

2011

annual
report



MADAGASCAR OIL



Strategy

Madagascar Oil Limited (the “Company” or “Madagascar Oil”) and its subsidiaries (collectively, the “Group”) have aggregated one of the largest onshore positions in a major emerging hydrocarbon province.

The Company’s focus over the near term is to demonstrate commercial production capability in its multi-billion barrel field on the Tsimiroro Block.

The Group also operates three blocks with conventional oil and gas prospects, and has an interest in a fifth block that contains a potential multi-billion barrel bitumen mining resource which is undergoing evaluation of conventional oil and gas prospects.

Over the next twelve to eighteen months, Madagascar Oil will be undertaking a number of key value changing events including:

- Completion of the installation and initiation of the steam flood pilot to test commercial production of heavy oil at the Tsimiroro field;
- Additional drilling to expand and upgrade the Tsimiroro field resource base;
- Evaluation of conventional oil and gas deposits on the Bemolanga Block, while continuing to monitor the potential for viable economic alternatives for the mining project, with its operational partner Total E&P Madagascar S.A.S. (“Total E&P”); and
- Continued work on development of drillable prospects on its three exploration blocks, subject to negotiation and approval of its 2012 work programmes by the Government of Madagascar.

The Group successfully raised an additional US\$26.5 million through a share placing in early 2012. The additional capital will be used to fund the Tsimiroro pilot project through the end of the license exploration period and to pursue the Group’s other work programmes.

The Directors believe that the potential world-class oil resource being developed by the Company in the Tsimiroro Block is well located for access to the increasing worldwide market for heavy oil in both Asia and the United States. The Group has retained a top tier team encompassing the following key characteristics:

- World-class technical expertise in executing and monetizing unconventional resources through the application of steam flood technology;
- Extensive expertise in managing, budgeting and executing multi-million US Dollar projects globally; and
- A Board with a high level of oil industry experience that is actively engaged in strategic oversight.

Madagascar Oil at a Glance

Madagascar Oil has one of the largest positions in onshore exploration and development in Madagascar, the Company's sole geographic area of focus. Madagascar Oil holds licenses in five blocks, representing an area of approximately 29,500 square kilometres (7.3 million acres). The Group has been in operation since 2004, having completed a variety of drilling and coring projects and has progressively evaluated the heavy oil and conventional oil and gas prospects on the blocks. To date, Madagascar Oil has invested in excess of \$230 million, more than any other company in Madagascar's oil sector, and is actively working with the country of Madagascar to realise the development of its oil resources:

Block Name	PSC	Operator	MOL Interest	Status	License Area (km2)
Tsimiroro	3104	Madagascar Oil	100%	Exploration/ Appraisal	6,670
Bemolanga	3102	Total E&P	40%	Exploration/ Appraisal	5,463
Manambolo	3105	Madagascar Oil	100%	Exploration	3,995
Morondava	3106	Madagascar Oil	100%	Exploration	6,825
Manandaza	3107	Madagascar Oil	100%	Exploration	6,580

The Company conducted key exploratory operations on Tsimiroro and Bemolanga in 2011 and, since June 2011, is proceeding on schedule with its work programme for the initiation of production from the Tsimiroro steam flood pilot at the end of 2012. The Company continues to pursue the necessary approvals to restart work on its three exploration blocks.

The political situation in Madagascar continues to weigh on the country's oil and gas industry. The country's political factions continue to try to find a way to work together toward realising the roadmap for legitimate elections as originally mandated by The Southern African Development Committee ("SADC"), and operations on the Company's three exploration blocks have been stalled pending resolution of these issues. Currently, the outstanding claims of force majeure by the Company's subsidiary remain in effect. Please see the Chairman/CEO Statement and Note 33 to the Company's financial statements, each of which is included in this Annual Report, for further discussion of these matters.



TSIMIRORO FIELD OIL-IN-PLACE ESTIMATES

Independent reserve analysts Netherland, Sewell & Associates, Inc. ("NSAI") reviewed the work accomplished in the field in 2010 and in September 2011 issued a new estimate of the oil-in-place volumes for the Tsimiroro field. The new figures indicate a Best Estimate of Contingent in-place resources of approximately 1.7 billion barrels (a 75% increase from the prior 2009 analysis), plus an additional 2.2 billion barrels of Best Estimate Prospective in-place resources (a 178% increase). The new estimates of oil-in-place are as follows:

OIP Resources (mm bbl)	Low Estimate	Best Estimate	High Estimate
Contingent	1,100	1,688	2,459
Prospective	991	2,189	6,872

This increase in Contingent resource estimate by NSAI also provides a potential Best Estimate recoverable volume of 1.1 billion barrels utilizing the 70% recovery factor estimated by NSAI for a steam flood development. Inclusion of the Prospective volume increases the estimate for recovery to 2.6 billion barrels and ranks Tsimiroro among the largest heavy oil fields in the world with a potential peak production rate of 300,000 bopd and a projected field life in excess of 50 years.



