were down 7.5% in 2012 to US$9.31/Mcf from changes in the sales mix, and average power sector gas prices increased 15% over 2011 to US$3.18/mcf from US$2.77/mcf, pursuant to the PGSA and ARGA.
- Current TANESCO receivable is US$49.3 million, or about US$0.90 per share on a net basis – Government of Tanzania has raised US$600 million in debt and US$100 million in World Bank budget support finance and assured the Company that arrears will be paid from these proceeds.
- Songo Songo PSA and GNT issues remain unresolved, however the Company has continued to work in cooperation with the Government and has tabled a PSA amendment for the Government's consideration.
- Establishing commercial terms for future incremental gas sales is a key condition to the Company's commitment to Songo Songo development – the Company has recently entered into discussions with TPDC concerning a gas sales agreement.
- Government of Tanzania succeeded in arranging a US$1.2 billion project financing with the China Exim Bank to deliver a major natural gas infrastructure expansion project which was inaugurated in November 2012 and is expected to be completed by the end of 2014.
- On 1st November 2012, the Government of Tanzania issued a draft natural gas policy which contemplates a restructuring of TPDC, strategic participation throughout the upstream, midstream and downstream sectors, ownership and control over gas infrastructure and setting domestic natural gas prices – at the request of the Government, the Company submitted its views on the draft policy and a second draft policy is expected in the near future.
- The La Tosca well in the Longastrino exploration block in the Po Valley, Northern Italy was drilled in August and has been plugged and abandoned having encountered gas shows - Orca has earned a 70% working interest and, subject to government approval, operatorship of the block. The Company intends to review the technical and drilling data to determine whether or not to continue exploration on the block. The offshore Italy Elsa appraisal well is now expected to be drilled in 2014.
- With the completion of SS-11, brought onstream in October 2012, the Company has substantially upgraded the quality of its wellbore portfolio. Subsequent to bringing SS-11 onstream, the SS-9 and SS-3 wells were taken off production leaving the field producing at maximum capacity and having no redundancy.
- Songo Songo gas reserves remain solid with a 9% decrease in Songo Songo's Total Proved Additional Gas reserves to the end of the license period, with no change on a life of field basis; total Additional Gas production of 20.6 Bcf during the year; an 11% decrease in the Proved plus Probable Additional Gas reserves on a Gross Company life of license basis from 548.5 Bcf to 489.3 Bcf. The decrease is primarily due to the delay in the expansion project which has moved probable reserves into possible reserves on a life of licence basis. NPV10% 2P was estimated at US$386 million.

CHAIRMAN & CEO'S LETTER TO THE SHAREHOLDERS

Increased gas sales and profitability

To meet constant high demand for natural gas production throughout 2012, Orca Exploration operated its Tanzania Songo Songo gas field at maximum plant and pipeline capacity resulting in record operating and financial results. Profit after tax for the year was a record US$18.3 million, or US$0.52 per share diluted, up 130% over 2011. Income included a US$8.3 million write down of costs associated with the unsuccessful La Tosca, Italy well.

The increase in gas sales volumes plus a 10% increase in the average gas price, together with higher cost recoveries as a result of capital spending during the year, combined to double funds flow from operations over 2011 to a record US$45.9 million, or US$1.30 per share diluted. Taking out capital cost recoveries, funds from operations in 2012 would have been approximately US$25 million, or US$0.70 per share. The difficulty was that given the TANESCO non-payments, this funds flow did not translate to cash. Capital spending in 2012 was US$54.7 million (2011: US$18.1 million) of which US$38 million was expended on SS-11 drilling and completion, US$7.9 million on preparation for SS-12 and Songo Songo West drilling, and US$7.5 million on the unsuccessful La Tosaca exploration well in Italy. Cash balances at the end of 2012 were US$16.0 million, down 54% from 2011, net of capital spending during the year and including US$6.0 million in bank borrowings. Working capital was US$47.3 million, which included a US$33.3 million receivable from TANESCO. At the end of the year the Company had drawn US$6.0 million of a US$10.0 million senior debt facility which was set up in Q3 to assist in financing TANESCO receivables.

Average natural gas sales prices were up 10% in 2012 to US$4.31/Mcf from US$3.92/Mcf the year prior, largely a result of higher prices provided under the Portfolio Gas Sales Agreement ("PGSA") with TANESCO. While world energy prices were flat year over year, industrial gas prices were down 7.5% in 2012 to US$9.31/Mcf from changes in the sales mix. Average power sector gas prices increased 15% over 2011 to US$3.18/mcf from US$2.77/mcf, a result of a step change in the wellhead price in July (after an annual 2% indexation) as provided under the PGSA and ARGA from US$2.06/MMbtu to US$2.76/MMbtu.

Aided by the drilling and completion of the high productivity SS-11 well at mid-year, the Company posted record Additional Gas production of 56.4 million cubic feet per day ("MMcfd") in 2012, up 18% over 2011. High margin industrial sales volumes increased by 39% to 10.4 MMcfd (2011: 7.5 MMcfd). Demand for power increased gas sales to the power sector by 14% to 46.0 MMcfd (2011: 40.3 MMcfd).

A challenging year

Despite these achievements, 2012 was the most challenging year the Company has ever faced. Tanzania's state-owned utility TANESCO has not stayed current, let alone paid down arrears for natural gas production, leaving Orca currently with US$49.3 million in receivables from TANESCO.

Orca recognizes that increasing natural gas development is at the core of Tanzania's energy strategy. But even with all the offshore exploration in the country, significant new gas production in Tanzania is still years away. This leaves Orca as substantially the only producer of natural gas in Tanzania, currently supplying 99% of gas production, which in turn powers some 50% of the national power grid. This is a position of great responsibility and Orca continues to work closely with the Government of Tanzania in seeking solutions to resolve outstanding financial issues and move natural gas development at Songo Songo forward.

At the same time Orca's responsibility to its shareholders is also of the highest priority. Considerable uncertainty still hangs over the Company and management's top priority is to de-risk the business by reducing that uncertainty. Equity markets have given us this message loud and clear. The market currently capitalises our Tanzania business, net of working capital, at approximately US$35 million, less than one-year's cash flow. This is unacceptable for all concerned. To restore confidence and secure a future which addresses profitability and still maintains its responsibilities to the people of Tanzania, your Company is working closely with the Government towards a full and fair resolution of all outstanding issues including:

- the collection of TANESCO arrears and security over future payments;
- resolution of all Government Negotiating Team ("GNT") matters; and
- resolution of commercial terms affecting future incremental gas sales.

De-risking the business

TANESCO receivables, the largest single issue facing the Company, must be fairly and quickly resolved. Going into 2012 TANESCO owed the Company US$24.2 million. Over much of the year, TANESCO receivables stayed at approximately this level. However by the end of 2012, TANESCO was unable to stay current and the receivable had grown to US$33.3 million. Today, TANESCO owes the Company US$49.3 million. Net of obligations relating to this amount, the net TANESCO receivable equates to approximately US$0.90 per share, or roughly 40% of the Company's current market capitalisation.

Whilst the Company can currently maintain operations from industrial gas sales alone, it does require payments from TANESCO to comply with our obligations to pay VAT and Excise Tax to the Tanzania Revenue Authority ("TRA") against TANESCO invoices. Without payments from TANESCO Orca may need to reduce operations to avoid accumulating any further liabilities with the TRA.

TANESCO receivables -- common ground exists for a solution

Orca Exploration is completely aligned with the Government of Tanzania insofar as we agree that a viable state utility is a critical component to delivering on Tanzania's industrialization and economic growth strategies. Despite TANESCO's current financial situation we also remain confident that power prices reflecting the real cost of service in the country, together with a changing fuel mix weighted towards natural gas, can restore the state utility to a viable business model by the time the pipeline expansion is commissioned in 2014.

In this situation the Government has not been idle. One of the major accomplishments of the Government of Tanzania in 2012 was to arrange the financing of a US$1.2 billion natural gas infrastructure project, critical to delivering natural gas to markets, and specifically to power generation hubs. The Government has also been working diligently to arrange financing to address its budget needs and deal with the TANESCO arrears, which not only affect Orca, but indeed ripple through the entire Tanzania economy. Recently, the Government closed a US$600 million debt financing in international capital markets and further received US$100 million in a first tranche of a World Bank Tanzania budget support package. We have been assured by the Government that it is their intention to repay all of the TANESCO arrears from these proceeds and that a significant payment would be made to the Company in the near future. Prompt payment of the TANESCO arrears will clear a critical condition in our ability to proceed with additional Songo Songo development.

Resolution of PSA issues

The dispute over the Songo Songo Production Sharing Agreement ("PSA") and other matters have cast a shadow over the Company since allegations were made in November 2011. Following the establishment of a Government Negotiating Team ("GNT") in February 2012, the Company entered into discussions culminating in negotiation sessions during July 2012. Out of this came a framework for an agreement on several major issues including PSA profit sharing ratios, Tanzania Petroleum Development Corporation ("TPDC") back-in rights, TANESCO payments, downstream unbundling and disputed cost pool recoveries. While a full resolution was not achieved by the end of the year as originally envisaged, the Company has continued discussions in good faith and in April 2013 Orca proposed an amendment to the PSA, which is now in front of the Government for its consideration.

Ensuring future economic viability

Before making commitments for further development at Songo Songo, the Company needs to establish that the commercial terms of future gas sales will ensure economic viability. Currently the government's Natural Gas Infrastructure Project is contemplating allocating additional gas from Songo Songo and Mnazi Bay to power markets in the Dar es Salaam area. The project, which we understand is financed on a standalone basis, will require the repayment of loans to come exclusively from tariffs revenues derived from the pipeline and infrastructure. Accordingly, transportation and processing tariffs will be an important component of the cost of delivering gas to the markets, and in turn will have an impact on both the net back price to gas producers and the delivered gas price to TANESCO as the power producer.

To deliver the lowest cost power to Tanzanians, the Government has the objective of purchasing gas at the lowest possible price, whilst the producers will be seeking a price which will deliver the appropriate economic returns. Bridging these differing objectives will be the subject of negotiations between the producers and TPDC in its capacity as gas aggregator. With the support of the Ministry of Energy and Mines ("MEM") the Company has recently entered into negotiations with TPDC for Additional Gas sales.

Natural Gas Infrastructure Project initiated

During the year, the Government of Tanzania succeeded in arranging a US$1.2 billion project financing with the Export-Import Bank of China to deliver a major infrastructure expansion project. The 532km Mnazi Bay to Dar es Salaam Gas Pipeline Project is planned to tie into expanded Songo Songo facilities onshore at Somanga Funga and provide Orca with much needed process and pipeline capacity expansion for Songo Songo gas.

On 8 November 2012, His Excellency Jakaya Kikwete, President of the United Republic of Tanzania, formally commissioned the start of pipeline construction. The Company has had initial technical consultations with project manager and Songo Songo partner TPDC in mid-November and consultations are ongoing. The Company's current objective is to have approximately 190 MMcfd of total gas (or approximately 150 MMcfd Additional Gas sales) onstream by the end of 2014. A field development plan is being prepared for discussion with TPDC. Approximately 120 MMcfd would be expected to be dedicated to the expanded facilities and pipeline, with the balance to be processed and transported through the existing Songas facilities.

Tanzania natural gas policy development

In November 2012, the Government of Tanzania issued a draft natural gas policy for review and consultation. Natural gas discoveries in the country, reported by the Government at 36 TCF of resources, have accelerated the need for Tanzania to develop a comprehensive framework for natural gas exploration and development. From a policy perspective, the Government of Tanzania is seeking to participate across the upstream, mid-stream and downstream sectors of the industry through a national oil company and to regulate the industry through a new regulatory body.

The Government's objective is also to promote the development of facilities for natural gas processing, liquefaction, transportation, storage and distribution. To achieve this, the draft policy contemplates a restructured TPDC, acting as a national aggregator of natural gas, owning and managing natural gas infrastructure. The draft policy does not contemplate a market-driven gas price structure, but rather a government role in establishing "an appropriate pricing structure" which can both encourage economic use of the system capacities as well as provide incentives for promoting investment.

The policy also contemplates strategic involvement by the government in the LNG value chain and the promotion of efficient LNG production. As part of the government's role, as stewards of the country's national resources, the draft policy also addresses the management of natural gas revenues, local content, community & social responsibilities and issues of transparency and accountability.

The Oil and Gas Association of Tanzania ("OGAT"), of which Orca is a member, has prepared a submission on behalf of industry on the draft policy. The Company also submitted its own views on the draft policy at the request of the Government of Tanzania, recognizing that Orca is the principal producer of natural gas currently and for the near-to-medium term. The Government has been considering the views of the Company and many other stakeholders and international parties and is expected to release a second draft policy in the near future.

OPERATIONS

Tanzania

Operationally the Company substantially upgraded the quality of its wellbore inventory at Songo Songo during the year. SS-11 was drilled as a directional well from onshore Songo Songo Island and was completed in May 2012. The well entered the top Neocomian reservoir at a 40 degree angle at its highest position in the Songo Songo field. A total of 352 meters of total gas reservoir was encountered and extensive new reservoir data was acquired during the drilling of the well.

During the third quarter Orca brought SS-11 on-stream maintaining and strengthening field deliverability. SS-11 is currently producing approximately 38 MMcfd of natural gas through a six-inch diameter Technip Coflexip® pipe laid along the seabed to achieve an efficient natural cooling of the gas stream prior to the plant inlet. The installation involved developing innovative solutions to a number of engineering challenges which were met entirely by local Tanzanian contractors and suppliers who delivered the project on budget and in approximately one-third the time of other solutions.

SS-11 is an important addition to the production wellbore inventory of Songo Songo. Subsequent to bringing SS-11 onstream, the SS-9 well was taken off production. A debottlenecking of the gas gathering infrastructure is currently underway with the objective of increasing the productive potential of SS-11 to over 40 MMcfd.

The SS-9 well, which was producing approximately 30 MMcfd, was planned to be shut in and used only as spare capacity until SS-12 could be drilled. During Q3, rising casing annulus pressures resulting from a tubing leak dictated that SS-9 be permanently suspended. After suspending SS-9, similar tubing integrity issues also dictated suspending SS-3. Whilst the quality of existing producing wells is much improved, there is currently no redundant capacity in the facility or pipeline until shut in wells can be worked over and/or additional wells can be drilled in the field.

Italian operations

In the Longastrino Block in the Po Valley region of Northern Italy the La Tosca farm-in well was spud on 7 August 2012 and reached total depth of 2,335 metres and was plugged and abandoned in early September having encountered gas shows. The drilling indicated a more limited reservoir sand development than expected from earlier extrapolation of data from nearby wells. Total cost of the well to the Company was US$7.5 million, which together with past costs was written off during the year. As a result of the drilling, the Company has earned a 70% working interest and once approved as the new operator, Orca intends to review the technical and drilling data to determine whether to continue exploration on the block.

During the year, the Elsa offshore Italy opportunity cleared an important regulatory hurdle. Legislative Decree 83/2012 (the "Decree"), published on 26 June 2012 was approved by both houses of the Italian Parliament with no substantial modifications. On 12 August 2012, the Decree became law. The new legislation removes uncertainty concerning exploration, development and production activities in Italian waters clearing the way for a new drilling application. A well is now expected to be drilled following finalisation of an environmental impact study currently expected in 2014. Orca will not be liable to any costs associated with the drilling of Elsa-2 until a rig contract is signed.

Management and Board changes

Three new executive appointments were made during the year and two new directors were elected in June 2012. Beer van Straten was named Chief Operating Officer replacing Dale Rollins who resigned in March 2012. Mr. van Straten is responsible for the Company's field operations including future large scale development and exploration drilling programmes in Tanzania. Robert S. Wynne was appointed Chief Financial Officer & Director in June 2012 following the resignation of Nigel Friend who had been a valued member of Orca's management team for the past seven years. In October 2012, David K. Roberts was appointed as Orca's Vice President Operations and Tanzania Country Manager based in Dar es Salaam. William H. Smith was also elected to the Board of Directors in June 2012.

Mr. van Straten is a senior international oil and gas industry executive with over 25 years of high level exploration, production and commercial experience in the North Sea, Middle East and Africa. He has been associated with Orca since June 2010. From 1999 to 2006 Mr. Wynne and Mr. Roberts were instrumental in managing PanOcean Energy's growth in Gabon from 400 bopd to 20,000 bopd, and Mr. Smith brings additional hands on experience that helped to realise the PanOcean success.

Corporate Social Responsibility

With a 20-year history in Tanzania, the Company feels strongly about giving back to the communities in which we operate. Building upon its existing high impact social development projects, designed to deliver sustainable enhancements to the Songo Songo and Kilwa District communities, Orca has continued to expand its Corporate Social Responsibility Programme in Tanzania during the year. Focussed on the communities' critical educational and health needs, Orca has committed in excess of US$250,000 to its existing projects, which include enhancement of teaching facilities on Songo Songo Island; continuation of teacher development by sponsoring future staff through teacher training colleges in Dar es Salaam; sponsoring a further 10 students from Songo Songo through secondary education in Dar es Salaam; and continuing to provide routine healthcare and health awareness training to the Island's people. Potentially with increased impact however, Orca has contributed a further US$130,000 in 2012 to the design and delivery of a bespoke technology-based English Language course to selected secondary schools in the Kilwa District. The six-week intensive training course is delivered, critically, at the start of a child's secondary education and is designed to aide learning for students transitioning from a primary, Kiswahili-based curriculum to a secondary, English-based curriculum. Extremely encouraging test results from pilot courses suggest the course delivers a dramatic increase in a child's ability to learn and with it significant enhancement of a child's prospects beyond graduation. The Company's intent is to continue to roll-out the course across other schools in the district in the next two to three years.

The will to create solutions

Orca and its predecessors have had a 20-year history in Tanzania, successfully partnering with the Government and the World Bank to create the first natural gas-to-electricity development and the first industrial gas market in East Africa. Comparatively recently a tremendous wealth of natural gas resources has been discovered in Tanzania and the country is now faced with new challenges in realizing and protecting this wealth for its people and future generations. The potential to realize such a prize has placed significant pressure on the Government of Tanzania to establish policies and frameworks to guide the fledgling industry and maximize the benefits that can follow. Our new Orca team is working in a spirit of cooperation and collaboration with the new leadership in the Ministry of Energy and Minerals to find a way to better align our interests and remove impediments to development and growth. We remain optimistic that the will exists amongst all stakeholders to create equitable long-term solutions.

W. David Lyons
Chairman & CEO

26 April 2013

GAS RESERVES

In accordance with National Instrument 51-101 Standards of Disclosure for Oil and Gas Activities, the independent petroleum engineers, McDaniel & Associates Ltd. prepared a report dated April 2013 that assessed the Orca Exploration natural gas reserves based on information on the Songo Songo Field and Songo Songo North as at 31 December 2012 (the "McDaniel Report"). A summary of the remaining Additional Gas reserves on a life of license and life of field basis are presented below. The Total Proved (1P) and Proved plus Probable (2P) reserves are based on production to the end of the license period (October 2026).

During the course of 2012 no significant geological or geophysical data has been acquired on or close to the Songo Songo field that might allow a re-assessment of the volumetric gas initially in place ("GIIP") and reserves. On a Gross Company basis there has been a 9% decrease in Songo Songo's Total Proved Additional Gas reserves to the end of the license period, with no change on a life of field basis, with a total Additional Gas production of 20.6 Bcf during the year. There has been a 11% decrease in the Proved plus Probable Additional Gas reserves on a Gross Company life of license basis from 548.5 Bcf to 489.3 Bcf. The decrease is primarily due to the delay in the expansion project which has moved probable reserves into possible reserves on a life of licence basis.

The gross and net Company Additional Gas reserves to end of license are as follows:

SONGO SONGO ADDITIONAL GAS RESERVES TO OCTOBER 2026 *(Bcf)*	2012		2011	
	Gross [1]	*Net* [2]	*Gross*	*Net*
Independent reserves evaluation				
Proved producing	**280.0**	**181.2**	316.3	215.4
Proved undeveloped	**149.2**	**87.8**	152.8	82.2
Total proved *(1P)*	**429.2**	**269.0**	469.1	297.6
Probable	**60.1**	**37.3**	79.4	48.9
Total proved and probable *(2P)*	**489.3**	**306.3**	548.5	346.5

(1) *Gross equals the gross reserves that are available for the Company after estimating the effect of the TPDC back in (see below).*

(2) *Net equals the economic allocation of the Gross reserves to the Company as determined in accordance with the Production Sharing Agreement.*

SONGO SONGO ADDITIONAL GAS RESERVES TO END OF FIELD LIFE *(Bcf)*	2012		2011	
	Gross [1]	*Net* [2]	*Gross*	*Net*
Independent reserves evaluation				
Proved Producing	**492.6**	**314.8**	539.8	355.0
Proved Undeveloped	**54.2**	**34.6**	6.5	0.4
Total Proved *(1P)*	**546.8**	**349.4**	546.3	355.4
Probable	**111.4**	**68.2**	127.6	79.2
Total Proved and Probable *(2P)*	**658.2**	**417.6**	673.9	434.6

(1) *Gross equals the gross reserves that are available for the Company after estimating the effect of the TPDC back in (see below).*

(2) *Net equals the economic allocation of the Gross reserves to the Company as determined in accordance with the Production Sharing Agreement.*

The McDaniel Report has assumed that TPDC will exercise its right to 'back in' to the field development by contributing 20% of the costs of the future wells, including SS-10 and SS-11, and a proportion of the infrastructure and operating costs, in return for a 20% increase in the profit share for the production emanating from these wells. McDaniel has taken the view that this 'back in' right should be treated as a TPDC working interest and therefore the Gross reserves have been adjusted for the volumes of Additional Gas that are allocated to TPDC for their working interest share. The implications and workings of the 'back in' are currently being discussed with MEM as part of the conclusion of the GNT process and may lead to future modifications in the way the Gross Company reserves are calculated.

For the purpose of calculating the Gross Additional Gas reserves, McDaniel has assumed in its 2P case that 162 Bcf (2011: 171 Bcf) or an average of 13.5 Bcf per annum will be required to meet the demands of the Protected Gas users from 1 January 2013 to 31 July 2024. During 2012, the Protected Gas users consumed 14.4 Bcf.

The principal assumptions used by McDaniel in its evaluation of the Tanzanian PSA are as follows:

	Additional Gas Price 1P	Gross Additional Gas Volumes 1P	Additional Gas Price 2P	Gross Additional Gas Volumes 2P
Year	*US$/mcf*	*MMcfd*	*US$/mcf*	*2P MMcfd*
2013	4.84	50.97	4.84	53.45
2014	4.91	53.44	4.92	55.99
2015	6.27	129.97	6.06	134.92
2016	6.34	129.97	6.17	134.92
2017	6.42	129.97	6.29	134.92
2018	6.51	129.97	6.40	134.92
2019	6.60	129.97	6.50	134.92
2020	6.69	115.68	6.60	134.92
2021	6.78	94.97	6.70	122.76
2022	6.87	78.25	6.83	102.74
2023	6.96	62.56	6.95	86.53
2024	7.06	64.97	7.06	86.98
2025	7.18	71.97	7.15	96.75
2026	7.27	64.11	7.29	79.30

Present value of reserves

The estimated value of the Songo Songo reserves on a life of license basis based on the assumptions on production and pricing are as follows:

	2012			2011		
US$ millions	*5%*	*10%*	*15%*	*5%*	*10%*	*15%*
Proved Producing	**312.8**	**226.2**	**172.0**	301.3	209.3	152.4
Proved Undeveloped	**148.5**	**127.7**	**107.5**	139.2	118.9	99.2
Total Proved *(1P)*	**461.3**	**353.9**	**279.5**	440.5	328.2	251.6
Probable	**51.9**	**31.6**	**19.4**	39.9	22.8	13.5
Total Proved and Probable *(2P)*	**513.2**	**385.5**	**298.9**	480.4	351.0	265.1

There has been a 10% increase on the 2P present value at a 10% discount basis from US$351 million to US$386 million on a life of licence basis. The increase is due to several factors: the increase in industrial sales prices to reflect the correlation between the price of Brent and Heavy Fuel Oil (the alternative fuel against which gas prices are set for industrial customers) and the increase in the Power price to reflect the current terms under which volumes in excess of 36 MMcfd are invoiced to the Power sector, the increase in cost of operations and the level of capital expenditure together with the timing of capital expenditure. These factors together have led to a positive increase in the present value of cash flows in excess of the absolute increase in cash flow as a result of the timing of Additional Profit Tax payments.

MANAGEMENT'S DISCUSSION & ANALYSIS

FORWARD LOOKING STATEMENTS

THIS MD&A OF FINANCIAL CONDITIONS AND RESULTS OF OPERATIONS SHOULD BE READ IN CONJUNCTION WITH THE AUDITED CONSOLIDATED FINANCIAL STATEMENTS AND NOTES THERETO FOR YEAR ENDED 31 DECEMBER 2012. THIS MD&A IS BASED ON THE INFORMATION AVAILABLE ON 26 APRIL 2013.

CERTAIN STATEMENTS IN THIS MD&A INCLUDING (I) STATEMENTS THAT MAY CONTAIN WORDS SUCH AS "ANTICIPATE", "COULD", "EXPECT", "SEEK", "MAY", "INTEND", "WILL", "BELIEVE", "SHOULD", "PROJECT", "FORECAST", "PLAN" AND SIMILAR EXPRESSIONS, INCLUDING THE NEGATIVES THEREOF; (II) STATEMENTS THAT ARE BASED ON CURRENT EXPECTATIONS AND ESTIMATES ABOUT THE MARKETS IN WHICH ORCA EXPLORATION GROUP INC., ITS SUBSIDIARIES AND AFFILIATES (COLLECTIVELY, "ORCA EXPLORATION", OR THE "COMPANY" OPERATES AND (III) STATEMENTS OF BELIEF, INTENTIONS AND EXPECTATIONS ABOUT DEVELOPMENTS, RESULTS AND EVENTS THAT WILL OR MAY OCCUR IN THE FUTURE, CONSTITUTE "FORWARD-LOOKING STATEMENTS" AND ARE BASED ON CERTAIN ASSUMPTIONS AND ANALYSIS MADE BY ORCA EXPLORATION. FORWARD-LOOKING STATEMENTS IN THIS MD&A INCLUDE, BUT ARE NOT LIMITED TO, STATEMENTS WITH RESPECT TO FUTURE CAPITAL EXPENDITURES, INCLUDING THE AMOUNT, NATURE AND TIMING THEREOF, NATURAL GAS PRICES AND DEMAND.

SUCH FORWARD-LOOKING STATEMENTS ARE SUBJECT TO IMPORTANT RISKS AND UNCERTAINTIES, WHICH ARE DIFFICULT TO PREDICT AND THAT MAY AFFECT ORCA EXPLORATION'S OPERATIONS, INCLUDING, BUT NOT LIMITED TO: THE IMPACT OF GENERAL WORLD ECONOMIC CONDITIONS AND SPECIFCALLY IN TANZANIA, ITALY AND CANADA; INDUSTRY CONDITIONS, INCLUDING THE ADOPTION OF NEW ENVIRONMENTAL, SAFETY AND OTHER LAWS AND REGULATIONS AND CHANGES IN HOW THEY ARE INTERPRETED AND ENFORCED; SANCTITY OF CONTRACT; VOLATILITY OF OIL AND NATURAL GAS PRICES; OIL AND NATURAL GAS PRODUCT SUPPLY AND DEMAND, RIG AVAILABILITY; RISKS INHERENT IN ORCA EXPLORATION'S ABILITY TO GENERATE SUFFICIENT CASH FLOW FROM OPERATIONS, THIRD PARTY FINANCE OR ASSETS SALES TO MEET ITS CURRENT AND FUTURE OBLIGATIONS; INCREASED COMPETITION; THE FLUCTUATION IN FOREIGN EXCHANGE OR INTEREST RATES; STOCK MARKET VOLATILITY; COST POOL AUDITS AND OTHER FACTORS, MANY OF WHICH ARE BEYOND THE CONTROL OF ORCA EXPLORATION.

ORCA EXPLORATION'S ACTUAL RESULTS, PERFORMANCE OR ACHIEVEMENTS COULD DIFFER MATERIALLY FROM THOSE EXPRESSED IN, OR IMPLIED BY, THESE FORWARD-LOOKING STATEMENTS AND, ACCORDINGLY, NO ASSURANCE CAN BE GIVEN THAT ANY OF THE EVENTS ANTICIPATED BY THE FORWARD-LOOKING STATEMENTS WILL TRANSPIRE OR OCCUR, OR IF ANY OF THEM DO TRANSPIRE OR OCCUR, WHAT BENEFITS ORCA EXPLORATION WILL DERIVE THEREFROM. SUBJECT TO APPLICABLE LAW, ORCA EXPLORATION DISCLAIMS ANY INTENTION OR OBLIGATION TO UPDATE OR REVISE ANY FORWARD-LOOKING STATEMENTS, WHETHER AS A RESULT OF NEW INFORMATION, FUTURE EVENTS OR OTHERWISE. ALL FORWARD-LOOKING STATEMENTS CONTAINED IN THIS DOCUMENT ARE EXPRESSLY QUALIFIED BY THIS CAUTIONARY STATEMENT.

NON-GAAP MEASURES

THE COMPANY EVALUATES ITS PERFORMANCE USING A NUMBER OF NON-GAAP (GENERALLY ACCEPTED ACCOUNTING PRINCIPLES) MEASURES. THESE NON-GAAP MEASURES ARE NOT STANDARDISED AND THEREFORE MAY NOT BE COMPARABLE TO SIMILAR MEASUREMENTS OF OTHER ENTITIES.

- **FUNDS FLOW FROM OPERATING ACTIVITIES** IS A TERM THAT REPRESENTS CASH FLOW FROM OPERATIONS BEFORE WORKING CAPITAL ADJUSTMENTS. IT IS A KEY MEASURE AS IT DEMONSTRATES THE COMPANY'S ABILITY TO GENERATE CASH NECESSARY TO ACHIEVE GROWTH THROUGH CAPITAL INVESTMENTS.
- **OPERATING NETBACKS** REPRESENT THE PROFIT MARGIN ASSOCIATED WITH THE PRODUCTION AND SALE OF ADDITIONAL GAS AND IS CALCULATED AS REVENUES LESS PROCESSING AND TRANSPORTATION TARIFFS, GOVERNMENT PARASTATAL'S REVENUE SHARE, OPERATING AND DISTRIBUTION COSTS FOR ONE THOUSAND STANDARD CUBIC FEET OF ADDITIONAL GAS. THIS IS A KEY MEASURE AS IT DEMONSTRATES THE PROFIT GENERATED FROM EACH UNIT OF PRODUCTION, AND IS WIDELY USED BY THE INVESTMENT COMMUNITY.
- **FUNDS PER SHARE FROM OPERATING ACTIVITIES** IS CALCUALATED ON THE BASIS OF THE FUNDS FLOW FROM OPERATIONS DIVIDED BY THE WEIGHTED AVERAGE NUMBER OF SHARES.
- **NET CASH FLOWS PER SHARE FROM OPERATING ACTIVITIES** IS CALCULATED AS CASH FLOW FROM OPERATIONS DIVIDED BY THE WEIGHTED AVERAGE NUMBER OF SHARES.

ADDITIONAL INFORMATION REGARDING ORCA EXPLORATION GROUP INC. IS AVAILABLE UNDER THE COMPANY'S PROFILE ON SEDAR AT *www.sedar.com*.

BACKGROUND

Tanzania

Orca Exploration Group Inc.'s (together with its subsidaries and affiliates, "Orca Exploration", or the "Company") principal operating asset is its interest in a Production Sharing Agreement ("PSA") with the Tanzania Petroleum Development Corporation ("TPDC") and the Government of Tanzania in the Republic of Tanzania. This PSA covers the exploration, development, production and marketing of certain gas from the Songo Songo gas field.

The gas in the Songo Songo field is divided between Protected Gas and Additional Gas. The Protected Gas is owned by TPDC and is sold under a 20-year gas agreement (until July 2024) to Songas Limited ("Songas"). Songas is the owner of the infrastructure that enables the gas to be delivered to Dar es Salaam, which includes a gas processing plant on Songo Songo Island, 232 kilometres of pipeline to Dar es Salaam and a 16 kilometre spur to the Wazo Hill Cement Plant.

Songas utilizes the Protected Gas (maximum 45.1 MMcfd) as feedstock for its gas turbine electricity generators at Ubungo, for onward sale to the Wazo Hill cement plant and for electrification of some villages along the pipeline route. Orca Exploration receives no revenue for the Protected Gas delivered to Songas and operates the field and gas processing plant on a 'no gain no loss' basis.

Orca Exploration has the right under the PSA to produce and market all gas in the Songo Songo field in excess of the Protected Gas requirements ("Additional Gas").

Italy

During 2010 Orca Exploration farmed in to an oil appraisal block in the Adriatic Sea in Italy and to a gas exploration prospect in the Po Valley in Northern Italy. In early August 2012, the operator of the La Tosca well in the Po Valley commenced drilling operations. On 27 August 2012 the well was plugged and abandoned having reached total depth, the gas shows encountered and data obtained during drilling having not warranted completion and testing of the well. The costs of the well have been written off in the current period.

Orca has earned a 70% working interest in the block and, subject to government approval, operatorship of the block. The Company intends to review the technical and drilling data to determine whether to continue exploration on the block.

PRINCIPAL TERMS OF THE TANZANIAN PSA AND RELATED AGREEMENTS

The principal terms of the Songo Songo PSA and related agreements are as follows:

Obligations and restrictions

(a) The Company has the right to conduct petroleum operations, market and sell all Additional Gas produced and share the net revenue with TPDC for a term of 25 years expiring in October 2026.

(b) The PSA covers the two licenses in which the Songo Songo field is located ("Discovery Blocks"). The Proven Section is essentially the area covered by the Songo Songo field within the Discovery Blocks.

(c) No sale of Additional Gas may be made from the Discovery Blocks if in Orca Exploration's reasonable judgment such sales would jeopardise the supply of Protected Gas. Any Additional Gas contracts entered into are subject to interruption. Songas has the right to request that the Company and TPDC obtain security reasonably acceptable to Songas prior to making any sales of Additional Gas from the Discovery Block to secure the Company's and TPDC's obligations in respect of Insufficiency (see (d) below).

(d) "Insufficiency" occurs if there is insufficient gas from the Discovery Blocks to supply the Protected Gas requirements or is so expensive to develop that its cost exceeds the market price of alternative fuels at Ubungo.

Where there have been third party sales of Additional Gas by Orca Exploration and TPDC from the Discovery Blocks prior to the occurrence of the Insufficiency, Orca Exploration and TPDC shall be jointly liable for the Insufficiency and shall satisfy its related liability by either replacing the Indemnified Volume (as defined in (e) below) at the Protected Gas price with natural gas from other sources; or by paying money damages equal to the difference between: (a) the market price for a quantity of alternative fuel that is appropriate for the five gas turbine electricity generators at Ubungo without significant modification together with the costs of any modification; and (b) the sum of the price for such volume of Protected Gas (at US$0.55/Mmbtu) and the amount of transportation revenues previously credited by Songas to the state electricity utility, the Tanzania Electric Supply Company ("TANESCO"), for the gas volumes.

(e) The "Indemnified Volume" means the lesser of the total volume of Additional Gas sales supplied from the Discovery Blocks prior to an Insufficiency and the Insufficiency Volume. "Insufficiency Volume" means the volume of natural gas determined by multiplying the average of the annual Protected Gas volumes for the three years prior to the Insufficiency by 110% and multiplied by the number of remaining years (initial term of 20 years) of the power purchase agreement entered into between Songas and TANESCO in relation to the five gas turbine electricity generators at Ubungo from the date of the Insufficiency.

Access and development of infrastructure

(f) The Company is able to utilise the Songas infrastructure including the gas processing plant and main pipeline to Dar es Salaam. Access to the pipeline and gas processing plant is open and can be utilised by any third party who wishes to process or transport gas. Ndovu Resources Limited, with support from TPDC and the Ministry of Energy and Mines ("MEM"), has indicated that they wish to tie into the gas processing plant on Songo Songo Island and sell up to 10 MMcfd from their Kiliwani North field. The Tanzania Natural Gas Infrastructure Project contemplates additional processing and transportation capacity on Songo Songo to handle these additional gas volumes. Access has not yet been granted and it is not clear when, or if, this will occur.

Songas is not required to incur capital costs with respect to additional processing and transportation facilities unless the construction and operation of the facilities are, in the reasonable opinion of Songas, financially viable. If Songas is unable to finance such facilities, Songas shall permit the seller of the gas to construct the facilities at its expense, provided that, the facilities are designed, engineered and constructed in accordance with good pipeline and oilfield practices.

Revenue sharing terms and taxation

(g) 75% of the gross revenues less processing and pipeline tariffs and direct sales taxes in any year ("Net Revenues") can be used to recover past costs incurred. Costs recovered out of Net Revenues are termed "Cost Gas".

The Company pays and recovers costs of exploring, developing and operating the Additional Gas with two exceptions: (i) TPDC may recover reasonable market and market research costs as defined under the PSA (US$1.1 million as at 31 December 2012 for marketing costs that have been incurred by TPDC since start up); and (ii) TPDC has the right to elect to participate in the drilling of at least one well for Additional Gas in the Discovery Blocks for which there is a development program as detailed in an Additional Gas plan ("Additional Gas Plan") as submitted to the Ministry of Energy and Minerals subject to TPDC being able to elect to participate in a development program only once and TPDC having to pay a proportion of the costs of such development program by committing to pay between 5% and 20% of the total costs ("Specified Proportion"). If TPDC does not notify the Company within 90 days of notice from the Company that the MEM has approved the Additional Gas Plan, then TPDC is deemed not to have elected. If TPDC elects to participate, then it will be entitled to a rateable proportion of the Cost Gas and their profit share percentage increases by the Specified Proportion for that development program.

TPDC has indicated that they wish to exercise their right to 'back in' to the field development. The implications and workings of the 'back in' have been discussed with the Government Negotiation Team ("GNT") and there may be the need for reserve and accounting modifications once these discussions are concluded. For the purpose of the reserves certification as at 31 December 2012, it has been assumed that they will 'back in' for 20% for all future new wells and other developments and this is reflected in the Company's net reserve position.

(h) On 27 February 2009, the energy regulator, Energy and Water Utility Regulatory Authority ("EWURA"), issued an order that saw the introduction of a flat rate tariff of US$0.59/mcf from 1 January 2010. The Company's long-term gas price to the power sector as set out in the initialed Amended and Restated Gas Agreement ("ARGA") and the Portfolio Gas Sales Agreement ("PGSA") is based on the price of gas at the wellhead. As a consequence, the Company is not impacted by the changes to the tariff paid to Songas or other operators in respect of sales to the power sector.

During Q2 2011, the Company signed a Re-rating Agreement with TANESCO and Songas to run the gas processing plant at levels of up to 110 MMcfd (the pipeline and pressure requirements at the Ubungo power plant restrict the infrastructure capacity to a maximum of 102 MMcfd). Under the terms of the Re-rating Agreement, the Company effectively pays an additional tariff of US$0.30/mcf for sales between 70 MMcfd and 90 MMcfd and US$0.40/mcf for volumes above 90 MMcfd in addition to the tariff of US$0.59/mcf payable to Songas as set by the energy regulator, EWURA.

The Re-rating Agreement expired 31 December 2012; the terms of an extension are currently under discussion with Songas, TANESCO and TPDC. The Company has been advised by MEM that Songas has agreed to continue the Re-Rating Agreement until September 2013.

(i) The cost of maintaining the wells and flowlines is split between the Protected Gas and Additional Gas users in proportion to the volume of their respective sales. The cost of operating the gas processing plant and the pipeline to Dar es Salaam is covered through the payment of the pipeline tariff.

(j) Profits on sales from the Proven Section ("Profit Gas") are shared between TPDC and the Company, the proportion of which is dependent on the average daily volumes of Additional Gas sold or cumulative production.

The Company receives a higher share of the net revenues after cost recovery, based on the higher the cumulative production or the average daily sales. The Profit Gas share is a minimum of 25% and a maximum of 55%.

Average daily sales of Additional Gas	Cumulative sales of Additional Gas	TPDC's share of Profit Gas	Company's share of Profit Gas
MMcfd	*Bcf*	*%*	*%*
0 - 20	0 – 125	75	25
> 20 <= 30	> 125 <= 250	70	30
> 30 <= 40	> 250 <= 375	65	35
> 40 <= 50	> 375 <= 500	60	40
> 50	> 500	45	55

For Additional Gas produced outside of the Proven Section, the Company's Profit Gas share is 55%.

Where TPDC elects to participate in a development program, their profit share percentage increases by the Specified Proportion (for that development program) with a corresponding decrease in the Company's percentage share of Profit Gas.

The Company is liable to income tax. Where income tax is payable, there is a corresponding deduction in the amount of the Profit Gas payable to TPDC.

(k) Additional Profits Tax ("APT") is payable where the Company has recovered its costs plus a specified return out of Cost Gas revenues and Profit Gas revenues. As a result: (i) no APT is payable until the Company recovers its costs out of Additional Gas revenues plus an annual return of 25% plus the percentage change in the United States Industrial Goods Producer Price Index ("PPI"); and (ii) the maximum APT rate is 55% of the Company's Profit Gas when costs have been recovered with an annual return of 35% plus PPI return. The PSA is, therefore, structured to encourage the Company to develop the market and the gas fields in the knowledge that the profit share can increase with larger daily gas sales and that the costs will be recovered with a 25% plus PPI annual return before APT becomes payable. APT can have a significant negative impact on the project economics if only limited capital expenditure is incurred.

Operatorship

(l) The Company is appointed to develop, produce and process Protected Gas and operate and maintain the Songas gas production facilities and processing plant, including the staffing, procurement, capital improvements, contract maintenance, maintain books and records, prepare reports, maintain permits, handle waste, liaise with the Government of Tanzania and take all necessary safe, health and environmental precautions all in accordance with good oilfield practices. In return, the Company is paid or reimbursed by Songas so that the Company neither benefits nor suffers a loss as a result of its performance.

(m) In the event of loss arising from Songas' failure to perform and the loss is not fully compensated by Songas, Orca Exploration, or insurance coverage, then Orca Exploration is liable to a performance and operation guarantee of US$2.5 million when (i) the loss is caused by the gross negligence or wilful misconduct of the Company, its subsidiaries or employees, and (ii) Songas has insufficient funds to cure the loss and operate the project.