Chairman / CEO Statement

2011 was ultimately a year of great progress for Madagascar Oil, with the Company continuing to develop our principal asset, the Tsimiroro field in Madagascar.

Tsimiroro will continue to occupy our operational focus in the near term, and we were delighted when Netherland, Sewell & Associates recently revised upwards the Best Estimate Contingent oil-in-place number for the block by 75% to 1.7 billion barrels. This further reinforces our view that Tsimiroro is a truly world class asset, and with our work programme for 2012 having been approved by the Government we now expect first oil production from the Tsimiroro steam flood pilot project in the fourth quarter of 2012. We are currently installing the relevant infrastructure to achieve this goal, and have commenced drilling our 28 pilot wells.

We were very pleased to update the market with news of a successful share placing in February 2012, in which we raised gross proceeds of approximately US\$26.5 million. This significant strengthening of our balance sheet affords us the ability to maximise the effectiveness of our work programmes in Madagascar and continue to invest in the communities in which we operate. In particular, the Company can extend the testing phase of the Tsimiroro steam flood pilot through August 2014, conduct additional development drilling, and undertake a Fugro Airborne Gravity Gradiometry ("AGG") survey, as well as acquire additional seismic on our Exploration Blocks.

At Bemolanga we were granted a modification of our work programme to shift the focus to exploration activity for one year, with an option to extend further this exploration phase by two years. In partnership with Total E&P, the work programme is now focused on the block's conventional hydrocarbon potential and we are currently processing data obtained from an 8,400km AGG survey. This cutting edge technology will allow us to understand better the field's deeper oil and gas potential. We intend to fund our initial cash requirements for the Bemolanga project with the \$6 million gross carry, which remains under the terms of our agreement with Total E&P as of the end of 2011.

Before we look ahead to 2012, I want to briefly mention our status with the Government of Madagascar. The Company spent the first half of 2011 clarifying its ownership position with the Government so as to establish its right to proceed with operations under its production sharing contracts. The dispute over Tsimiroro was resolved in June 2011, with the Government of Madagascar acknowledging the validity of the Tsimiroro production sharing contract and approving the 2011-2012 budget. Trading in the Company's shares on AIM recommenced in June 2011 following an approximate six month suspension.

Throughout the process we were both co-operative and confident in achieving a favourable resolution to this matter. We engaged in a constructive dialogue with the Government of Madagascar and we were able to reach a solution on Tsimiroro by evidencing compliance with our contracts, demonstrating the amount of work that has been completed to date, and laying out clear plans for the future. While this was a difficult period in the Company's short history as a publicly listed company, we were always confident that our work exceeded the requirements in the agreements that we had signed, and that the rule of law would ultimately prevail. The Company's three Exploration Blocks are still awaiting the necessary approvals to restart operations. We continue to carry on discussions with the regulator to resolve the governmental delays on these blocks; however, there remains some lack of clarity over the oversight of the country's oil and gas operators following the current reorganisation within the Government following the October 2011 signing of the Southern African Development Community ("SADC") roadmap. Management believes that the Group will ultimately resolve the delays around the Exploration Blocks.

As mentioned in our December 2011 Annual General Meeting update, we continue to challenge the Madagascar Tax Administration's request for taxes on foreign services. We resolved the portion of the dispute related to income tax in our favour and continue to work through the appeals process on the request for VAT on foreign services.

Looking ahead to 2012, notwithstanding the general political uncertainties in Madagascar, the Company can move forward with confidence now that a particularly turbulent period has passed. It is the Directors' belief that we have the operational team in place to realise the considerable value contained in our assets. We will continue to engage actively with our regulator and partner L'Office Des Mines Nationales et Des Industries Strategiques ("OMNIS"), with robust plans to build on the progress achieved last year at Tsimiroro and resolve the governmental delays in our exploration block operations. These efforts in turn will help continue to de-risk our assets, and give investors confidence.

We should also note that in conjunction with our increase in operations, we are ramping up implementation of a significant corporate social responsibility programme to increase our investment in the people and communities of Madagascar. This programme will further complement and build on our existing public and social works from which the country and its people are already receiving the clear benefits. To assist us in this effort, we have formed a relationship with the Forum for Former African heads of State and Government (www.africaforum.org), a non-governmental organisation designed to support the advancement of African development. We take our responsibilities seriously in this regard, and we will continue to commit to be a key participant in the future of Madagascar and its people.

On behalf of the Board, I would like to take this opportunity to thank our investors and employees for their continued support. After a challenging year, we are poised to see first oil production in Madagascar in 2012. This will be an historic event in that it will represent the first sustained production in the country. We are delighted to be working with the Government to play a significant role in this potentially world-class development.