Consolidation

The companies that are being consolidated are:

Company	Incorporated
Orca Exploration Group Inc.	British Virgin Islands
Orca Exploration Italy Inc.	British Virgin Islands
Orca Exploration Italy Onshore Inc.	British Virgin Islands
PAE PanAfrican Energy Corporation	Mauritius
PanAfrican Energy Tanzania Limited	Jersey
Orca Exploration UK Services Limited	United Kingdom

RESULTS FOR THE YEAR ENDED 31ST DECEMBER 2012

OPERATING VOLUMES

The sales volumes for the year were 20,645 MMcf or 56.4 MMcfd. This represents an overall increase of 18% over the previous year. The Company's sales volumes were split between the industrial and power sectors as follows:

OPERATING VOLUMES	2012	2011
Gross sales volume *(MMcf)*		
Industrial sector	**3,813**	2,742
Power sector	**16,832**	14,722
Total volumes	**20,645**	17,464
Gross daily sales volume *(MMcfd)*		
Industrial sector	**10.4**	7.5
Power sector	**46.0**	40.3
Total daily sales volume	**56.4**	47.8

Industrial sector

Industrial sales volume increased by 39% to 3,813 MMcf from 2,742 MMcf in 2011. The overall increase is predominately a consequence of increased sales to Kioo Glass as a result of the full year supply of Additional Gas for that company's own power generation which commenced in September 2011. Sales of Additional Gas to the Wazo Hill cement plant operated by the Tanzanian Portland Cement Company ("TPCC") nearly doubled as a consequence of bringing Kiln 4 back into operation late in 2011. Industrial sales for the year averaged 10.4 MMcfd (2011: 7.5 MMcfd).

Power sector

Power sector sales volumes increased by 14% to 16,832 MMcf or 46.0 MMcfd, compared to 14,722 MMcf or 40.3 MMcfd in 2011. The increase is a result of continued decline in the use of hydro-generation due to the low levels of rainfall experienced during 2011/12 and a general increase in electricity demand. In order to meet the increased demand the Symbion power plant was re-commissioned in July 2011 and was in operation throughout 2012.

Capacity constraints

The increase in volume in 2012 is a result of the plant re-rating which occurred in June 2011, pursuant to which the capacity of the Songas plant was increased to 102 MMcfd. The re-rating agreement which was signed between the Company, Songas and TPDC, expired on 31 December 2012. The parties to the agreement have since cooperated in good faith to maintain the plant at the re-rated capacity. At such a time as the terms of the re-rating agreement cease, plant capacity will be restored to the original 70 MMcfd, which will result in a material reduction in the Company's sales volumes of Additional Gas.

SONGO SONGO DELIVERABILITY

As at 31 December 2012, the Company had a production capacity of approximately 113 MMcfd, restricted to 102 MMcfd by the available infrastructure.

The new production well SS-11 was successfully brought on stream on 3rd October 2012 and is currently producing approximately 38 MMcfd. As planned SS-9, which was producing approximately 30 MMcfd, has been suspended. The Company has also permanently suspended SS-3 as a result of production tubing integrity issues and rising casing annulus pressures. The condition of SS-4 is being monitored and it may have to be suspended in the future.

The Company plans to make up the production shortfall with additional volumes from SS-10 and SS-11. As a result no material change in field production levels of approximately 98 MMcfd is currently anticipated. There will, however, be no redundant capacity in the facility or pipeline until additional wells can be drilled in the field and facilities expanded. A loss or material reduction in the production of any given well will have a material adverse effect on the total production and funds flow from operations of the Company.

Production equipment originally installed in the SS-9, SS-5, SS-4 and SS-3 wells drilled by TPDC between 1976 and 1983 has reached the end of its useful life. To expand field productive capacity, upon successful settlement of the outstanding TANESCO receivable situation, the Company plans to rework and recomplete these wells by the end of 2014. The SS-10 well was drilled by the Company in 2007 and SS-11 was drilled in 2012. Plans for an additional development well, SS-12, as well as the reworking and recompletion of existing wells, have been placed on hold until the re-negotiation of certain terms of the Songo Songo PSA and related issues arising from the GNT discussions have been fully resolved as well as the significant outstanding TANESCO receivable having been collected, substantive progress on the Tanzania Natural Gas Infrastructure Project and financing.

COMMODITY PRICES

The commodity prices achieved in the different sectors during the quarter are shown in the table below:

US$/mcf	**2012**	2011
Average sales price		
Industrial sector	**9.30**	10.05
Power sector	**3.18**	2.77
Weighted average price	**4.31**	3.92

Industrial sector

The average gas price for the year was US$9.30/mcf (2011: US$10.05/mcf). In the context of essentially flat energy prices over 2011, the overall decrease in price achieved during the year is a consequence of a relative increase in the level of Additional Gas sales to Wazo Hill to 1.5 Bcf (2011: 0.75 Bcf). The sales to the Wazo Hill cement plant are priced by reference to imported coal (the company's alternative fuel supply) and accordingly are priced relatively lower than the rest of the Company's industrial customers.

Power sector

The average sales price to the power sector was US$3.18/mcf for the year, compared to US$2.77/mcf in 2011. The 15% increase is the result of a step change in the wellhead price, a component of the price to the power sector, from US$2.06/MMbtu to US$2.76/MMbtu with effect from 1st July 2012 as provisioned in the PGSA and ARGA. The ARGA and PGSA provide for indexation at the lower of US CPI and 2% with effect from each 1st July.

OPERATING REVENUE

Under the terms of the Songo Songo PSA, Orca Exploration is responsible for invoicing, collecting and allocating the revenue from Additional Gas sales.

Orca Exploration is able to recover all costs incurred on the exploration development and operations of the project out of 75% of the Net Revenues ("Cost Gas"). Any costs not recovered in any period are carried forward for recovery out of future revenues. Once the cost pool has been recovered TPDC will again be able to recover its past marketing costs, being an estimated US$1.1 million accrued to date in accordance with the terms of the PSA. TPDC marketing costs are treated as a reduction to Orca Exploration's Cost Gas entitlement.

The Additional Gas sales volumes throughout the year were in excess of 50 MMcfd entitling the Company to a 55% share of "Profit Gas" (Revenue less cost recovery share of revenue). The corresponding shares for 2011 were Q1 35%, Q2 40% and 55% for both Q3 and Q4.

From January 2011, a significant proportion of the gas production was from the SS-10 well, which has been deemed "backed into" by TPDC. As a result TPDC's profit share increased by 20% for the production attributable to SS-10. The same approach has been taken with respect to SS-11. The implications and workings of the 'back in' have been discussed with the GNT, but further discussion is required to finalise the arrangement by way of an amendment to the PSA.

Orca Exploration was allocated a total of 87.0% in 2012 (2011: 73.7%) of the Net Revenues as follows:

US$'000	**2012**	2011
Gross sales revenue	**89,053**	68,394
Gross tariff for processing plant and pipeline infrastructure	**(15,290)**	(11,672)
Gross revenue after tariff ("Net Revenues")	**73,763**	56,722
Analysed as to:		
Company Cost Gas	**53,473**	29,215
Company Profit Gas	**10,719**	12,579
Company operating revenue	**64,192**	41,794
TPDC share of revenue	**9,571**	14,928
	73,763	56,722

The Company's total revenues for the year amounted to US$77,259 after adjusting the Company's operating revenue of US$64,192 by:

i) adding US$16,530 for income tax in the current year – the Company is liable for income tax in Tanzania, but the income tax is recoverable out of TPDC's Profit Gas when the tax is payable and to account for this, revenue is adjusted to reflect the current year income tax charge or loss; and

ii) subtracting US$3,463 for the deferred effect of Additional Profits Tax – this tax is considered a royalty and is netted against revenue.

Revenue presented on the Consolidated Statement of Comprehensive Income may be reconciled to the operating revenue as follows:

US$'000	**2012**	2011
Industrial sector	**35,463**	27,562
Power sector	**53,590**	40,832
Gross sales revenue	**89,053**	68,394
Processing and transportation tariff	**(15,290)**	(11,672)
TPDC share of revenue	**(9,571)**	(14,928)
Company operating revenue	**64,192**	41,794
Additional Profits Tax	**(3,463)**	(2,527)
Current income tax adjustment	**16,530**	6,626
Revenue	**77,259**	45,893

The 68% increase in revenue compared to 2011 is the result of several factors. An 18% increase in sales volumes and a 10% increase in weighted average gas prices have contributed to an overall increase together with a significant increase in Cost Gas, reducing TPDC's share of Profit Gas as a consequence of a high level of capital investment during the year.

PROCESSING AND TRANSPORTATION TARIFF

Since early 2011, the Company has paid a flat rate regulated gas processing and transportation tariff of US$0.59/mcf to Songas. Under the terms of the gas contracts with the power sector, the Company will pass on any increase or decrease in the EWURA approved charges to its customers. This protocol insulates Orca Exploration from any increases in the gas processing and pipeline infrastructure costs.

During Q2 2011, the Company signed a Re-rating Agreement with TANESCO and Songas to run the gas processing plant at levels of up to 110 MMcfd (the pipeline and pressure requirements at the Ubungo power plant restrict the infrastructure capacity to a maximum of 102 MMcfd). Under the terms of this agreement, the Company effectively pays an additional tariff of US$0.30/mcf for sales between 70 MMcfd and 90 MMcfd and US$0.40/mcf for volumes above 90 MMcfd in addition to the regulated tariff of US$0.59/mcf payable to Songas. The charge for the additional tariff was US$3.1 million for the year, a 121% increase over US$1.4 million paid in 2011.

PRODUCTION AND DISTRIBUTION EXPENSES

The well maintenance costs are allocated between Protected and Additional Gas based on the proportion of their respective sales during the year. The total costs for the maintenance for the year was US$1,008 (2011: US$1,453) of which US$594 (2011: US$806) was allocated for the Additional Gas. The 2012 well maintenance costs also includes US$360 relating to corrosion studies.

Other field and operating costs include an apportionment of the annual PSA licence costs, regulatory fees and some costs associated with the evaluation of the reserves and the cost of personnel that are not recoverable from Songas.

Distribution costs represent the direct cost of maintaining the ringmain distribution pipeline and pressure reduction station (security, insurance and personnel).

In the context of the GNT negotiations and the recently announced draft Natural Gas Policy, TPDC and MEM have indicated that they wish Orca Exploration to unbundle the downstream distribution business in Tanzania. The methodology for this is currently being discussed with the government and may lead to future modifications to the accounts.

These costs are summarized in the table below:

US$'000	**2012**	2011
Share of well maintenance	**954**	806
Other field and operating costs	**1,744**	2,829
	2,698	3,635
Ringmain distribution costs	**3,255**	2,453
Production and distribution expenses	**5,953**	6,088

OPERATING NETBACKS

The netback per mcf before general and administrative costs, overheads, tax and APT may be analysed as follows:

US$'000	**2012**	2011
Gas price – industrial	**9.30**	10.05
Gas price – power	**3.18**	2.77
Weighted average price for gas	**4.31**	3.92
Processing and transportation tariff	**(0.74)**	(0.67)
TPDC share of revenue	**(0.46)**	(0.85)
Net selling price	**3.11**	2.40
Well maintenance and other operating costs	**(0.13)**	(0.21)
Ringmain distribution pipeline	**(0.16)**	(0.14)
Operating netback	**2.82**	2.05

The operating netback increased by 38% from US$2.05/mcf to US$2.82/mcf in 2012, a result of higher volumes, higher weighted average gas prices and increased recoveries of Cost Gas from higher capital expenditures during the year.

The 10% increase in the weighted average selling price from US$3.92/mcf to US$4.31/mcf in 2012 is partly a consequence of a change in the sales mix resulting in lower average industrial prices, offset by a 39% increase in Industrial gas volumes, and partly the result of a 15% increase in the Power price as a consequence of contractual step change in wellhead price during the year.

TPDC's share of revenue in 2012 decreased as a result of capital investment which entitled the Company to claim 75% of Net Revenues as Cost Gas for most of the year, before allocating Profit Gas. This was not the case in 2011 when the cost pool had been fully recovered, which also allowed TPDC to recover US$1.4 million in past marketing costs.

The 38% reduction in the well maintenance and other operating costs on a per mcf basis is primarily the result of higher sales volumes during the year.

GENERAL AND ADMINISTRATIVE EXPENSES

The administrative expenses ("G&A") may be analysed as follows:

US$'000	**2012**	2011
Employee & related costs	**9,441**	8,949
Office costs	**3,903**	2,952
Marketing costs including legal fees	**1,283**	2,192
Reporting, regulatory and corporate	**3,362**	1,347
	17,989	15,440

The G&A includes the costs of running the natural gas distribution business in Tanzania which is recoverable as Cost Gas and is relatively fixed in nature. G&A averaged approximately US$1.50 million per month in 2012 compared to US$1.29 million in 2011. G&A per mcf decreased to US$0.87/mcf (2011: US$0.88/mcf) the result of increased sales volumes.

The main variances for the year are summarized below:

Employee & related costs

The 5.5% increase in employee and related costs over 2011 relate primarily to the payment of severance, as well as retention, contractual and performance bonuses and consulting fees arising from the change of substantially all senior management positions during the year.

Office costs

The increase is primarily due to the establishment of an Orca UK Services office.

Marketing costs and legal fees

The decrease in marketing and legal fees compared to 2011 is a consequence of finalizing the PGSA and the associated legal fees which was signed at the end of Q2 2011.

Reporting, regulatory and corporate costs

The increase of US$2.0 million is due to a tax penalty of US$0.3 million and an increase of US$1.6 million in directors fees during the year, which amount includes fees and bonuses paid to the Chairman & Chief Executive Officer and the Chief Financial Officer & Director.

Stock based compensation

The breakdown of the costs incurred in relation to stock based compensation is detailed in the table below:

US$'000	**2012**	2011
Stock options	**720**	1,171
Stock appreciation rights	**432**	(320)
	1,152	851

A total of 1,922,400 stock options were issued and outstanding at the end of 2012 compared to 3,057,400 at the end of 2011, a result of exercise, expiries and relinquishments over the year. A total of 400,000 stock options were issued during 2012 with an exercise price of CDN$3.18, a five-year term and immediate vesting at the date of grant. A total one off charge of US$0.7 million was recorded in relation to these options.

A total of 745,000 stock appreciation rights were outstanding at the end of 2012 compared to 1,005,000 at the end of 2011, the reduction a result of expiries and relinquishments over the year. In August 2012, 100,000 rights were issued with an exercise price of CDN$2.70, a five year term and vest in three equal instalments, the first third on the anniversary of the grant date. A further 330,000 were issued in December 2012 at a price of CDN$2.35 and vested immediately.

As stock appreciation rights are settled in cash, they are re-valued at each reporting date using the Black-Scholes option pricing model. As at 31 December 2012, the following assumptions were used for the valuation of stock options and stock appreciation rights: stock volatility between 53% and 71%, a risk free interest rate of 1.50% and a closing stock price of CDN$3.00. A total charge of US$0.4 million was recorded in the year, principally as a consequence of issuing 330,000 rights which vested immediately.

NET FINANCE COSTS

The movement in net financing costs is summarized in the table below:

US$'000	**2012**	2011
FINANCE INCOME		
Interest income	**23**	5
Foreign exchange gain	**93**	80
	116	85
FINANCE CHARGES		
Loan interest and related financing costs	**(315)**	(100)
Foreign exchange loss	**(412)**	(938)
	(727)	(1,038)
NET FINANCE COSTS	**(611)**	(953)

The increase in loan interest and related financing costs year over is a result of the Company drawing down $6.0 million of a bank facility in September 2012.

TAXATION

Income Tax

Under the terms of the PSA with TPDC and the Government of Tanzania, the Company is liable for income tax in Tanzania at the corporate tax rate of 30%. However, where income tax is payable, this is recovered from TPDC by deducting an amount from TPDC's profit share. This is reflected in the accounts by increasing the Company's revenue by the appropriate amount.

As at 31 December 2012, there were temporary differences between the carrying value of the assets and liabilities for financial reporting purposes and the amounts used for taxation purposes under the Income Tax Act 2004. Applying the 30% Tanzanian tax rate, the Company has recognised a deferred tax liability of US$20.4 million (2011: US$15.2 million) which represents an additional deferred future income tax charge of US$5.2 million for the year (2011: US$2.4 million). This tax has no impact on cash flow until it becomes a current income tax at which point the tax is paid to the Commissioner of Taxes and recovered from TPDC's share of Profit Gas.

Additional Profits Tax

Under the terms of the PSA, in the event that all costs have been recovered with an annual return of 25% plus the percentage change in the United States Industrial Goods Producer Price Index ("PPI"), an Additional Profits Tax ("APT") is payable.

The Company provides for APT by forecasting the total APT payable as a proportion of the forecast Profit Gas over the term of the PSA. The effective APT rate of 31.8% (2011: 20%) was then applied to Profit Gas of US$10.7 million in 2012 (2011: US$12.6 million). Accordingly, US$3.5 million (2011: US$2.5 million) has been netted off revenue for the year ended 31 December 2012.

Management does not anticipate that any APT will be payable in 2013, as the forecast revenues will not be sufficient to cover the un-recovered costs brought forward as inflated by 25% plus the PPI percentage change and the forecast expenditures for 2013. The actual APT that will be paid is dependent on the achieved value of the Additional Gas sales and the quantum and timing of the operating costs and capital expenditure program.

The APT can have a significant negative impact on the Songo Songo project economics as measured by the net present value of the cash flow streams. Higher revenue in the initial years leads to a rapid payback of the project costs and consequently accelerates the payment of the APT that can account for up to 55% of the Company's profit share. Therefore, the terms of the PSA rewards the Company for taking higher risks by incurring capital expenditure in advance of revenue generation.

DEPLETION AND DEPRECIATION

The Natural Gas Properties are depleted using the unit of production method based on the production for the period as a percentage of the total future production from the Songo Songo proven reserves. As at 31 December 2012 the proven reserves as evaluated by the independent reservoir engineers, McDaniel & Associates Consultants Ltd., were 429.1 Bcf, after TPDC 'back-in', on a life of licence basis. A depletion expense of US$8,968 (2011: US$8,092) on total annual production of 20.65 Bcf (2011: 17.5 Bcf) yields an average depletion charge of US$0.43/mcf for the year (2011: US$0.47/mcf). The reduction in per mcf depletion charge is primarily the result of an increase in sales volumes over 2011.

Non-Natural Gas Properties are depreciated as follows:

Leasehold improvements	Over remaining life of the lease
Computer equipment	3 years
Vehicles	3 years
Fixtures and fittings	3 years

CARRYING AMOUNT OF ASSETS

Capitalised costs are periodically assessed to determine whether it is likely that such costs will be recovered in the future. To the extent that these capitalised costs are unlikely to be recovered in the future, they are impaired and recorded in the statement of comprehensive income (loss). In Q3 the Company recognised impairment of the La Tosca exploration well and has expensed the total cost of US$8.3 million when it was determined that the well did not have commercially viable quantities of mineral resources. The residual cost represents equipment with a resale value which the Company intends to realise.

FUNDS GENERATED BY OPERATIONS

Funds from operations before working capital changes were US$45.9 million for the year ended 31 December 2012 (2011: US$22.7 million). Removing the contribution of capital cost recoveries for the year, funds from operations in 2012 would have been approximately US$25 million, or US$0.70 per share.

US$'000	**2012**	2011
Profit after taxation	**18,329**	7,986
Adjustments (i)	**27,620**	14,672
Funds flow from operating activities	**45,949**	22,658
Working capital adjustments (i)	**(15,381)**	(18,081)
Net cash flows from operating activities	**30,568**	4,577
Net cash flows used in investing activities	**(55,388)**	(14,584)
Net cash flows from/(used in) financing activities	**5,980**	(681)
Increase in cash and cash equivalents	**(18,840)**	(10,688)
Effect of change in foreign exchange	**207**	(151)
Net decrease in cash and cash equivalents	**(18,633)**	(10,839)

(i) See consolidated statement of cash flows

The 103% increase in funds from operations over 2011 is due primarily to the 54% increase in operating revenue.

The increase in operating revenue is not reflected in the overall cash and cash equivalents as a consequence of TANESCO's inability to pay its invoices together with the high level of capital expenditure incurred during the year.

The post-tax profit adjustment includes US$8.3 million relating to a non-cash adjustment associated with the impairment of the La Tosca well in Longastrino, Italy.

CAPITAL EXPENDITURES

Capital expenditures amounted to US$54.7 million during the year (2011: US$18.1 million). The capital expenditure may be analysed as follows:

US$'000	**2012**	2011
Geological and geophysical and well drilling	**53,059**	16,475
Pipelines and infrastructure	**785**	1,158
Power development	**182**	37
Other equipment	**669**	465
	54,695	18,135

Geological and geophysical and well drilling

During the year the Company drilled and tied in the SS-11 development well at a cost of US$37.6 million including demobilization costs. Prior to suspension of the 2012 drilling programme additional costs of US$4.4 million were incurred on materials required for the drilling of the SS-12 development well, and a further US$3.5 million was spent on materials and a site survey for the Songo Songo West offshore exploration well.

A further US$7.5 million was spent drilling the La Tosca exploration well on the Longastrino block in the Po Valley in northern Italy; the well was unsuccessful and the costs have been written off in the current year.

Pipelines and infrastructure

A total of US$0.38 million was incurred during the year on the installation of new customers and enhancing existing customer connections.

An additional US$0.4 million was incurred during the year on the continued expansion of compressed natural gas ("CNG") facilities at Mikocheni.

WORKING CAPITAL

Working capital as at 31 December 2012 was US$46.8 million (31 December 2011: US$56.0 million) and may be analysed as follows:

	2012	2011
Cash and cash equivalents	**16,047**	34,680
TANESCO receivable	**33,256**	24,226
Songas receivable	**14,283**	3,720
Other debtors	**25,956**	12,402
Trade and other receivables	**73,495**	40,348
Taxation receivable	**14,692**	5,880
Prepayments	**246**	302
	104,480	81,210
Trade and other payables	**45,496**	22,801
Bank loan	**5,842**	–
Taxation payable	**6,322**	2,403
Working capital(1)	**46,820**	56,006

Note (1) Working capital as at 31 December 2012 includes a TANESCO receivable of US$33.3 million (2011: US$24.2 million) and a net Songas receivable of US$5.9 million (2011: US$0.7 million).

Working capital as at 31 December 2012 was down 16% over 2011, primarily as a result of 2012 capital expenditure.

At 31 December 2012 the majority of the Company's cash was held in Tanzania. There are no restrictions in Tanzania for converting Tanzania Shillings into US dollars.

Trade and other receivables at 31 December 2012 comprise trade receivables US$60.3 million (2011: US$35.7 million) and other receivables US$13.2 million (2011: US$4.6 million). Of the trade receivables US$33.3 million (2011: US$24.2 million) relates to sales to TANESCO. The increase in other receivables, relates principally to an increase in the amount due from Songas for operation of the gas processing plant and associated projects. The tax related receivable represents an additional share of revenue based on the current tax charge. The tax charge for the year ended 31 December 2012 is US$11.9 million (2011: US$4.9 million), this sum grossed for income tax at 30%, is recovered from TPDC once the tax has been paid.

The Company obtains 59% of its operating revenue from Songas and TANESCO. Songas' financial security is heavily reliant on the payment of capacity and energy charges by TANESCO. TANESCO is dependent on the Government of Tanzania for some of its funding. Despite having a history of delayed payments, TANESCO has previously settled in full the outstanding balance subsequent to each quarter end. During the year, there has been no substantive progress on payment of arrears owed by TANESCO. During the year, TANESCO failed to remain current and accordingly the TANESCO receivable grew to US$33.3 million (including arrears of US$28.4 million) by 31 December 2012, an increase of 38% year over year. As at the date of this report the TANESCO receivable is US$49.3 million (including arrears of US$43.0 million). Subsequent to the end of the year, in April 2013, the Government of Tanzania raised approximately US$600 million in international credit markets as well as a received World Bank budget support package of US$100 million, the first of three tranches of World Bank funding. The Government of Tanzania has assured the Company that a portion of the proceeds of these financings will be used to repay all of the outstanding arrears of TANESCO. In the event that Company does not collect from TANESCO the outstanding receivables during the current year and TANESCO continues to be unable to pay the Company for subsequent 2013 gas deliveries, the Company will need additional funding for its ongoing operations. There are no guarantees that such additional funding will be available when needed, or will be available on suitable terms.

At the end of 2012, Songas owed the Company US$23.4 million, whilst the Company owed Songas US$17.5 million; there is no legal right to offset these amounts. The net Songas receivable was US$5.9 million (2011: US$0.7 million).

As at 31 December 2012, the Company has US$45.5 million of financial liabilities with regards to trade and other payables (2011: US$22.8 million) of which US$17.5 million was due to Songas (2011: US$5.8 million). The financial liabilities are payable as follows: US$38.5 million is due within one to three months, nil is due within three to six months, and US$7.1 million is due within six to twelve months. The Company has a current taxation liability of US$6.3 million payable within three months.

BANK LOAN

In September 2012, the Company closed a US$10 million 18-month bridge loan facility with a Tanzanian bank to finance the Company's working capital requirements in Tanzania. The facility is secured by an assignment of accounts receivable and a fixed and floating charge on the assets of the Company. As at 31 December the Company had drawn down US$6.0 million under the facility and paid US$0.2 million in financing fees. Subsequent to year-end, in March 2013, the Company drew down the remaining US$4.0 million under the line. Principal amounts drawn under the facility are repayable in 12 equal monthly instalments which commenced in March 2013. Interest is payable monthly at three-month US LIBOR plus 8%. An additional interest rate of 2% will be applied for any period in which the TANESCO receivable is greater than 240-days.

FUTURE OPERATIONS

These financial statements have been prepared on a going concern basis. The going concern basis of presentation assumes that the Company will continue in operation for the foreseeable future and be able to realize its assets and discharge its liabilities and commitments in the normal course of business.

The ability of the Company to continue as a going concern is dependent on the Company's ability to collect its receivables from government entities to fund ongoing operations and the exploration and development program. The continued deterioration of the financial position of the state utility, TANESCO, has created uncertainty whether the Company will be able to collect sufficient cash to continue operations and meet its commitments. The immediate need to collect from its debtors may create significant doubt about the Company's ability to continue as a going concern.

The financial statements do not reflect adjustments that would be necessary if the going concern assumption were not appropriate. If the going concern basis were not appropriate for these financial statements, then adjustments would be necessary in the carrying amounts of assets and liabilities, the reported revenues and expenses, and the balance sheet classifications used.

The Company generates in excess of 59% of its operating revenue from sales to the power sector companies, Songas and TANESCO. Songas' financial security is heavily reliant on the payment of capacity and energy charges by TANESCO. TANESCO is dependent on the Government of Tanzania for some of its funding. Prior to 2012, despite having a history of delayed payments, TANESCO had settled in full the outstanding balance subsequent to each quarter end.

At 31 December 2012, TANESCO owed the Company US$33.3 million (including arrears of US$28.4 million) compared to US$24.2 million (including arrears of US$20.2 million) as at 31 December 2011. Subsequent to the end of the year, the Company has received US$1.0 million and, as of the date of this report, the arrears total US$43.0 million.

At the end of 2012, Songas owed the Company US$23.4 million, whilst the Company owed Songas US$17.5 million; there is no legal right to offset these amounts. Subsequent to the end of the year, the Company has neither received nor paid any amounts in settlement of these balances.

During 2012, there has been no substantive progress on payment of arrears owed by TANESCO and as well the state utility failed to remain current. Subsequent to the end of the year, in April 2013, the Government of Tanzania has informed the Company that it raised approximately US$600 million in international credit markets as well as having received a World Bank budget support package of US$100 million, the first of an expected three tranches of World Bank funding. The Government of Tanzania has assured the Company that a portion of the proceeds of these financings will be used to repay all of the outstanding arrears of TANESCO. In the event that Company does not collect from TANESCO the outstanding receivables at December 31, 2012 and TANESCO continues to be unable to pay the Company for subsequent 2013 gas deliveries, the Company will need additional funding for its ongoing operations within three to four months of the date of this report. There are no guarantees that such additional funding will be available when needed, or will be available on suitable terms.

During 2012, to help alleviate the funding gap caused by the delays in TANESCO payments the Company put in place a US$10 million facility with a bank in Tanzania. As at 31 December 2012, the Company had drawn down US$6.0 million of this facility, incurring financing charges of US$0.2 million. Subsequent to the end of the year, the Company drew the remaining US$4.0 million under the facility. Repayments commenced in March 2013.

SHAREHOLDERS' EQUITY AND OUTSTANDING SHARE DATA

There were 34.6 million shares outstanding as at 31st December 2012 which may be analysed as follows:

Number of shares ('000)	**2012**	2011
SHARES OUTSTANDING		
Class A shares	**1,751**	1,751
Class B shares	**32,892**	32,746
	34,643	34,497
CONVERTIBLE SECURITIES		
Options	**1,922**	3,057
Fully diluted Class A and Class B shares	**36,565**	37,554
WEIGHTED AVERAGE		
Class A and Class B shares	**34,642**	34,656
Convertible securities		
Stock options	**811**	1,176
Weighted average diluted Class A and Class B shares	**35,453**	35,832

The movement in Class B shares during the year is analysed in the table below:

Number of shares ('000)	**2012**	2011
As at 1 January	**32,746**	32,939
Stock options exercised	**150**	–
Normal course issuer bid	**(4)**	(193)
As at 31 December	**32,892**	32,746

As at 26 April 2013, there were a total of 32,892,015 Class B shares and 1,751,195 Class A shares outstanding.

STOCK OPTIONS

	2012		2011	
Thousands of options or CDN$	Options	Exercise Price	Options	Exercise Price
Outstanding as at 1 January	**3,057**	**1.00 to 13.55**	2,557	1.00 to 13.55
Forfeited/Expired	**(1,385)**	**4.75 to 13.55**	–	–
Exercised	**(150)**	**1.00**	–	–
Issued	**400**	**3.18**	500	3.60 to 4.75
Outstanding as at 31 December	**1,922**	**1.00 to 3.60**	3,057	1.00 to 13.55

The weighted average remaining life and weighted average exercise prices of options at 31 December 2012 were as follows:

Exercise Price *(CDN$)*	Number Outstanding as at 31 December 2012	Weighted Average Remaining Contractual Life *(years)*	Number Exercisable as at 31 December 2012	Weighted Average Exercise Price *(CDN$)*
1.00	1,272	1.66	1,272	1.00
3.18	400	4.29	400	3.18
3.60	250	3.75	250	3.60
	1,922		**1,922**	

There were 400,000 new stock options issued during the year with an exercise price of CDN$3.18. The stock option issued fully vested on 31 December 2012 and have a term of five years. A total charge of US$0.7 million has been recognised for the year in relation to the stock options and is included in General & Administrative expenses.

STOCK APPRECIATION RIGHTS

Thousands of stock appreciation rights or CDN$	**2012**		2011	
	SAR	**Exercise Price**	SAR	Exercise Price
Outstanding as at 1 January	**1,005**	**4.20 to 13.55**	1,005	4.20 to 13.55
Expired	**(690)**	**8.70 to 13.55**	–	–
Granted *(i)*	**430**	**2.35 to 2.70**	–	–
Outstanding as at 31 December *(ii)*	**745**	**2.35 to 5.30**	1,005	4.20 to 13.55

(i) A total of 100,000 stock appreciation rights were issued in August 2012 with an exercise price of CDN$2.70. These rights have a term of five years and vest in three equal instalments, the first third vesting on the anniversary of the grant date. A further 330,000 stock appreciation rights were issued in December 2012 at CDN$2.35 which vested immediately. There is no maximum liability associated with these rights.

The Company records a charge to the income statement using the Black-Scholes fair valuation option pricing model every reporting period with a resulting liability being recognised in trade and other payables. In the valuation of both the stock options and stock appreciation rights at the reporting date, the following assumptions have been made: a risk free rate of interest of 1.50%; stock volatility of 53% to 71%; a 0% dividend yield; 0% forfeiture; and a closing stock price of CDN$3.00 per share.

As at 31 December 2012, a total accrued liability of US$0.6 million (2011: US$0.2 million) has been recognised in relation to the stock appreciation rights. The liability increased by US$0.4 million during the year reflects the issue of additional stock appreciation rights, many of which vested immediately.

CONTRACTUAL OBLIGATIONS AND COMMITTED CAPITAL INVESTMENT

CONTRACTUAL OBLIGATIONS

Protected Gas

Under the terms of the original gas agreement for the Songo Songo project ("Gas Agreement"), in the event that there is a shortfall/insufficiency in Protected Gas as a consequence of the sale of Additional Gas, then the Company is liable to pay the difference between the price of Protected Gas (US$0.55/MMbtu) and the price of an alternative feedstock multiplied by the volumes of Protected Gas up to a maximum of the volume of Additional Gas sold (85.7 Bcf as at 31 December 2012). The Company did not have a shortfall during the reporting period does not anticipate a shortfall arising during the licence period.

The Gas Agreement may be superseded by an initialled ARGA. The ARGA provides clarification of the Protected Gas volumes and removes all terms dealing with the security of the Protected Gas and the consequences of any insufficiency to a new Insufficiency Agreement ("IA"). The IA specifies terms under which Songas may demand cash security in order to keep them whole in the event of a Protected Gas insufficiency. Once the new IA is signed, it will govern the basis for determining security. Under the provisional terms of the IA, when it is calculated that funding is required, the Company shall fund an escrow account at a rate of US$2/MMbtu on all industrial Additional Gas sales out of its and TPDC share of revenue, and TANESCO shall contribute the same amount on Additional Gas sales to the power sector. The funds provide security for Songas in the event of an insufficiency of Protected Gas. The Company is actively monitoring the reservoir and, supported by the report of its independent engineers, does not anticipate that a liability will occur in this respect.

Re-rating Agreement

During Q2 2011, the Company signed a re-rating agreement with TANESCO and Songas (the "Re-Rating Agreement") to increase the gas processing capacity to a maximum of 110 MMcfd (the pipeline and pressure requirements at the Ubungo power plant restrict the infrastructure capacity to a maximum of 102 MMcfd). Under the terms of the Re-rating Agreement, the Company effectively pays an additional tariff of US$0.30/mcf for sales between 70 MMcfd and 90 MMcfd and US$0.40/mcf for volumes above 90 MMcfd in addition to the tariff of US$0.59/mcf payable to Songas as set by the energy regulator, EWURA.

Under the terms of this agreement, the Company agreed to indemnify Songas for damage to its facilities caused by the re-rating, up to a maximum of US$15 million, but only to the extent that this was not already covered by indemnities from TANESCO or Songas' insurance policies. The Re-rating Agreement expired 31 December 2012 and the matter of increased capacity, whether by new or amended agreements, is currently under discussion with Songas and TANESCO. In the interim, the Company has been advised by MEM that Songas has agreed to continue the Re-Rating Agreeement until September 2013.

Portfolio Gas Sales Agreement

On 17 June 2011, a long term (to June 2023) PGSA was signed between Orca Exploration and TANESCO. Under the PGSA, Orca is obligated, subject to infrastructure capacity, to sell a maximum of approximately 37 MMcfd for use in any of TANESCO's current power plants except those operated by Songas at Ubungo. Under the agreement, the current basic wellhead gas price of US$2.82/mcf is due to increase to approximately US$2.88/mcf on 1 July 2013.

Operating leases

The Company has two office rental agreements. One in Dar es Salaam which expires on 30 November 2013 at an annual rental of US$238 and one in Winchester (UK) which expires on 25 September 2022 at an annual rental of GBP35 (US$58) per annum for the first two years and GBP71 (US$115) thereafter. Both are recognised in the General and Administrative expenses.

CAPITAL COMMITMENTS

Italy

On 31 May 2010, the Company signed an agreement with Petroceltic International plc ("Petroceltic") to farm in on Petroceltic's Central Adriatic B.R268.RG Permit offshore Italy. The farm-in commits the Company to fund 30% of the Elsa-2 appraisal well up to a maximum of US$11.5 million to earn a 15% working interest in the permit. Thereafter, the Company will fund all future costs relating to the well and the permit in proportion to its participating interest. The Company has also agreed to pay Petroceltic fifteen per cent (15%) of the back costs in relation to the well up to a maximum of US$0.5 million.

Petroceltic was due to spud the Elsa-2 well prior to 31 October 2010, but the Italian government passed a decree, following the blowout of the Macondo well in the U.S., that prevented the drilling in the Italian seas within five nautical miles of the coastline and within 12 nautical miles around the perimeter of protected Marine Parks. In view of this, Petroceltic suspended the permit until such time as the Ministry of Environment issued a decree of environmental compatibility for the drilling program. Legislative Decree 83/2012 (the "Decree"), was published on 26 June 2012 and was approved by both houses of the Italian Parliament with no substantial modifications. On 12th August, the Decree became law following publication in the Italian Official Journal. The new law modifies restrictions on offshore oil and gas exploration and production originally introduced by DLGS 128/2010 in August 2010. The well is now expected to be drilled following finalisation of an environmental impact study currently expected in 2014. Orca will not be liable to any costs associated with the drilling of Elsa-2 until a rig contract is signed.

There are no further capital commitments in Italy.

Songo Songo

There are no contractual commitments for capital expenditure at Songo Songo. Any significant additional capital expenditure in Tanzania remains dependent on TANESCO payments being brought up to date, the satisfactory conclusion of the GNT issues, material progress on infrastructure expansion, the conclusion of commercial terms and the subsequent raising of finance. Significant additional capital expenditure will be required to enable the Songo Songo field to produce 190 MMcfd in line with the anticipated infrastructure expansion.

CONTINGENCIES

Downstream unbundling

In connection with the GNT negotiations and the recently announced draft Natural Gas Policy, TPDC and MEM have indicated that they wish Orca Exploration to unbundle the downstream distribution business in Tanzania. The methodology for this has been discussed with the GNT along with other issues. The Company anticipates further negotiations will be necessary before this matter is concluded.

Access to infrastructure

Ndovu Resources Limited, with support from TPDC and MEM, has indicated that they wish to tie into the gas processing plant on Songo Songo Island and sell up to 10 MMcfd from their Kiliwani North field. The Tanzania Natural Gas Infrastructure Project contemplates additional processing and transportation capacity on Songo Songo to handle these additional gas volumes. Access has not yet been granted and it is not clear when, or if, this will occur.

TPDC Back in

TPDC has indicated that they wish to exercise its right under the PSA to 'back in' to the Songo Songo field development. The implications and workings of the 'back in' have been discussed with the GNT along with other issues. The issues are not yet fully resolved, however, there may be the need for additional reserve and accounting modifications once these discussions are concluded. For the purpose of the reserves certification as at 31 December 2012, it was assumed that they will 'back in' for 20% for all future new drilling activities and other developments and this is reflected in the Company's net reserve position.

Cost recovery

The Company's cost pool in Tanzania was recovered early in Q2 2011 resulting in a reduction in the percentage of net revenue attributable to the Company. During the current year the level of Cost Gas increased significantly as a consequence of drilling the SS-11 well, however, the cost pool was recovered in Q4 2012.

TPDC conducted an audit of the historic cost pool and in 2011 disputed approximately US$34 million of costs that had been allocated to the cost pool from 2002 through to 2009. The Company contends that the disputed costs were appropriately incurred on the Songo Songo project in accordance with the terms of the PSA. This matter was not resolved during the year in conjunction with the GNT negotiations and while the Company remains confident that the final outcome will be satisfactory, it is prepared to utilise the extensive dispute resolution mechanisms outlined in the PSA if necessary. This matter has had no impact on the results for the year.

Taxation

During the year, the Company received an assessment for additional withholding tax from the Tanzanian Revenue Authority (TRA), which together with interest and penalties totals approximately US$2.0 million. The Company considered the assessment to be without merit and appealed to the Tax Revenue Appeals Board. The Tax Revenue Appeals Board considered the appeal in March 2013 and upheld the assessment. The Company will now pursue the case with the Tax Revenue Appeals Tribunal and if necessary the Court of Appeal of Tanzania.

RELATED PARTY TRANSACTIONS

One of the non-executive Directors is a partner at a law firm. During the year, the Company incurred US$0.4 million (2011: US$0.2 million) to this firm for services provided. The transactions with this related party were made at the exchange amount. As at 31 December 2012 the Company has a total of US$0.2 million recorded in trade and other payables in relation to the related party. Each of the Chief Executive Officer and the Chief Financial Officer provide services to the Company through consulting agreements with personal services companies. During the year, the Company incurred fees and bonus compensation of US$0.1 million and US$0.2 million to the Chief Executive Officer and the Chief Financial Officer respectively (2011: US$0.2 million and US$ nil respectively).

SUMMARY QUARTERLY RESULTS

The following is a summary of the results for the Company for the last eight quarters:

(US$'000 except where otherwise stated)	**2012**				2011			
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
FINANCIAL								
Revenue	**20,712**	22,425	16,915	17,207	17,500	10,457	8,296	9,640
Profit/(loss) after taxation	**5,504**	1,266	5,167	6,392	5,267	(54)	383	2,390
Operating netback *(US$/mcf)*	**3.01**	3.14	2.56	2.55	2.41	1.78	1.80	2.16
Working capital	**46,820**	37,730	38,689	47,063	56,006	58,369	57,070	55,759
Shareholders' equity	**125,935**	120,204	118,938	113,051	106,659	101,563	100,956	100,573
Profit/(loss) per share – basic *(US$)*	**0.15**	0.04	0.15	0.19	0.15	0.00	0.01	0.07
Profit/(loss) per share – diluted *(US$)*	**0.15**	0.04	0.15	0.18	0.15	0.00	0.01	0.07
CAPITAL EXPENDITURES								
Geological and geophysical and well drilling	**2,160**	14,749	17,732	18,418	10,989	3,463	1,124	899
Pipeline and infrastructure	**(258)**	261	563	219	11	421	364	362
Power development	**(15)**	22	84	91	22	–	11	4
Other equipment	**562**	1	86	20	239	41	94	91
OPERATING								
Additional Gas sold – industrial *(MMcf)*	**1,127**	1,022	829	835	786	719	688	550
Additional Gas sold – power *(MMcf)*	**4,417**	4,270	4,172	3,973	4,521	4,442	2,965	2,794
Average price per mcf – industrial *(US$)*	**8.56**	9.21	10.14	9.63	9.94	10.47	10.28	9.42
Average price per mcf – power *(US$)*	**3.61**	3.55	2.80	2.72	2.97	2.76	2.64	2.62

The principal developments in Q4 2012 were as follows:

- Sales volume for the quarter of 5,544 MMcf (Q4 2011: 5,307 MMcf) or 60.3 MMcfd (Q4 2011: 57.6 MMcf) which represents the best quarter since sales began in 2004. Gross sales revenue amounted to US$24.7 million.
- The new production well SS-11 was brought onstream at the beginning of the quarter and is currently producing approximately 38 MMcfd of natural gas.
- The SS-9 well was taken off production and suspended, permanently. The well, which was producing approximately 30 MMcfd, has been permanently suspended due to a tubing leak resulting in rising casing annulus pressures. SS-3 was subsequently suspended on the basis of tubing integrity issues.
- On 1st November 2012, the Government of Tanzania issued a draft natural gas policy for review and consultation among the various stakeholders. At the request of MEM, the Company has submitted its comments in writing.

SELECTED FINANCIAL INFORMATION

Selected annual financial information derived from the audited consolidated financial statements for the years ended 31 December 2010, 2011 and 2012 is set out below:

US$'000s except per share amounts	2012	2011	2010
Revenue	**77,259**	45,893	38,808
Funds flow from operating activities	**45,949**	22,658	20,836
Net cash flows from operating activities	**30,568**	4,577	15,534
Profit after taxation	**18,329**	7,986	10,011
Total assets	**212,244**	151,844	124,408
Profit per share:			
Basic *(US$)*	**0.53**	0.23	0.33
Diluted *(US$)*	**0.52**	0.22	0.31

Revenue increased by 68% to US$77.3 million in 2012 from US$45.9 million in 2011. The sales volumes were 18% higher in 2012 than 2011, with the weighted average price increasing from US$3.92/mcf to US$4.31/mcf. In 2012, current taxation of US$11.6 million was payable (2011: US$4.6 million) which in accordance with the terms of the PSA is recoverable from TPDC. Consequently revenue in 2012 has been uplifted by the gross amount of US$16.5 million (2011: US$6.6 million)

The level of industrial volumes increased by39% to 3,813 MMcf in 2012 from 2,742 MMcf in 2011, mainly as a consequence of the increase in sales to Kioo Limited and Wazo Hill. The level of power volumes increased by 14% to 16,832 MMcf (2011: 14,722 MMcf. The increase in power sales is attributable to more reliance on natural gas to generate electricity, increased generation and infrastructure capacity.

Revenue increased by 18% to US$45.9 million in 2011 from US$38.8 million in 2010. The increase was a result of an increase in production volumes of 30% together with a 5% increase in the weighted average realized price from US$3.74/mcf in 2010 to US$3.92/mcf in 2011.

Funds from operations before working capital changes increased by 103% from US$22.7 million in 2011 to US$45.9 million in 2012 as a consequence of increased sales revenue. The funds from operations before working capital changes increased by 8% from US$20.8 million in 2010 to US$22.7 million in 2011 as a consequence of increased sales revenue, the impact of which was reduced by an increase in the level of general and administrative expenses.

BUSINESS RISKS

Operating Hazards and Uninsured Risks

The business of Orca Exploration is subject to all of the operating risks normally associated with the exploration for, and the production, storage, transportation and marketing of oil and gas. These risks include blowouts, explosions, fire, gaseous leaks, downhole design and integrity, migration of harmful substances and oil spills, any of which could cause personal injury, result in damage to, or destruction of, oil and gas wells or formations or production facilities and other property, equipment and the environment, as well as interrupt operations. In addition, all of Orca Exploration's operations will be subject to the risks normally incident to drilling of natural gas wells and the operation and development of gas properties, including encountering unexpected formations or pressures, premature declines of reservoirs, blowouts, equipment and tubing failures and other accidents, sour gas releases, uncontrollable flows of oil, natural gas or well fluids, adverse weather conditions, pollution and other environmental risks. Drilling conducted by Orca Exploration overseas will involve increased drilling risks of high pressures and mechanical difficulties, including stuck pipe, collapsed casing and separated cable. The impact that any of these risks may have upon Orca Exploration is increased due to the fact that Orca Exploration currently only has one producing property. Orca Exploration will maintain insurance against some, but not all, potential risks; however, there can be no assurance that such insurance will be adequate to cover any losses or exposure for liability. The occurrence of a significant unfavourable event not fully covered by insurance could have a material adverse effect on Orca Exploration's financial condition, results of operations and cash flows. Furthermore, Orca Exploration cannot predict whether insurance will continue to be available at a reasonable cost or at all.

Foreign Operations

Orca Exploration's operations and related assets are located in Italy and Tanzania which may be considered to be politically and/or economically unstable. Exploration or development activities in Tanzania and Italy may require protracted negotiations with host governments, national oil companies and third parties and are frequently subject to economic and political considerations, such as, the risks of war, actions by terrorist or insurgent groups, expropriation, nationalization, renegotiation or nullification of existing contracts and production sharing agreements, taxation policies, foreign exchange restrictions, changing political conditions, international monetary fluctuations, currency controls and foreign governmental regulations that favour or require the awarding of drilling contracts to local contractors or require foreign contractors to employ citizens of, or purchase supplies from, a particular jurisdiction. In addition, if a dispute arises with foreign operations, Orca Exploration may be subject to the exclusive jurisdiction of foreign courts.

In Tanzania the, the state retains ownership of the minerals and consequently retains control of, the exploration and production of hydrocarbon reserves. Accordingly, these operations may be materially affected by the government through royalty payments, export taxes and regulations, surcharges, value added taxes, production bonuses and other charges. The Government of Tanzania tabled a draft Natural Gas Policy in 2012, which policy contemplates greater government control over the industry and in some areas conflicts with the Company's rights under the Songo Songo PSA. There can be no assurance that the rights of the Company under the PSA will be grandfathered with respect to any future natural gas legislation arising from this policy.

Orca's development properties and its current proved natural gas reserves located offshore on the Songo Songo Island in Tanzania, are subject to regulation and control by the government of Tanzania and certain of its national and parastatal organizations including the energy regulator, EWURA and TPDC. Orca Exploration and its predecessors have operated in Tanzania for a number of years and believe that it has reasonably good relations with the current Tanzanian government. However, there can be no assurance that present or future administrations or governmental regulations in Tanzania will not materially adversely affect the operations or future cash flows of Orca Exploration.

The Tanzania Revenue Authority ("TRA") is responsible for the collection of taxes in Tanzania. The TRA is not party to the Songo Songo PSA and there is no assurance that the TRA will consider itself bound by its terms. Accordingly, there is a risk that the TRA will take interpretations of issues distinct from the PSA and result in assessments, penalties and fines which have not been contemplated by the Company and result in additional costs which are not recoverable under the PSA. The TRA has significant powers in Tanzania and is capable of causing the Company's operations in that country to cease.

The Company requires additional gas processing and transportation infrastructure to allow additional development and the ultimate monetisation of the Company's reserves through additional gas sales. In 2012, the Government of Tanzania announced a US$1.2 billion natural gas infrastructure expansion project, the scope of which would provide sufficient capacity to process and transport the necessary volumes of gas. There has to date been limited discussions of commercial terms for such facilities and there is no assurance that the Company's gas could be processed and transported to markets on economic terms.

PSA Negotiations

In February 2012 on the recommendation of MEM, the Government announced that it was establishing a negotiating team, the GNT, to discuss a number of issues raised in parliament in relation to the Company's Songo Songo PSA with TPDC. In Tanzania, government negotiating teams are a common mechanism to negotiate with business. The scope of the GNT was to discuss a number of points that were raised by the Parliamentary Committee for Energy into the workings of the PSA. This included, but is not limited to, TPDC back in rights, profit sharing arrangements, the unbundling of the downstream assets, cost recovery and Orca's management of the upstream operations. After making submissions to the GNT, the Company commenced discussions in April 2012 and further in July 2012. In July 2012, Parliament dissolved the Parliamentary Committee for Energy and Minerals on the grounds of alleged widespread corruption and abuse of power. A Parliamentary team formed to investigate the allegations subsequently cleared Members of Parliament of any wrong doing. In July 2012, an agreement in principle was been reached on a number of major points to resolve the issues. The GNT has completed its mandate and the responsibility for finalisation, documentation and implementation has moved back to MEM. The agreement in principal contemplated completion this process by the end of 2012. As at the date of this report, a number of conditions precedent have not been fulfilled and a number of issues remain to be fully resolved and documented, including an agreed form of amendment to the PSA. The outcome of these negotiations could have a significant impact on the operations of the Company, which cannot be estimated at this time.

Additional Financing

Depending on future exploration, development, and marketing plans, and the status of the TANESCO and Songas receivables situation, Orca Exploration may require additional financing. The ability of Orca Exploration to arrange such financing in the future will depend in part upon the prevailing capital market conditions as well as the business performance of Orca Exploration. There can be no assurance that Orca Exploration will be successful in its efforts to arrange additional financing on terms satisfactory to Orca Exploration. If additional financing is raised by the issuance of shares from treasury of Orca Exploration, control of the Company may change and shareholders may suffer additional dilution.

From time to time Orca Exploration may enter into transactions to acquire assets or the shares of other companies. These transactions may be financed partially or wholly with debt, which may temporarily increase Orca Exploration's debt levels above industry standards.

Industry Conditions

The oil and gas industry is intensely competitive and Orca Exploration competes with other companies which possess greater technical and financial resources. Many of these competitors not only explore for and produce oil and natural gas, but also carry on refining operations and market petroleum, natural gas products and other products on an international basis. Oil and gas production operations are also subject to all the risks typically associated with such operations, including premature decline of reservoirs and invasion of water into producing formations. Currently, Orca Exploration operates the Songo Songo natural gas property and has interests in two permits in Italy. There is a risk that in the future either the operatorship could change and the property operated by third parties or operations may be subject to control by national oil companies, Songas, or parastatal organisations and, as a result, Orca Exploration may have limited control over the nature and timing of exploration and development of such properties or the manner in which operations are conducted on such properties.

The marketability and price of natural gas which may be acquired, discovered or marketed by Orca Exploration will be affected by numerous factors beyond its control. There is currently no developed natural gas market in Tanzania and no infrastructure with which to serve potential new markets beyond that being constructed by Orca Exploration and Songas. The ability of Orca Exploration to market any natural gas from current or future reserves in Tanzania may depend upon its ability to develop natural gas markets in Tanzania and the surrounding region, obtain access to the necessary infrastructure to deliver sales gas volumes, including acquiring capacity on pipelines which deliver natural gas to commercial markets. Orca Exploration is also subject to market fluctuations in the prices of oil and natural gas, uncertainties related to the delivery and proximity of its reserves to pipelines and processing facilities and extensive government regulation relating to prices, taxes, royalties, land tenure, allowable production, the export of oil and gas and many other aspects of the oil and gas business. Orca Exploration is also subject to a variety of waste disposal, pollution control and similar environmental laws.

The oil and natural gas industry is subject to varying environmental regulations in each of the jurisdictions in which Orca Exploration may operate. Environmental regulations place restrictions and prohibitions on emissions of various substances produced concurrently and oil and natural gas and can impact on the selection of drilling sites and facility locations, potentially resulting in increased capital expenditures.

Additional Gas

Orca Exploration has the right, under the terms of the PSA, to market volumes of Additional Gas subject to satisfying the requirements to deliver Protected Gas to Songas.

There is a risk that Songas could interfere in Orca Exploration's ability to produce, transport and sell volumes of Additional Gas if Orca Exploration's obligations to Songas under the Gas Agreement are not met. In particular, Songas has the right to request reasonable security on all Additional Gas sales.

The Government of Tanzania has released a draft Natural Gas Policy in November 2012, which policy contemplates TPDC becoming sole aggregator of natural gas in the country. This policy objective conflicts with the Company's prior right under the PSA to directly market Additional Gas, and there is a risk that this prior right will not be recognized and that the Company's ability to maximise revenue on Additional Gas sales may be impaired by a requirement to sell gas to TPDC as aggregator.

Replacement of Reserves

Orca Exploration's natural gas reserves and production and, therefore, its cash flows and earnings are highly dependent upon the Company developing and increasing its current reserve base and discovering or acquiring additional reserves. Without the addition of reserves through exploration, acquisition or development activities, Orca Exploration's reserves and production will decline over time as reserves are depleted. To the extent that cash flow from operations is insufficient and external sources of capital become limited or unavailable, the Company's ability to make the necessary capital investments to maintain and expand its oil and natural gas reserves will be impaired. There can be no assurance that Orca Exploration will be able to find and develop or acquire additional reserves to replace production at commercially feasible costs.

Asset Concentration

Orca Exploration's natural gas reserves are currently limited to one producing property, the Songo Songo field, and the production potential from this field is limited to four wells. There has been limited production from the Songo Songo field to date. There is no assurance that Orca Exploration will have sufficient deliverability through the existing wells to provide additional natural gas sales volumes, and that there may be significant capital expenditures associated with any remedial work, workovers, or new drilling required to achieve deliverability. In addition, any difficulties relating to the operation or performance of the field would have a material adverse effect on Orca Exploration. The Company is currently producing the existing wells at maximum capacity. **There will, however, be no redundant capacity in the facility or pipeline until additional wells can be drilled in the field and facilities expanded. A loss or material reduction in the production of any given well will have a material adverse effect on the total production and funds flow from operations of the Company.** The Italian licences in which Orca has an interest are currently in the exploration phase of their cycle and it may be several years before Orca is able to obtain a revenue stream from these assets.

Environmental and Other Regulations

Extensive national, state, and local environmental laws and regulations in foreign jurisdictions will affect nearly all of Orca Exploration's operations. These laws and regulations set various standards regulating certain aspects of health and environmental quality, provide for penalties and other liabilities for the violation of such standards and establish in certain circumstances obligations to remediate current and former facilities and locations where operations are or were conducted. In addition, special provisions may be appropriate or required in environmentally sensitive areas of operation. There can be no assurance that Orca Exploration will not incur substantial financial obligations in connection with environmental compliance. Significant liability could be imposed on Orca Exploration for damages, cleanup costs or penalties in the event of certain discharges into the environment, environmental damage caused by previous owners of property purchased by Orca Exploration or non-compliance with environmental laws or regulations. Such liability could have a material adverse effect on Orca Exploration. Moreover, Orca Exploration cannot predict what environmental legislation or regulations will be enacted in the future or how existing or future laws or regulations will be administered or enforced. Compliance with more stringent laws or regulations, or more vigorous enforcement policies of any regulatory authority, could in the future require material expenditures by Orca Exploration for the installation and operation of systems and equipment for remedial measures, any or all of which may have a material adverse effect on Orca Exploration. As party to various licenses, Orca Exploration has an obligation to restore producing fields to a condition acceptable to the authorities at the end of their commercial lives.

While management believes that Orca Exploration is currently in compliance with environmental laws and regulations applicable to Orca Exploration's operations in Tanzania and Italy, no assurances can be given that Orca Exploration will be able to continue to comply with such environmental laws and regulations without incurring substantial costs.

Orca Exploration's petroleum and natural gas operations are subject to extensive governmental legislation and regulation and increased public awareness concerning environmental protection.

No provision has been recognised for future decommissioning costs in Tanzania which are anticipated to be minimal as it is forecast that there will still be commercial gas reserves once Orca Exploration relinquishes the license in 2026. Orca Exploration expects that the cost of complying with environmental legislation and regulations will increase in the future. Compliance with existing environmental legislation and regulations has not had a material effect on capital expenditures, earnings or competitive position of Orca Exploration to date. Although management believes that Orca Exploration's operations and facilities are in material compliance with such laws and regulations, future changes in these laws, regulations or interpretations thereof or the nature of its operations may require the Company to make significant additional capital expenditures to ensure compliance in the future.

Volatility of Oil and Gas Prices and Markets

Orca Exploration's financial condition, operating results and future growth will be dependent on the prevailing prices for its natural gas production. Historically, the markets for oil and natural gas have been volatile and such markets are likely to continue to be volatile in the future. Prices for oil and natural gas are subject to large fluctuations in response to relatively minor changes to the demand for oil and natural gas, whether the result of uncertainty or a variety of additional factors beyond the control of Orca Exploration. Any substantial decline in the prices of oil and natural gas could have a material adverse effect on Orca Exploration and the level of its natural gas reserves. Additionally, the economics of producing from some wells may change as a result of lower prices, which could result in a suspension of production by Orca Exploration.

No assurance can be given that oil and natural gas prices will be sustained at levels which will enable Orca Exploration to operate profitably. From time to time Orca Exploration may avail itself of forward sales or other forms of hedging activities with a view to mitigating its exposure to the risk of price volatility. The terms of the industrial gas supply contracts were extended in 2008 for a period of five years. These contracts contain pricing caps and floors that limit the industrial downside price to US$7.38/mcf. The Company also entered into fixed price contracts with TANESCO and Songas for the supply of Additional Gas to the power sector. The steps taken by the Company in 2008 were important steps in mitigating the exposure to price volatility.

The Songo Songo field was the first gas field to be developed in East Africa and was followed by a commercial gas discovery in the south of Tanzania at Mnazi Bay. The Company is the only supplier of gas into the main demand centre of Dar es Salaam and has therefore been able to negotiate industrial gas sales contracts with gas prices that are at a discount to the lowest cost alternative fuels in Dar es Salaam, namely HFO and coal.

There has an increase in exploration activity in Tanzania, which has yielded significant discoveries of natural gas that could, when developed, lead to increased competition for gas markets and lower gas prices in the future.

In addition, various factors, including the availability and capacity of oil and gas gathering systems and pipelines, the effect of foreign regulation of production and transportation, general economic conditions, changes in supply due to drilling by other producers and changes in demand may adversely affect Orca Exploration's ability to market its gas production.

Uncertainties in Estimating Reserves and Future Net Cash Flows

There are numerous uncertainties inherent in estimating quantities of proved and probable reserves and cash flows to be derived therefrom, including many factors beyond the control of Orca Exploration. The reserve and cash flow information contained herein represents estimates only. The reserves and estimated future net cash flow from Orca Exploration's properties have been independently evaluated by McDaniel & Associates Consultants Ltd. These evaluations include a number of assumptions relating to factors such as initial production rates, production decline rates, ultimate recovery of reserves, timing and amount of capital expenditures, marketability of production, crude oil price differentials to benchmarks, future prices of oil and natural gas, operating costs, transportation costs, cost recovery provisions and royalties, TPDC "back-in" methodology and other government levies that may be imposed over the producing life of the reserves. These assumptions were based on price forecasts in use at the date of the relevant evaluations were prepared and many of these assumptions are subject to change and are beyond the control of Orca Exploration. Actual production and cash flows derived therefrom will vary from these evaluations, and such variations could be material.

Title to Properties

Although title reviews have been done and will continue to be done according to industry standards prior to the purchase of most oil and natural gas producing properties or the commencement of drilling wells, such reviews do not guarantee or certify that an unforeseen defect in the chain of title will not arise to defeat the claim of Orca Exploration which could result in a reduction of the revenue received by Orca Exploration.

Acquisition Risks

Orca Exploration intends to acquire natural gas infrastructure and possibly additional oil and gas properties. Although Orca Exploration performs a review of the acquired properties that it believes is consistent with industry practices, such reviews are inherently incomplete. It generally is not feasible to review in depth every individual property involved in each acquisition. Ordinarily, Orca Exploration will focus its due diligence efforts on the higher valued properties and will sample the remainder. However, even an in depth review of all properties and records may not necessarily reveal existing or potential problems, nor will it permit a buyer to become sufficiently familiar with the properties to assess fully their deficiencies and capabilities. Inspections may not be performed on every well, and structural or environmental problems, such as ground water contamination, are not necessarily observable even when an inspection is undertaken. Orca Exploration may be required to assume pre-closing liabilities, including environmental liabilities, and may acquire interests in properties on an "as is" basis. There can be no assurance that Orca Exploration's acquisitions will be successful.

Reliance on Key Personnel

Orca Exploration is highly dependent upon its executive officers and key personnel. The unexpected loss of the services of any of these individuals could have a detrimental effect on Orca Exploration. Orca Exploration does not maintain key life insurance on any of its employees or officers.

Controlling Shareholder

W. David Lyons, the Company's Chairman, and Chief Executive Officer is the beneficial controlling shareholder of Orca Exploration and holds approximately 99.5% of the outstanding Class A shares and approximately 16.7% of the Class B shares. Consequently, Mr. Lyons is the beneficial holder of approximately 20.8% of the equity (22.4% fully diluted) and controls 59.3% of the total votes of Orca Exploration.

CRITICAL ACCOUNTING ESTIMATES

In applying the Company's accounting policies, which are described in Note 3 to the Audited Financial Statements, management makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, vary to the actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

I) RESERVES

There are numerous uncertainties inherent in estimating quantities of proved and probable reserves and cash flows to be derived therefrom, including many factors beyond the control of Orca Exploration. The reserve and cash flow information contained herein represents estimates only. The reserves and estimated future net cash flow from Orca Exploration's properties have been independently evaluated by McDaniel & Associates Consultants Ltd. These evaluations include a number of assumptions relating to factors such as initial production rates, production decline rates, ultimate recovery of reserves, timing and amount of capital expenditures, marketability of production, abandonment provisions, crude oil price differentials to benchmarks, future prices of oil and natural gas, operating costs, transportation costs, cost recovery provisions and royalties, TPDC "back-in" methodology and other government levies that may be imposed over the producing life of the reserves. These assumptions were based on price forecasts in use at the date of the relevant evaluations were prepared and many of these assumptions are subject to change and are beyond the control of Orca Exploration.

Reserves are integral to the amount of depletion charged to the profit or loss.

II) EXPLORATION AND EVALUATION ASSETS

Under the Company's accounting policy expenditures incurred on the exploration for, and evaluation of, reserves are capitalized as intangible assets. These intangibles assets are then assessed for impairment when circumstances suggest that the carrying amount may exceed its recoverable value. Such circumstances include but are not limited to:

- the period for which the Company has the right to explore in the specific area has expired during the period, or will expire in the near future, and is not expected to be renewed;
- no further expenditure on exploration and evaluation is budgeted or planned;
- no reserves have been encountered;
- the evaluation of seismic data indicates that the reserves are unlikely to be of a commercial quantity;
- the quantity of hydrocarbon reserves are deemed not to be of commercially viable quantities and the entity has decided to discontinue further activities; and
- sufficient data exists to indicate that, although a development in the specific area is likely to proceed, the carrying amount of the exploration and evaluation asset is unlikely to be recovered in full from successful development or by sale.

The assessment for impairment involves estimates as to (i) the likely future commerciality of the asset and when such commerciality should be determined, (ii) future revenues and costs associated with the asset, and (iii) the discount rate to be applied to such revenues and costs for the purpose of deriving a recoverable value.

Exploration and evaluation assets are assessed for impairment if (i) sufficient data exists to determine technical feasibility and commercial viability, or (ii) facts and circumstances suggest that the carrying amount exceeds the recoverable amount. For purposes of impairment testing, exploration and evaluation assets are grouped by concession.

The technical feasibility and commercial viability of extracting a resource is considered to be determinable based on several factors including the assignment of proven reserves. A review of each exploration license or field is carried out, at least annually, to ascertain whether the project is technically feasible and commercially viable. Upon determination of technical feasibility and commercial viability, intangible exploration and evaluation assets attributable to those reserves are first tested for impairment and then reclassified from exploration and evaluation assets to a separate category within property and equipment referred to as oil and natural gas interests.

III) FAIR VALUE OF STOCK BASED COMPENSATION

All stock options issued or stock appreciation rights granted by the Company have to be valued at their fair value. In assessing the fair value of the equity based compensation, estimates have to be made as to (i) the volatility in share price, (ii) risk free rate of interest, and (iii) the level of forfeiture. In the case of stock options, this fair value is estimated at the date of issue and is not revalued, where as the fair value of stock appreciation rights is recalculated at each reporting period.

IV) COST RECOVERY

The Company is able to recover reasonable costs incurred on the development of the Songo Songo project out of 75% of the gross revenues less processing and pipeline tariffs ("Net Revenue"). There are inherent uncertainties in estimating when costs have been recovered as the government has several years to review the reasonableness of the costs.

V) RECEIVABLES

The Company considers the Songas and TANESCO receivables to be collectable, despite being long overdue. Both Songas and the Company have been impacted by TANESCO's inability to pay. The combination of written assurances from MEM backed by confirmation that the Government of Tanzania has raised substantial funding which is intended for the settlement of TANESCO debts, give management confidence that these debts will be recovered within a reasonable timeframe.

The accompanying consolidated financial statements of Orca Exploration Group Inc. are the responsibility of the Directors. The financial and operating information presented in this annual report is consistent with that shown in the consolidated financial statements.

The consolidated financial statements have been prepared by management, on behalf of the Board, in accordance with the accounting policies disclosed in the notes to the consolidated financial statements. Where necessary, management has made informed judgments and estimates in accounting for transactions which were not complete at the balance sheet date. In the opinion of management, the consolidated financial statements have been prepared within acceptable limits of materiality and are in accordance with International Financial Reporting Standards appropriate in the circumstances.

Management, with the participation of the Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Company's disclosure controls and procedures and has concluded that such disclosure controls and procedures are effective.

Management maintains appropriate systems of internal controls. Policies and procedures are designed to give reasonable assurance that transactions are properly authorised, assets are safeguarded and financial records are properly maintained to provide reliable information for the preparation of financial statements. An independent firm of Chartered Accountants, as appointed by the Shareholders, audited the consolidated financial statements in accordance with the Canadian Generally Accepted Auditing Standards and International Auditing Standards to enable them to express an opinion on the fairness of the consolidated financial statements in accordance with International Financial Reporting Standards.

The Board of Directors carries out its responsibility for the financial reporting and internal controls principally through an Audit Committee. The committee has met with external auditors and Management in order to determine if Management has fulfilled its responsibilities in the preparation of the consolidated financial statements. The consolidated financial statements have been approved by the Board of Directors on the recommendation of the Audit Committee.

W. David Lyons
Chairman and Chief Executive Officer
26 April 2013

Robert S. Wynne
Chief Financial Officer
26 April 2013

To the Shareholders of Orca Exploration Group Inc.

We have audited the accompanying consolidated statements of Orca Exploration Group Inc., which comprise the consolidated statements of financial position as at December 31, 2012 and December 31, 2011, the consolidated statements of comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of Orca Exploration Group Inc. as at December 31, 2012 and December 31, 2011, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board.

Emphasis of matter

Without modifying our opinion, we draw attention to Note 1 in the consolidated financial statements which describes that the Company needs to collect its receivables to fund ongoing operations and its exploration and development program. This condition, along with other matters as set forth in Note 1, indicates the existence of a material uncertainty that may cast significant doubt about the Company's ability to continue as a going concern.

KPMG LLP

Chartered Accountants
Calgary, Canada

April 26, 2013

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

YEARS ENDED 31 DECEMBER *US$'000 except per share amounts*	NOTE	**2012**	2011
REVENUE	*6, 7*	**77,259**	45,893
Cost of sales			
Production and distribution expenses		**(5,953)**	(6,088)
Depletion expense	*13*	**(8,968)**	(8,092)
		62,338	31,713
General and administrative expenses		**(17,989)**	(15,440)
Exploration asset impairment	*12*	**(8,284)**	–
Net finance costs	*9*	**(611)**	(953)
Profit before taxation		**35,454**	15,320
Taxation	*10*	**(17,125)**	(7,334)
Profit after taxation		**18,329**	7,986
Foreign currency translation gain from foreign operations		**89**	–
Total comprehensive income for the year		**18,418**	7,986
EARNINGS PER SHARE			
Basic *(US$)*	*17*	**0.53**	0.23
Diluted *(US$)*	*17*	**0.52**	0.22

Future operations (Note 1)

See accompanying notes to the consolidated financial statements.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

AS AT *US$'000*	NOTE	**31 Dec 2012**	31 Dec 2011
ASSETS			
Current assets			
Cash and cash equivalents		**16,047**	34,680
Trade and other receivables	*11*	**73,495**	40,348
Taxation receivable	*10*	**14,692**	5,880
Prepayments		**246**	302
		104,480	81,210
Non-current assets			
Exploration and evaluation assets	*12*	**5,720**	2,921
Property, plant and equipment	*13*	**102,044**	67,713
		107,764	70,634
Total assets		**212,244**	151,844
EQUITY AND LIABILITIES			
Current liabilities			
Trade and other payables	*14*	**45,496**	22,801
Bank loan	*15*	**5,842**	–
Taxation payable	*10*	**6,322**	2,403
		57,660	25,204
Non-current liabilities			
Deferred income taxes	*10*	**20,399**	15,194
Deferred additional profits tax	*10*	**8,250**	4,787
		28,649	19,981
Total liabilities		**86,309**	45,185
EQUITY			
Capital stock	*16*	**84,983**	84,610
Contributed surplus		**6,753**	6,268
Accumulated other comprehensive income		**89**	–
Accumulated income		**34,110**	15,781
		125,935	106,659
Total equity and liabilities		**212,244**	151,844

See accompanying notes to the consolidated financial statements.

Contractual obligations and committed capital investment (Note 19)
Contingencies (Note 20)

The consolidated audited financial statements were approved by the Board of Directors on 26 April 2013.

W H Smith

Director

Director

CONSOLIDATED STATEMENT OF CASH FLOWS

YEARS ENDED 31 DECEMBER *US$'000*	NOTE	2012	2011
CASH FLOWS FROM OPERATING ACTIVITIES			
Profit after taxation		**18,329**	7,986
Adjustment for:			
Depletion and depreciation	*13*	**9,281**	8,389
Impairment of assets	*12*	**8,284**	–
Gain on disposable of vehicle		**–**	(5)
Stock-based compensation	*16*	**1,152**	851
Deferred income taxes	*10*	**5,205**	2,385
Deferred additional profits tax	*7, 10*	**3,463**	2,527
Interest income	*9*	**(23)**	(5)
Unrealised loss on foreign exchange		**258**	530
Funds flow from operating activities		**45,949**	22,658
Increase in trade and other receivables		**(33,133)**	(27,171)
Increase in taxation receivable		**(8,812)**	(1,871)
Decrease in prepayments		**56**	107
Increase in trade and other payables		**22,589**	10,451
Increase in taxation payable		**3,919**	403
Net cash flows from operating activities		**30,568**	4,577
CASH FLOWS USED IN INVESTING ACTIVITIES			
Exploration and evaluation expenditures	*12*	**(11,083)**	(1,979)
Property, plant and equipment expenditures	*13*	**(43,612)**	(16,156)
Interest received	*9*	**23**	5
Proceeds from sale of vehicle		**–**	5
(Decrease)/increase in trade and other payables		**(716)**	3,541
Net cash used in investing activities		**(55,388)**	(14,584)
CASH FLOWS (USED IN)/FROM FINANCING ACTIVITIES			
Normal course issuer bid	*16*	**(12)**	(681)
Proceeds from exercise of options		**150**	–
Bank loan proceeds	*15*	**5,842**	–
Net cash flow from/(used in) financing activities		**5,980**	(681)
Decrease in cash and cash equivalents		**(18,840)**	(10,688)
Cash and cash equivalents at the beginning of the year		**34,680**	45,519
Effect of change in foreign exchange		**207**	(151)
Cash and cash equivalents at the end of the year		**16,047**	34,680

See accompanying notes to the consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

US$'000	CAPITAL STOCK	CONTRIBUTED SURPLUS	CUMULATIVE TRANSLATION ADJUSTMENT	ACCUMULATED INCOME	TOTAL
Note	*16*				
Balance as at 1 January 2012	84,610	6,268	–	15,781	106,659
Stock based compensation	–	720	–	–	720
Options exercised	383	(233)	–	–	150
Normal course issuer bid	(10)	(2)	–	–	(12)
Foreign currency translation of foreign operations	–	–	89	–	89
Total comprehensive income for the period	–	–	–	18,329	18,329
Balance as at 31 December 2012	**84,983**	**6,753**	**89**	**34,110**	**125,935**

US$'000	CAPITAL STOCK	CONTRIBUTED SURPLUS	CUMULATIVE TRANSLATION ADJUSTMENT	ACCUMULATED INCOME	TOTAL
Note	*16*				
Balance as at 1 January 2011	85,100	5,288	–	7,795	98,183
Stock based compensation	–	1,171	–	–	1,171
Normal course issuer bid	(490)	(191)	–	–	(681)
Total comprehensive income for the period	–	–	–	7,986	7,986
Balance as at 31 December 2011	**84,610**	**6,268**	**–**	**15,781**	**106,659**

See accompanying notes to the consolidated financial statements.

General Information

Orca Exploration Group Inc. ("Orca Exploration" or the "Company") was incorporated on 28 April 2004 under the laws of the British Virgin Islands. The Company produces and sells natural gas to the power and industrial sectors in Tanzania and has gas and oil exploration interests in Italy.

The consolidated audited financial statements of the Company and its subsidiaries for the year ended 31 December 2012 were authorised for issue in accordance with a resolution of the directors on 26th April 2013.

1 FUTURE OPERATIONS

These financial statements have been prepared on a going concern basis. The going concern basis of presentation assumes that the Company will continue in operation for the foreseeable future and be able to realize its assets and discharge its liabilities and commitments in the normal course of business.

The ability of the Company to continue as a going concern is dependent on the Company's ability to collect its receivables from government entities to fund ongoing operations and the exploration and development program. The continued deterioration of the financial position of the state utility, the Tanzanian Electrical Supply Company ("TANESCO"), has created uncertainty as to whether the Company will be able to collect cash to continue operations and meet its commitments. The immediate need to collect from its debtors may create significant doubt about the Company's ability to continue as a going concern.

The financial statements do not reflect adjustments that would be necessary if the going concern assumption were not appropriate. If the going concern basis were not appropriate for these financial statements, then adjustments would be necessary in the carrying amounts of assets and liabilities, the reported revenues and expenses, and the balance sheet classifications.

The Company generates in excess of 59% of its operating revenue from sales to the power sector companies, Songas Limited ("Songas") and TANESCO. Songas' financial security is heavily reliant on the payment of capacity and energy charges by TANESCO. TANESCO is dependent on the Government of Tanzania for some of its funding. Prior to 2012, despite having a history of delayed payments, TANESCO had settled in full the outstanding balance subsequent to each quarter end.

At 31 December 2012, TANESCO owed the Company US$33.3 million (including arrears of US$28.4 million) compared to US$24.2 million (including arrears of US$20.2 million) as at 31 December 2011. Subsequent to the end of the year, the Company has received US$1.0 million and, as of the date of this report, the arrears total US$43.0 million.

At the end of 2012, Songas owed the Company US$23.4 million, whilst the Company owed Songas US$17.5 million; there is no legal right to offset these amounts. Subsequent to the end of the year, the Company has neither received nor paid any amounts in settlement of these balances.

During 2012, there has been no substantive progress on payment of arrears owed by TANESCO and further, the state utility failed to remain current. Subsequent to the end of the year, in April 2013, the Government of Tanzania informed the Company that it raised approximately US$600 million in international credit markets as well as received a World Bank budget support package of US$100 million, the first of an expected three tranches of World Bank funding. The Government of Tanzania has assured the Company that a portion of the proceeds of these financings will be used to repay all of the outstanding arrears of TANESCO. In the event that Company does not collect from TANESCO the outstanding receivables at December 31, 2012 and TANESCO continues to be unable to pay the Company for subsequent 2013 gas deliveries, the Company will need additional funding for its ongoing operations within three to four months from the date of this report. There are no guarantees that such additional funding will be available when needed, or will be available on suitable terms.

During 2012, to help alleviate the funding gap caused by the delays in TANESCO payments the Company put in place a US$10 million facility with a bank in Tanzania. As at 31 December 2012, the Company had drawn down US$6.0 million of this facility, incurring financing charges of US$0.2 million. Subsequent to the end of the year, the Company drew the remaining US$4.0 million under the facility. Repayments commenced in March 2013.

2 BASIS OF PREPARATION

These consolidated financial statements are measured and presented in US dollars. Management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the period. Actual results could differ from these estimates. See Note 4 – Use of Estimates and Judgements.

A) Statement of Compliance

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board ("IASB").

B) Basis of consolidation

i) Subsidiaries

The consolidated financial statements include the accounts of Orca Exploration Group Inc, and all its wholly owned subsidiaries (collectively, "Orca Exploration" or the "Company"). Subsidiaries are those enterprises controlled by the Company. The following companies have been consolidated within the Orca Exploration financial statements:

Subsidiary	Registered	Holding	Functional currency
Orca Exploration Group Inc.	British Virgin Islands	Parent Company	US dollar
Orca Exploration Italy Inc.	British Virgin Islands	100%	Euro
Orca Exploration Italy Onshore Inc.	British Virgin Islands	100%	Euro
PAE PanAfrican Energy Corporation	Mauritius	100%	US dollar
PanAfrican Energy Tanzania Limited	Jersey	100%	US dollar
Orca Exploration UK Services Limited	United Kingdom	100%	GB Sterling

ii) Transactions eliminated upon consolidation

Inter-company balances and transactions, and any unrealised gains or losses arising from inter-company transactions, are eliminated in preparing the consolidated financial statements.

C) Foreign currency

i) Foreign currency transactions

The functional currencies of Orca Exploration Italy Inc. and Orca UK Services are the Euro and Sterling respectively. The assets and liabilities of these companies are translated into U.S. dollars at the period-end exchange rate. The income and expenses of the companies are translated into U.S. dollars at the average exchange rate for the period. Translation gains and losses are included in other comprehensive income

ii) Foreign currency translation

Orca Exploration Italy Inc. and Orca UK Services use the Euro and Sterling as their functional currencies. The assets and liabilities of these companies are translated into U.S. dollars at the period-end exchange rate. The income and expenses of the companies are translated into U.S. dollars at the average exchange rate for the period. Translation gains and losses are included in other comprehensive income.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements, and have been applied consistently by the Company.

A) Exploration and evaluation of assets, property plant and equipment

i) Exploration and evaluation assets

Exploration and evaluation costs are capitalised as intangible assets. Intangible assets includes lease and license acquisition costs, geological and geophysical costs and other direct costs of exploration and evaluation which the directors consider to be unevaluated until reserves are appraised to be commercially viable and technologically feasible as commercial, at which time they are transferred to property, plant and equipment following an impairment review and depleted accordingly. Where properties are appraised to have no commercial value or are appraised at values less than book values, the associated costs are treated as an impairment loss in the period in which the determination is made.

ii) Property, plant and equipment

Property, plant and equipment comprises the Company's tangible natural gas assets, development wells, together with leasehold improvements, computer equipment, motor vehicles and fixtures and fittings and are carried at cost, less any accumulated depletion, depreciation and accumulated impairment losses. Cost includes purchase price and construction costs for qualifying assets. Depletion of these assets commences when the assets are ready for their intended use. Only costs that are directly related to the discovery and development of specific oil and gas reserves are capitalised. The cost associated with tangible natural gas assets are amortised on a field by field unit of production method based on commercial proven reserves. The calculation of the unit of production amortisation takes into account the estimated future development cost of the field.

iii) Impairment of exploration and evaluation assets, property, plant and equipment

At each balance sheet date, the Company reviews the carrying amounts of its property, plant and equipment and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. Individual assets are grouped together as a cash generating unit for impairment assessment purposes at the lowest level at which there are identifiable cash flows that are independent from other group assets. In the case of exploration and evaluation assets, this will normally be at the Company's field level. If any such indication of impairment exists, the Company makes an estimate of its recoverable amount. The recoverable amount is the higher of fair value less costs to sell and value in use. Where the carrying amount of a cash generating unit exceeds its recoverable amount, the cash generating unit is considered impaired and is written down to its recoverable amount. In assessing the value in use, the estimated future cash flows are adjusted for the risks specific to the cash generating unit and are discounted to their present value with a discount rate that reflects the current market indicators. Where an impairment loss subsequently reverses, the carrying amount of the asset cash–generating unit is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the cash generating unit in prior years. A reversal of an impairment loss is recognised as income immediately.

B) Operatorship

The Company operates the Songo Songo gas field, flow lines and gas processing plant. The Songas wells, flowlines and gas plant are operated by the Company on behalf of Songas on a no cost no profit basis. The cost of operating and maintaining the wells and flow lines is paid for by Orca Exploration and Songas in proportion to the respective volumes of Protected Gas and Additional Gas sales. The costs of operating and maintaining the wells and flow lines are reflected in the accounts to the extent that the costs were incurred to accomplish Additional Gas sales. The cost of operating the gas processing plant and pipeline to Dar es Salaam is paid by Songas. When there are Additional Gas sales, a tariff is paid to Songas as compensation for using the gas processing plant and pipeline. This tariff is netted against revenue.

C) Employment Benefits

i) Pension

The Company does not operate a pension plan, but it does make defined contributions to the statutory pension fund for employees in Tanzania. Obligations for contributions to the statutory pension fund are recognised as an expense in the income statement as incurred.

ii) Stock options

The stock option plan provides for the granting of stock options to directors, Company officers and key personnel employees to acquire shares at an exercise price determined by the market value at the date of grant. The exercise price of each stock option is determined at the closing market price of the Class B shares on the day prior to the day of grant. Each stock option granted permits the holder to purchase one Class B share at the stated exercise price. The Company records a charge to the profit and loss account using the Black-Scholes fair valuation option pricing model. The valuation is dependent on a number of estimates, including the risk free interest rate, the level of stock volatility, together with an estimate of the level of forfeiture. The level of stock volatility is calculated with reference to the historic traded daily closing share price at the date of issue.

iii) Stock appreciation rights

Stock appreciation rights are issued to certain key managers, officers, directors and employees. The fair value of stock appreciation rights is expensed in the profit and loss in accordance with the service period. The fair value of the stock appreciation rights is revalued every reporting date with the change in the value recognized in the income statement.

D) Asset retirement obligations

No provision has been made for future site restoration costs in Tanzania since the Company has currently no legal or contractual or constructive obligation under the Songo Songo Production Sharing Agreement ("PSA") to restore the fields at the end of their commercial lives. At such a time as the Company may be granted an extension of the term of the PSA which encompasses the end of the field life, or other amendment to the PSA which requires the Company to do so, a provision will be made for future site restoration costs.

E) Revenue recognition, production sharing agreements and royalties

The Company recognises revenue related to Additional Gas sales when title passes to a customer. The Company conducts operations jointly with the Tanzanian government and the Tanzania Petroleum Development Corporation ("TPDC"), a "parastatal entity" in accordance with the PSA. Under this agreement, the Company pays both its share and the parastatal's share of operating, administrative and capital costs. The Company recovers all reasonably incurred operating, administrative and capital costs including the parastatal's share of these costs from future revenues over several years ("Cost Gas"). The parastatal's share of operating and administrative costs, are recorded in operating and general and administrative costs when incurred and capital costs are recorded in 'Property, plant and equipment'. All recoveries are recorded as revenue in the year of recovery. The Company is entitled to a share of production in excess of the Cost Gas ("Profit Gas"). Operating revenue represents the Company's share of Cost Gas and Profit Gas during the period.

F) Additional profits tax

Under the terms of the PSA, in the event that all costs have been recovered with an annual return of 25% plus the percentage change in the United States Industrial Goods Producer Price Index, an additional profits tax ("APT") is payable to the Government of Tanzania. This tax is considered to be a royalty and is netted against revenue. Deferred APT is provided for by forecasting the total APT payable as a proportion of the forecast Profit Gas over the term of PSA license. The actual APT that will be paid is dependent on the achieved value of the Additional Gas sales and the quantum and timing of the operating costs and capital expenditure program.

G) Taxation

Income tax on the profit for the year comprises current and deferred tax. The Company is liable for Tanzanian income tax, but this is recovered from TPDC through the profit-sharing arrangement. Where current income tax is payable, the Company's revenue is adjusted for the amount of current tax payable and the income tax is shown as current tax. Deferred tax is provided using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax provided is based on the expected manner of realisation or settlement of carrying amounts of assets and liabilities using tax rates substantively enacted at the balance sheet date. A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefits will be realised.

H) Segmental reporting

The Company has interests in Tanzania and Italy.

I) Depreciation

Depreciation for non-natural gas properties is charged to the income statement on a straight line basis over the estimated useful economic lives of each class of asset. The estimated useful lives are as follows:

Leasehold improvement	Over remaining life of the lease
Computer equipment	3 years
Vehicles	3 years
Fixtures and fittings	3 years

J) Financial Instruments

Non-derivative financial instruments include cash and cash equivalents, trade and other receivables, and trade and other payables. Non-derivative financial instruments are recognized initially at fair value plus any directly attributable transaction costs.

The Company has reported cash and cash equivalents at fair value. Cash and cash equivalents are comprised of cash on hand, term deposits held with banks, and other short-term highly liquid investments with original maturities of three months or less. Bank overdrafts that are repayable on demand and form an integral part of the Company's cash management, whereby management has the ability and intent to net bank overdrafts against cash, are included as a component of cash and cash equivalents for the purpose of the statement of cash flows. The Company's trade and other receivables, trade and other payables, are classified as other non-derivative financial instruments. Subsequent to the initial recognition, other non-derivative financial instruments are measured at amortized cost using the effective interest method, less any impairment losses.

K) Contributed surplus

This is used to record two types of transactions:

(i) To recognise the fair value of equity settled stock based compensation expensed in the year.

(ii) To account for the difference between the aggregated book value of the shares purchased under the normal course issuer bid and the actual consideration.

L) New accounting standards and interpretations

The following standards, amendments and interpretations applicable to the Company are in issue but not yet effective and have not been early adopted in these consolidated financial statements.

New and Amended Standards Effective for annual periods beginning on or after		
IFRS 9	Financial Instruments	January 1, 2015
IFRS 10	Consolidated Financial Statements	January 1, 2013
IFRS 11	Joint Arrangements and Consolidated Financial Statements, Joint Arrangements and Disclosures of Interests in Other Entities	January, 1 2013
IFRS 12	Disclosure of Interests in Other Entities and Consolidated Financial Statements, Joint Arrangements and Disclosures of Interests in Other Entities	January 1, 2013
IFRS 13	Fair Value Measurement	January 1, 2013
IAS 28 (amendments)	Investments in Associates and Joint Ventures	January 1, 2013
IAS 1 (amendments)	Investments in Associates and Joint Ventures	January 1, 2013
IAS 19 (amendments)	Employee Benefits	January 1, 2013
IAS 32 and IFRS 7 (amendments)	Offsetting Financial Assets and Liabilities	January 1, 2013

The Company intends to adopt the interpretation in its financial statements for the annual period beginning on January 1, 2013. The Company does not expect the adoption of the standards effective January 1, 2013 to have a material impact on the financial statements. The extent of the impact from the adoption of IFRS 9 has not been determined.

4 USE OF ESTIMATES AND JUDGEMENTS

In applying the Company's accounting policies, which are described in Note 3, management makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, vary to the actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

I) Reserves

There are numerous uncertainties inherent in estimating quantities of proved and probable reserves and cash flows to be derived therefrom, including many factors beyond the control of Orca Exploration. The reserve and cash flow information contained herein represents estimates only. The reserves and estimated future net cash flow from Orca Exploration's properties have been independently evaluated by McDaniel & Associates Consultants Ltd. These evaluations include a number of assumptions relating to factors such as initial production rates, production decline rates, ultimate recovery of reserves, timing and amount of capital expenditures, marketability of production, abandonment provisions, crude oil price differentials to benchmarks, future prices of oil and natural gas, operating costs, transportation costs, cost recovery provisions and royalties, TPDC "back-in" methodology and other government levies that may be imposed over the producing life of the reserves. These assumptions were based on price forecasts in use at the date of the relevant evaluations were prepared and many of these assumptions are subject to change and are beyond the control of Orca Exploration.

Reserves are integral to the amount of depletion charged to the profit or loss.

II) Exploration and evaluation assets

Under the Company's accounting policy expenditures incurred on the exploration for, and evaluation of, reserves are capitalized as intangible assets. These intangibles assets are then assessed for impairment when circumstances suggest that the carrying amount may exceed its recoverable value. Such circumstances include but are not limited to:

- the period for which the Company has the right to explore in the specific area has expired during the period, or will expire in the near future, and is not expected to be renewed;
- no further expenditure on exploration and evaluation is budgeted or planned;
- no reserves have been encountered;
- the evaluation of seismic data indicates that the reserves are unlikely to be of a commercial quantity;
- the quantity of hydrocarbon reserves are deemed not to be of commercially viable quantities and the entity has decided to discontinue further activities; and
- sufficient data exists to indicate that, although a development in the specific area is likely to proceed, the carrying amount of the exploration and evaluation asset is unlikely to be recovered in full from successful development or by sale.

The assessment for impairment involves estimates as to (i) the likely future commerciality of the asset and when such commerciality should be determined, (ii) future revenues and costs associated with the asset, and (iii) the discount rate to be applied to such revenues and costs for the purpose of deriving a recoverable value.

Exploration and evaluation assets are assessed for impairment if (i) sufficient data exists to determine technical feasibility and commercial viability, or (ii) facts and circumstances suggest that the carrying amount exceeds the recoverable amount. For purposes of impairment testing, exploration and evaluation assets are grouped by concession.

The technical feasibility and commercial viability of extracting a resource is considered to be determinable based on several factors including the assignment of proven reserves. A review of each exploration license or field is carried out, at least annually, to ascertain whether the project is technically feasible and commercially viable. Upon determination of technical feasibility and commercial viability, intangible exploration and evaluation assets attributable to those reserves are first tested for impairment and then reclassified from exploration and evaluation assets to a separate category within property and equipment referred to as oil and natural gas interests.

III) Fair value of stock based compensation

All stock options issued or stock appreciation rights granted by the Company have to be valued at their fair value. In assessing the fair value of the equity based compensation, estimates have to be made as to (i) the volatility in share price, (ii) the risk free rate of interest, and (iii) the level of forfeiture. In the case of stock options, this fair value is estimated at the date of issue and is not revalued, whereas the fair value of stock appreciation rights is recalculated at each reporting period.

IV) Cost recovery

The Company is able to recover reasonable costs incurred on the development of the Songo Songo project out of 75% of the gross revenues less processing and pipeline tariffs ("Net Revenue"). There are inherent uncertainties in estimating when costs have been recovered as the government has several years to review the reasonableness of the costs.

V) Receivables

The Company considers the Songas and TANESCO receivables to be collectable, despite being long overdue. Both Songas and the Company have been impacted by TANESCO's inability to pay. The combination of written assurances from the Ministry of Energy and Minerals ("MEM") backed by confirmation from the Government that it has raised substantial funding which is intended for the settlement of TANESCO debts, give management confidence that these debts will be recovered within a reasonable timeframe.

The Company has a substantial "Tax Receivable" balance. This arises from the revenue sharing mechanism within the PSA which entitles the Company to a share of revenue equivalent to its tax charge, grossed up at the prevailing rate. This debtor is collected by way of an offset against TPDC's share of revenue, as and when the Company pays its tax.

5 RISK MANAGEMENT

The Company, by its activities in oil and gas exploration, development and production, is exposed to the risk associated with the unpredictable nature of the financial markets as well as political risk associated with conducting operations in an emerging market. The Company seeks to manage its exposure to these risks wherever possible.

I) Foreign exchange risk

Foreign exchange risk arises when transactions and recognised assets and liabilities of the Company are denominated in a currency that is not the U.S. dollar functional currency.

The Company operates internationally and is exposed to foreign exchange risk arising from currency exposures to U.S. dollars. The main currencies to which the Company has an exposure are: Tanzanian shillings, British pounds sterling, Euros and Canadian dollars.

The majority of the expenditure associated with the operation of the gas distribution system is denominated in Tanzanian shillings. The majority of the consultants' contracts are denominated in British pounds sterling. All of the capital stock, equity financing and any associated stock based compensation are denominated in Canadian dollars. All of the operational revenue and the majority of capital expenditure are denominated in US dollars.

There are no forward exchange rate contracts in place.

A 10% increase in the U.S. dollars against the relevant foreign currency would result in an overall reduction in working capital by US$1.9 million to US$44.9 million and a reduction in profit before tax to US$33.6 million. The sensitivity includes only outstanding foreign currency denominated monetary items and adjusts their translation at period end for a 10% change in the foreign currency rates. A 10% sensitivity rate is used when reporting foreign currency risk internally to key management personnel and represents management's assessment of the reasonable possible change in foreign exchange rates.

II) Commodity price risk

The Songo Songo gas field is the first gas field to be developed in East Africa. The Company has therefore been able to negotiate industrial gas sales contracts with gas prices that are at a discount to the lowest cost alternative fuels in Dar es Salaam, namely Heavy Fuel Oil ("HFO") and coal. The price of HFO is exposed to the volatility in the market price of crude oil.

III) Interest rate risk

The Company has a medium term loan which is repayable in twelve instalments, beginning in March 2013. The interest rate is defined in relation to LIBOR and the exposure to rate changes is considered minor.

IV) Credit risk

The Company is exposed to significant credit risk. All of the Company's production is currently derived in Tanzania. The sales are made to the power sector and the industrial sector. In relation to sales to the power sector, the Company has a short-term contract with Songas for the supply of gas to the Ubungo power plant and a contract with TANESCO to supply approximately 37 MMcfd to fire 147 MW of TANESCO power generation. The contracts with Songas and TANESCO accounted for 59% of the Company's operating revenue during 2012 and US$47.5 million of the trade receivables at year-end. Songas itself is heavily reliant on the payment of capacity and energy charges by TANESCO for its liquidity.

Although TANESCO has a long history of delayed payments, it has, in previous years settled in full subsequent to the period end. However, during 2012, there has been a marked deterioration in the situation. Despite the Company receiving numerous assurances from TANESCO and the Government of Tanzania regarding payment, the outstanding balance has continued to grow. Since 31st December 2012, the Company has received US$1.0 million from TANESCO. As at the date of this report TANESCO owes the Company US$49.3 million.

Sales to the industrial sector, currently 37 customers, are subject to an internal credit review to minimize the risk of non-payment.

The Company is currently in discussions with TPDC concerning the commercial terms for the sale of gas volumes associated with a planned expansion of Songo Songo production, the conditions for which are described under V) below. The Company has no history with TPDC as a debtor. Any contract with TPDC will expose the Company to additional credit risk with a parastatal entity in Tanzania. Management intends to manage such credit exposure with risk insurance or other credit enhancement mechanisms.

V) Liquidity risk

Liquidity risk is the risk that the Company will not have sufficient funds to meet its liabilities. Cash forecasts identifying liquidity requirements of the Company are produced on a regular basis. These are reviewed to ensure sufficient funds exist to finance the Company's current operational and investment cash flow requirements. The Company has US$45.5 million of financial liabilities with regards to trade and other payables identified in Note 14 of which US$38.5 million is due within one to three months, nil is due within three to six months, and US$7.1 million is due within six to twelve months. The Company has a current taxation liability of US$6.3 million payable within three months. Management forecasts that, unless payment is secured from TANESCO over the next three to four months, the Company will be unable to meet its current liabilities as they fall due through the use of existing cash balances and self generated cash flows, and accordingly will require external financing, or a commensurate reduction in operations to avoid the accumulation of unfunded liabilities.

Developing additional productive capacity at Songo Songo, including the drilling of the SS-12 development well and the Songo Songo West exploration well, is dependent on (i) the receipt of outstanding overdue payments of approximately US$43 million from TANESCO; (ii) satisfactory completion of all outstanding issues relating to the Government Negotiating Team ("GNT"); (iii) completion of commercial terms for the sale and transport of incremental gas volumes; (iv) reasonable assurance of completion of the Government of Tanzania Natural Gas Infrastructure Project commissioned in November 2012; and (v) financing. There is no assurance that financing will be available when the Company requires same, and on reasonable terms and conditions.

VI) Capital risk management

The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to achieve an optimal capital structure to reduce the cost of capital. The level of risk currently in Tanzania prohibits the optimisation of capital structure as many sources of traditional capital are unavailable. The Company currently has a medium-term loan facility of US$10 million of which US$6 million had been drawn at the year end. Subsequent to year end, the remaining US$4 million was drawn and repayments commenced in March 2013.

VII) Material uncertainty

In February 2012 on the recommendation of MEM, the Government announced that it was establishing a negotiating team, the GNT, to discuss a number of issues raised in parliament in relation to the Company's Songo Songo PSA with TPDC and the Government of Tanzania. In Tanzania, government negotiating teams are a common mechanism to negotiate with business. The scope of the GNT was to discuss a number of points that were raised by the Parliamentary Committee for Energy into the workings of the PSA. This included, but is not limited to, TPDC back in rights, profit sharing arrangements, the unbundling of the downstream assets, cost recovery and Orca's Exploration's management of the upstream operations. After making submissions to the GNT, the Company commenced discussions in April 2012 and further in July 2012, at which time an agreement in principle was been reached on a number of major points to resolve the issues. The GNT has completed its mandate, and the responsibility for finalisation, documentation and implementation has moved back to MEM. The agreement in principal contemplated completion this process by the end of 2012. As at the date of this report, a number of conditions precedent have not been met and a number of issues remain to be fully resolved and documented. The outcome of these negotiations could have a significant impact on the operations of the Company, which cannot be estimated at this time. The Company will continue to discuss these matters in good faith with the government and will look to reach a satisfactory agreement that may lead to a material change in the economic terms of the PSA. However, the Company reserves its rights to defend its position should no satisfactory agreement be reached.

VIII) Evolving regulatory environment

The fiscal and regulatory environment for oil & gas exploration and development in Tanzania is in its infancy. Following the discovery of significant offshore natural gas resources by international exploration and development companies, there was pressure on the government to create a clear fiscal and regulatory framework for the industry. In November 2012, the Government of Tanzania introduced a draft natural gas policy for review and consultation amongst stakeholders. The draft policy contemplates, among other things, a restructuring of TPDC, increasing government ownership and control over infrastructure and resources, strategic involvement in the LNG value chain, the establishment of TPDC as monopoly gas aggregator in the country, and the establishment of government controlled natural gas prices. The draft policy as contemplated conflicts in a number of areas with the rights of the Company under the PSA and has the potential, if implemented in its current form to materially affect the Company's business.

The Company operates in jurisdictions with complex tax laws and regulations, which are evolving over time. The Company has taken certain tax positions in its filings and these filings are subject to audit and potential reassessment after the lapse of considerable time. Accordingly, the actual income tax impact may differ significantly from that estimated and recorded by management.

6 SEGMENT INFORMATION

The Company has one reportable segment which is international exploration, development and production of petroleum and natural gas. The Company currently has producing assets in Tanzania and exploration interests in Italy.

	2012			2011		
US$'000	Italy	Tanzania	Total	Italy	Tanzania	Total
External revenue	**–**	**77,758**	**77,259**	–	45,893	45,893
Segment income/(loss)	**(8,284)**	**26,613**	**18,329**	–	7,986	7,986
Total assets	**834**	**211,410**	**212,244**	911	150,933	151,844
Total liabilities	**714**	**85,595**	**86,309**	4	45,181	45,185
Capital additions	**7,531**	**47,164**	**54,695**	911	17,224	18,135
Depletion & depreciation	**–**	**9,281**	**9,281**	–	8,389	8,389
Exploration assets impairment	**8,284**	**–**	**8,284**	–	–	–

7 REVENUE

	YEARS ENDED 31 DECEMBER	
US$'000	**2012**	2011
Operating revenue	**64,192**	41,794
Current income tax adjustment	**16,530**	6,626
Deferred additional profits tax	**(3,463)**	(2,527)
Revenue	**77,259**	45,893

The Company's total revenues for the year amounted to US$77,259 after adjusting the Company's operating revenue of US$64,192 by:

i) adding US$16,530 for income tax for the current year. The Company is liable for income tax in Tanzania, but the income tax is recoverable out of TPDC's Profit Gas when the tax is payable. To account for this, revenue is adjusted to reflect the current income tax charge or loss.

ii) subtracting US$3,463 for the deferred effect of additional profits tax. This tax is considered a royalty and is netted against revenue.

8 PERSONNEL EXPENSES

The average number of employees during the year was 48 (2011: 42). The costs are as follows:

	YEARS ENDED 31 DECEMBER	
US$'000	**2012**	2011
Wages and salaries	**4,725**	4,745
Social security costs	**239**	677
Other statutory costs	**312**	312
	5,276	5,734
Stock based compensation	**1,152**	851
	6,428	6,585

The personnel stock based compensation is recorded under general and administrative expenses in the statement of comprehensive income. The balance of personnel expenses for 2012 of US$5.3 million (2011: US$5.7 million) is recorded in distribution and production expenses and general administrative expenses at US$0.8 million (2011: US$1.1 million) and US$4.5 million (2011: US$4.6 million) respectively.

9 NET FINANCE COSTS

	YEARS ENDED 31 DECEMBER	
US$'000	**2012**	2011
FINANCE INCOME		
Interest income	**23**	5
Foreign exchange gain	**93**	80
	116	85
FINANCE CHARGES		
Interest expense	**(315)**	(100)
Foreign exchange loss	**(412)**	(938)
	(727)	(1,038)
Net finance costs	**(611)**	(953)

10 TAXATION

Under the terms of the PSA with TPDC and the Government of Tanzania, the Company is liable to pay income tax at the corporate rate of 30% on profits generated in Tanzania. The amount paid is then recovered in full from TPDC by adjusting its share of Profit Gas when the current tax liability is paid.

	YEARS ENDED 31 DECEMBER	
US$'000	**2012**	2011
Current tax	**11,920**	4,949
Deferred tax	**5,205**	2,385
	17,125	7,334

Total taxes of US$7.7 million have been paid during the year in relation to the settlement of the 2011 tax liability and provisional payments for 2012. Total provisional tax payments of US$4.5 million were made in 2011.

TAX RATE RECONCILIATION	YEARS ENDED 31 DECEMBER	
US$'000	**2012**	2011
Profit before taxation	**35,454**	15,320
Provision for income tax calculated at the statutory rate of 30%	**10,636**	4,596
Add the tax effect of non-deductible income tax items:		
Administrative and operating expenses	**2,953**	2,042
Exploration assets impairment	**2,485**	–
Financing charge	**29**	–
Stock- based compensation	**346**	255
Permanent differences	**675**	441
	17,125	7,334

As at 31 December 2012, there were temporary differences between the carrying value of the assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Accordingly a deferred tax liability has been recognized for the year ended 31 December 2012.

A deferred tax asset of US$2.2 million in respect of Longastrino Italy E&E costs has not been recognised because it is not probable that there will be future profits against which this can be utilised.

The deferred income tax liability includes the following temporary differences:

	AS AT 31 DECEMBER	
US$'000	**2012**	2011
Differences between tax base and carrying value of property, plant and equipment	**16,341**	14,409
Income tax recoverable	**6,744**	2,416
Other liabilities		
Employee bonuses	**(109)**	(145)
TPDC Additional Profit Gas	**(102)**	(50)
Additional Profits Tax	**(2,475)**	(1,436)
	20,399	15,194

Additional Profits Tax

Under the terms of the PSA, in the event that all costs have been recovered with an annual return of 25% plus the percentage change in the United States Industrial Goods Producer Price Index ("PPI"), an Additional Profits Tax ("APT") is payable.

The Company provides for Deferred APT by forecasting the total APT payable as a proportion of the forecast Profit Gas over the term of the PSA. The effective APT rate of 31.8% is then applied to Profit Gas of US$10.7 million in 2012 (2011: US$12.6 million), accordingly, US$3.5 million (2011: US$2.5 million) has been netted off revenue for the year ended 31 December 2012.

Management does not anticipate that any APT will be payable in 2013, as the forecast revenues will not be sufficient to cover the un-recovered costs brought forward as inflated by 25% plus the PPI percentage change and the forecast expenditures for 2013. The actual APT that will be paid is dependent on the achieved value of the Additional Gas sales and the quantum and timing of the operating costs and capital expenditure program.

Tax Receivable

The Company has a "Tax Receivable" balance of US$14,692 (2011: US$5,880). This arises from the revenue sharing mechanism within the PSA which entitles the Company to a share of revenue equivalent to its tax charge, grossed up at the prevailing rate. This debtor is collected by way of an offset against TPDC's share of revenue, as and when the Company pays its tax.

11 TRADE AND OTHER RECEIVABLES

	YEARS ENDED 31 DECEMBER	
US$'000	**2012**	2011
TANESCO	**33,256**	24,226
Songas	**14,283**	3,720
Other debtors	**12,791**	7,767
Trade receivables	**60,330**	35,713
Other receivables	**13,165**	4,635
	73,495	40,348

AGED ANALYSIS	Current	>30 <60	>60 <90	>90	2012	2011
TANESCO	4,894	5,655	5,321	17,386	**33,256**	24,226
Songas	1,134	992	1,114	11,043	**14,283**	3,720
Other debtors	7,935	2,491	1,816	549	**12,791**	7,767
Trade receivables	13,963	9,138	8,251	28,977	**60,330**	35,713

Subsequent to 31 December 2012, US$1.0 million has been received from TANESCO, and US$10.7 million from other debtors. In addition to the trade receivable from Songas of US$14.3 million, an additional US$9.1 million is due from Songas with respect to Gas Plant operations, which is included in Other receivables.

The balance of other debtors which has yet to be collected relates to a take-or-pay obligation and is expected to be received in the near future.

12 EXPLORATION AND EVALUATION ASSETS

US$'000	Italy	Tanzania	Total
COSTS			
As at 1 January 2012	911	2,010	2,921
Additions	7,531	3,552	11,083
Impairment	(8,284)	–	(8,284)
As at 31 December 2012	**158**	**5,562**	**5,720**

US$'000	Italy	Tanzania	Total
COSTS			
As at 1 January 2011	–	942	942
Additions	911	1,068	1,979
As at 31 December 2011	**911**	**2,010**	**2,921**

TANZANIA

The exploration and evaluation asset represents site survey costs and materials purchased in preparation for the drilling of the first Songo Songo West well ("SSW-1") prior to suspension of the 2012 drilling programme. The SSW-1 well is part of the initial evaluation of the Songo Songo West prospect which is required to determine the existence of proven and probable reserves.

ITALY

Pursuant to the terms of the Company's Longastrino Block farm-in in the Po Valley Basin the Company spent US$7.5 million during 2012 related to the drilling of the La Tosca exploration well. The well was unsuccessful and the related accumulated costs were impaired. The residual cost represents equipment with a resale value which the Company intends to realise.

13 PROPERTY, PLANT AND EQUIPMENT

US$'000	Tanzania	Leasehold improvements	Computer equipment	Vehicles	Fixtures & Fittings	Total
COSTS						
As at 1 January 2012	96,014	320	701	249	334	97,618
Additions	42,944	–	46	–	622	43,612
Disposals	–	(64)	–	(47)	(6)	(117)
As at 31 December 2012	**138,958**	**256**	**747**	**202**	**950**	**141,113**
DEPLETION AND DEPRECIATION						
As at 1 January 2012	28,833	271	520	196	85	29,905
Charge for period	8,968	12	129	45	127	9,281
Depreciation on disposals	–	(64)	–	(47)	(6)	(117)
As at 31 December 2012	**37,801**	**219**	**649**	**194**	**206**	**39,069**
NET BOOK VALUES						
As at 31 December 2012	**101,157**	**37**	**98**	**8**	**744**	**102,044**

US$'000	Tanzania	Leasehold improvements	Computer equipment	Vehicles	Fixtures & Fittings	Total
COSTS						
As at 1 January 2011	80,323	320	509	231	108	81,491
Additions	15,691	–	192	47	226	16,156
Disposals	–	–	–	(29)	–	(29)
As at 31 December 2011	**96,014**	**320**	**701**	**249**	**334**	**97,618**
DEPLETION AND DEPRECIATION						
As at 1 January 2011	20,741	244	345	149	66	21,545
Charge for period	8,092	27	175	76	19	8,389
Depreciation on disposals	–	–	–	(29)	–	(29)
As at 31 December 2011	**28,833**	**271**	**520**	**196**	**85**	**29,905**
NET BOOK VALUE						
As at 31 December 2011	**67,181**	**49**	**181**	**53**	**249**	**67,713**

In determining the depletion charge, it is estimated by the independent reserve engineers that future development costs of US$107.1 million (2011: US$127.8 million) will be required to bring the total proved reserves to production. During the year the Company recognized depreciation of US$0.3 million (2011: US$0.3 million) in General and Administrative expenses.

14 TRADE AND OTHER PAYABLES

	AS AT 31 DECEMBER	
US$'000	**2012**	2011
TPDC	**4,378**	(81)
Songas	**17,459**	5,823
Other trade payables	**4,458**	12,993
Trade payables	**26,295**	18,735
Accrued liabilities	**19,030**	3,912
Related party (Note 18)	**171**	154
	45,496	22,801

The Company's exposure to credit, currency and interest risk related to trade and other payables is disclosed in Note 4.

15 BANK LOAN

In September 2012, the Company closed a US$10 million 18-month bridge loan facility with a Tanzania bank to finance the Company's working capital requirements in Tanzania. The facility is secured by an assignment of accounts receivable and a fixed and floating charge on the assets of the Company. As at 31 December the Company had drawn down US$6.0 million under the facility and paid US$0.2 million in financing fees. Subsequent to year-end, in March 2013, the Company drew the remaining US$4.0 million. Principal amounts drawn under the facility are repayable in 12 equal monthly instalments which commenced in March 2013. Interest is payable monthly at three-month US LIBOR plus 8%. An additional interest rate of 2% will be applied for any period in which the TANESCO receivable is greater than 240-days.

16 Capital stock

a) Authorised

50,000,000	Class A Common Shares	No par value
100,000,000	Class B Subordinate Voting Shares	No par value
100,000,000	First Preference Shares	No par value

The Class A and Class B shares rank pari passu in respect of dividends and repayment of capital in the event of winding-up. Class A shares carry twenty (20) votes per share and Class B shares carry one vote per share. The Class A shares are convertible at the option of the holder at any time into Class B shares on a one-for-one basis. The Class B shares are convertible into Class A shares on a one-for-one basis in the event that a take-over bid is made to purchase Class A shares which must, by reason of a stock exchange or legal requirements, be made to all or substantially all of the holders of Class A shares and which is not concurrently made to holders of Class B shares.

b) Changes in the capital stock of the Company were as follows:

Authorized and Issued Share Capital

	2012			2011		
Thousands of shares or US$'000	Authorised	Issued/ Repurchased	Amount	Authorised	Issued	Amount
CLASS A SHARES						
As at 1 January and 31 December	**50,000**	**1,751**	**983**	50,000	1,751	983
CLASS B SHARES						
As at 1 January	**100,000**	**32,746**	**83,627**	100,000	32,939	84,117
Stock options exercised	**–**	**150**	**383**	–	–	–
Normal course issuer bid	**–**	**(4)**	**(10)**	–	(193)	(490)
As at 31 December	**100,000**	**32,892**	**84,000**	100,000	32,746	83,627
Total shares as at 31 December	**150,000**	**34,643**	**84,983**	150,000	34,497	84,610

All of the issued capital stock is fully paid.

STOCK OPTIONS

	2012		2011	
Thousands of options or CDN$	**Options**	**Exercise Price**	Options	Exercise Price
Outstanding as at 1 January	**3,057**	**1.00 to 13.55**	2,557	1.00 to 13.55
Forfeited/Expired	**(1,385)**	**4.75 to 13.55**	–	–
Exercised	**(150)**	**1.00**	–	–
Issued	**400**	**3.18**	500	3.60 to 4.75
Outstanding as at 31 December	**1,922**	**1.00 to 3.60**	3,057	1.00 to 13.55

The weighted average remaining life and weighted average exercise prices of options at 31 December 2012 were as follows:

Exercise Price *(CDN$)*	Number outstanding as at 31 Dec 2012 *('000)*	Weighted Average Remaining Contractual Life *(years)*	Number Exercisable as at 31 Dec 2012 *('000)*	Weighted Average Exercise Price *(CDN$)*
1.00	1,272	1.66	1,272	1.00
3.18	400	4.29	400	3.18
3.60	250	3.75	250	3.60
	1,922		1,922	

There were 400,000 new stock options issued during the year with an exercise price of CDN$3.18. The stock options issued fully vested on 31 December 2012 and have a term of five years. A total charge of US$0.7 million has been recognised for the year in relation to the stock options and is included in General & Administrative expenses.

STOCK APPRECIATION RIGHTS

	2012		2011	
Thousands of stock appreciation rights or CDN$	**SAR**	**Exercise Price**	SAR	Exercise Price
Outstanding as at 1 January	**1,005**	**4.20 to 13.55**	1,005	4.20 to 13.55
Expired	**(690)**	**8.7 to 13.55**	–	–
Granted (i)	**430**	**2.35 to 2.70**	–	–
Outstanding as at 31 December	**745**	**2.35 to 5.30**	1,005	4.20 to 13.55

(i) *A total of 100,000 stock appreciation rights were issued in August 2012 with an exercise price of CDN$2.70. These rights have a term of five years and vest in three equal instalments, the first third vesting on the anniversary of the grant date. A further 330,000 stock appreciation rights were issued in December 2012 with an exercise price of CDN$2.35 which vested immediately. There is no maximum liability associated with these rights.*

The Company records a charge to the income statement using the Black-Scholes fair valuation option pricing model every reporting period with a resulting liability being recognised in trade and other payables. In the valuation of stock options and stock appreciation rights at the reporting date, the following assumptions have been made: a risk free rate of interest of 1.50% stock volatility of 53% to 71%; 0% dividend yield; 0% forfeiture; a closing stock price of CDN$3.00 per share.

As at 31 December 2012, a total accrued liability of US$0.6 million (2011: US$0.2 million) has been recognised in relation to the stock appreciation rights. The liability increased by US$0.4 million during the year reflects the issue of additional stock appreciation rights, many of which vested immediately.

17 EARNINGS PER SHARE

The calculation of basic earnings per share is based on the profit after taxation and comprehensive income for the year of US$18.3 million (2011: US$8.0 million) and a weighted average number of Class A and Class B shares outstanding during the period of 34,641,593 (2011: 34,655,656).

In computing the diluted earnings per share, the dilutive effect of the stock options was 811,386 (2011: 1,176,161) shares. These are added to the weighted average number of common shares outstanding during the year resulting in a diluted weighted average number of Class A and Class B shares of 35,452,979 for the year ended 31 December, 2012 (2011: 35,831,817). No adjustments were required to the reported earnings from operations in computing diluted per share amounts.

18 RELATED PARTY TRANSACTIONS

One of the non-executive Directors is a partner at a law firm. During the year, the Company incurred US$0.4 million (2011: US$0.2 million) to this firm for services provided. The transactions with this related party were made at the exchange amount. As at 31 December 2012 the Company has a total of US$ 0.2 million recorded in trade and other payables in relation to the related party. Each of the Chief Executive Officer and the Chief Financial Officer provide services to the Company through consulting agreements with personal services companies. During the year, the Company incurred fees and bonus compensation of US$0.1 million and US$0.2 million to the Chief Executive Officer and the Chief Financial Officer respectively (2011: US$0.2 million and US$ nil respectively). The full Chief Executive Officer's remuneration is included in Directors Emoluments, Note 21.

19 CONTRACTUAL OBLIGATIONS AND COMMITTED CAPITAL INVESTMENTS

CONTRACTUAL OBLIGATIONS

Protected Gas

Under the terms of the original gas agreement for the Songo Songo project ("Gas Agreement"), in the event that there is a shortfall/insufficiency in Protected Gas as a consequence of the sale of Additional Gas, the Company is liable to pay the difference between the price of Protected Gas (US$0.55/MMbtu) and the price of an alternative feedstock multiplied by the volumes of Protected Gas up to a maximum of the volume of Additional Gas sold (85.7 Bcf as at 31 December 2012). The Company did not have a shortfall during the reporting period and, supported by the work of its independent engineers, does not anticipate a shortfall arising during the term of the PSA.

Re-rating Agreement

During Q2 2011, the Company signed a re-rating agreement with TANESCO and Songas (the "Re-Rating Agreement") to increase the gas processing capacity to a maximum of 110 MMcfd (the pipeline and pressure requirements at the Ubungo power plant restrict the infrastructure capacity to a maximum of 102 MMcfd). Under the terms of the Re-rating Agreement, the Company effectively pays an additional tariff of US$0.30/mcf for sales between 70 MMcfd and 90 MMcfd and US$0.40/mcf for volumes above 90 MMcfd in addition to the tariff of US$0.59/mcf payable to Songas as set by the energy regulator, EWURA.

Under the terms of this agreement, the Company agreed to indemnify Songas for damage to its facilities caused by the re-rating, up to a maximum of US$15 million, but only to the extent that this was not already covered by indemnities from TANESCO or Songas' insurance policies. The Re-rating Agreement expired 31 December 2012 and the matter of increased capacity, whether by new or amended agreements, is currently under discussion with Songas and TANESCO. In the interim, the Company has been advised by the MEM that Songas has agreed to continue the Re-Rating Agreement until September 2013.

Portfolio Gas Sales Agreement

On 17 June 2011, a long term (to June 2023) Portfolio Gas Sales Agreement ("PGSA") was signed between the Company, TPDC and TANESCO. Under the PGSA, the Company is obligated, subject to infrastructure capacity, to sell a maximum of approximately 37 MMcfd for use in any of TANESCO's current power plants except those operated by Songas at Ubungo. The basic wellhead gas price was increased from US$2.02/mcf to US$2.70/mcf on 1 July 2012 pursuant to the terms of the contract.

Operating leases

The Company has two office rental agreements. One in Dar es Salaam which expires on 30 November 2013 at an annual rental of US$238, and one in Winchester (UK) which expires on 25 September 2022 at an annual rental of GBP 35 (US$58) per annum for the first two years and GBP71 (US$ 115) thereafter. Both are recognised in the General and Administrative expenses.

	AS AT 31 DECEMBER	
US$'000	**2012**	2011
Less than one year	**267**	222
Between one and five years	**577**	92
	844	314

CAPITAL COMMITMENTS

Italy

On 31 May 2010, the Company signed an agreement with Petroceltic International plc ("Petroceltic") to farm in on Petroceltic's Central Adriatic B.R268.RG Permit offshore Italy. The farm-in commits the Company to fund 30% of the Elsa-2 appraisal well up to a maximum of US$11.5 million to earn a 15% working interest in the permit. Thereafter, the Company will fund all future costs relating to the well and the permit in proportion to its participating interest. The Company has also agreed to pay Petroceltic fifteen per cent (15%) of the back costs in relation to the well up to a maximum of US$0.5 million.

Petroceltic was due to spud the Elsa-2 well prior to 31 October 2010, but the Italian government passed a decree, following the blowout of the Macondo well in the U.S., that prevented the drilling in the Italian seas within five nautical miles of the coastline and within 12 nautical miles around the perimeter of protected Marine Parks. In view of this, Petroceltic suspended the permit until such time as the Ministry of Environment issued a decree of environmental compatibility for the drilling program. Legislative Decree 83/2012 (the "Decree") was published on 26 June 2012 and was approved by both houses of the Italian Parliament with no substantial modifications. On 12th August, the Decree became law following publication in the Italian Official Journal. The new law modifies restrictions on offshore oil and gas exploration and production originally introduced by DLGS 128/2010 in August 2010.

The well is now expected to be drilled following finalisation of an environmental impact study currently expected in 2014. Orca will not be liable to any costs associated with the drilling of Elsa-2 until a rig contract is signed.

There are no further capital commitments in Italy.

Songo Songo commitments

Any significant additional capital expenditure in Tanzania remains dependent on TANESCO payments being brought up to date, the satisfactory conclusion of the GNT issues, conclusion of satisfactory commercial terms for the sale and transportation of incremental gas volumes, substantive progress on infrastructure expansion and the subsequent raising of finance. Currently there are no material commitments, although significant capital expenditure will be required to enable the Songo Songo field to produce 190 MMcfd in line with the anticipated infrastructure expansion.

20 CONTINGENCIES

Downstream Unbundling

In connection with the GNT negotiations and the draft Natural Gas Policy, TPDC and MEM have indicated that they wish Orca Exploration to unbundle the downstream distribution business in Tanzania. The methodology for this has been discussed with the GNT along with other issues. The Company anticipates further negotiations will be necessary before this matter is concluded.

Access to infrastructure

Ndovu Resources Limited, with support from TPDC and MEM, has indicated that they wish to tie into the gas processing plant on Songo Songo Island and sell up to 10 MMcfd from their Kiliwani North field. The Tanzania Natural Gas Infrastructure Project contemplates additional processing and transportation capacity on Songo Songo to handle these additional gas volumes. Access has not yet been granted and it is not clear when, or if, this will occur.

TPDC Back in

TPDC has indicated its wish to exercise that Company's right to 'back in' to the Songo Songo field development. The implications and workings of the 'back in' have been discussed with the GNT along with other issues. The issues are not yet fully resolved, however, and there may be the need for additional reserve and accounting modifications once these discussions are concluded. For the purpose of the reserves certification as at 31 December 2012, it was assumed that TPDC will 'back in' for 20% for all future new drilling activities and other developments and this is reflected in the Company's net reserve position.

Cost recovery

The Company's cost pool in Tanzania was recovered early in Q2 2011 resulting in a reduction in the percentage of net revenue attributable to the Company. During 2012 the level of Cost Gas increased significantly as a consequence of drilling the SS-11 well, however the cost pool was fully recovered in Q4 2012.

TPDC conducted an audit of the historic cost pool and in 2011 disputed approximately US$34 million of costs that had been allocated to the cost pool from 2002 through to 2009. The Company contends that the disputed costs were appropriately incurred on the Songo Songo project in accordance with the terms of the PSA. This matter was not resolved during the year and while the Company remains confident that the final outcome will be satisfactory, it is prepared to utilise the extensive dispute resolution mechanisms outlined in the PSA if necessary. This matter has had no impact on the results for the year.

Taxation

During the year, the Company received an assessment for additional withholding tax from the Tanzanian Revenue Authority (TRA), which together with interest and penalties totals approximately US$2.0 million. The Company considered the assessment to be without merit and appealed to the Tax Revenue Appeal Board. The Tax Revenue Appeals Board considered the appeal in March 2013 and upheld the assessment. The Company will now pursue the case with the Tax Revenue Appeal Tribunal and if necessary the Court of Appeal of Tanzania.

21 DIRECTORS AND OFFICERS EMOLUMENTS

US$'000	Year	Base	Bonus	Share based Compensation Expense	Total
Directors	**2012**	**1,655**	**510**	**402**	**2,567**
Directors	2011	924	–	–	924
Officers	**2012**	**2,060**	**470**	**750**	**3,280**
Officers	2011	1,977	580	851	3,408

The table above provides information on compensation relating to its officers and directors. Six officers and an average of four non-executive directors comprised the key management personnel during the year ended 31 December 2012 (2011: six officers and six non-executive directors).

CORPORATE INFORMATION

Board of Directors

W. David Lyons
Chairman and
Chief Executive Officer

Winchester
United Kingdom

David W. Ross
Non-Executive Director

Calgary, Alberta
Canada

William H. Smith
Non-Executive Director

Calgary, Alberta
Canada

Robert S. Wynne
Chief Financial Officer

Calgary, Alberta
Canada

Officers

W. David Lyons
Chairman and
Chief Executive Officer

Winchester
United Kingdom

Robert S. Wynne
Chief Financial Officer

Calgary, Alberta
Canada

Beer van Straten
Chief Operating Officer

Molkerum
Netherlands

Operating Office

PanAfrican Energy
Tanzania Limited

Barclays House, 5th Floor
Ohio Street, P.O. Box 80139
Dar es Salaam
Tanzania
Tel: + 255 22 2138737
Fax: + 255 22 2138938

Registered Office

Orca Exploration
Group Inc.

P.O. Box 3152
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Tortola
British Virgin Islands

Investor Relations

Robert S. Wynne
Chief Financial Officer

RSWynne@orcaexploration.com
www.orcaexploration.com

International Subsidiaries

PanAfrican Energy
Tanzania Limited

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Orca Exploration Italy Inc.

Orca Exploration Italy Onshore Inc.

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British Virgin Islands

Engineering Consultants

McDaniel & Associates
Calgary, Canada

Auditors

KPMG LLP
Calgary, Canada

Lawyers

Burnet, Duckworth
& Palmer LLP
Calgary, Canada

Transfer Agent

CIBC Mellon
Trust Company
Toronto & Montreal, Canada

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