J. Laurie Hunter

*Chairman of the Board and
Chief Executive Officer*



Operational Review

TSIMIRORO – BLOCK 3104

The Tsimiroro Block comprises 6,670 square kilometres, of which the northern portion comprises the approximate 1,600 square kilometre Tsimiroro heavy oil field. The field has a current Best Estimate Contingent oil-in-place volume, within the Amboloando sand, of 1.7 billion barrels with an average 14o API oil and an estimated recoverable volume of 1.1 billion barrels.

The results from the 2010 work programme were analysed by NSAI and the oil-in-place volumes were increased by 75% for Contingent resources and 178% for the Prospective resources. The 24 well delineation drilling programme, which found 18 wells with good oil shows, and the Electrical Resistivity Tomography data combined to increase the confidence level of oil-in-place estimates and better define the area of coverage of the reservoir areas in the Amboloando sand. The 2010 programme also found a potential new extension to the field to the south that appears to be a development in the slightly deeper Isalo sand.

Construction of the Tsimiroro nine pattern steam flood pilot project began in 2011. The location preparation for the wells and facilities was 98% completed and drilling commenced on the 28 pilot wells in early January 2012. All engineering and design work, which recommenced in July 2011 following resolution of the uncertainties surrounding the block and approval of the work programme by OMNIS, is moving ahead at a good pace for implementation of our steam flood project plans.

The steam flood pilot will test the application of both cyclic and continuous injection of steam in a vertical steam flood configuration. It is presently projected that cyclic steam injection will begin on the producers and injectors in Q3 2012 and continuous steam injection will commence at the end of Q4 2012. The decision to move ahead with commercial development is expected to be made prior to completion of the exploration phase of the production sharing contract ("PSC") in mid-2014.

Current projections for a full field development now indicate that the Best Case Contingent resource will yield a 150,000 barrel per day peak oil rate in approximately 10 years from the start of commercial operations. Full field development and expansion will take approximately 30 years and production will remain economic for over 50 years. In the cases where the Prospective resources are also considered, the peak production is estimated at 300,000 barrels per day and the field life is also calculated to be in excess of 50 years.

In an effort to continue to refine the resource estimates, an additional 13 delineation wells were drilled in 2011 and 12 of those wells showed good Amboloando sand development. These results will be incorporated into the resource analysis in the next few months. The Company also conducted a 10,000 square kilometre Airborne Gravity Gradiometry ("AGG" and also known as Full Tensor Gravity) survey over the entire Tsimiroro Block. We expect that this survey will assist us in defining the boundaries on the shallow oil deposits, however, the survey output should also highlight any potential deeper prospects on this block. We expect to complete this survey analysis during the second quarter of 2012.

BEMOLANGA – BLOCK 3102

The Bemolanga Block is a 5,463 square kilometre area and contains the oldest known hydrocarbon deposit in Madagascar. The first wells were drilled on the Bemolanga Block in the late 1800s and work has been conducted over the area of what has been determined to be a potential bitumen mining project. The Block is operated by Total E&P which holds a 60% working interest with the remaining 40% interest held by Madagascar Oil. Bemolanga contains multi-billion barrel Petroleum–Initially-in-Place volumes of bitumen, which was the original focus of the activities on the block. Detailed evaluation by Total E&P and Madagascar Oil indicates the projected recovery will not support proceeding with the mine project at the present time. The mine will continue to be evaluated for potential improvements in extraction and upgrading technology that would improve the economics.

In June 2011 Total E&P and Madagascar Oil received approval from OMNIS for a modification of the Bemolanga work programme to focus on deeper conventional plays on the block. An extension to the exploration phase of the PSC of one year was granted in June 2011, with the commitment to run an AGG survey over the entire block area to identify possible conventional hydrocarbon plays, followed by an option for a further two-year extension to drill a well. This airborne survey of 8,000 square kilometres was conducted in the third quarter 2011 and the results are currently being evaluated.

Approximately \$4 million was spent on the Bemolanga project in 2011, and Madagascar Oil's 40% share of the costs was carried by Total E&P as part of the farm-in transaction. Under the terms of the Joint Operating Agreement with Total E&P, the Company will be carried on the next \$6 million of gross expenditures for the revised work programme, which is expected to extend through to the end of 2012.

MANAMBOLO – BLOCK 3105 / MORONDAVA – BLOCK 3106 / MANANDAZA – BLOCK 3107

These three blocks, referenced collectively as the “Exploration Blocks”, comprise areas of 3,995, 6,825 and 6,580 square kilometres respectively. Madagascar Oil followed up on the successful 2009 seismic acquisition programme by running GORE® Sorber geochemical testing over nine structural leads in seven areas on the three blocks in 2010. The GORE micro-seepage testing indicated the presence of hydrocarbon signature on five of the leads. The GORE process is conducted by installing sampling modules in a grid on the surface above an identified subsurface structural feature, to determine which areas above the structures have micro-seepage of hydrocarbon at readings above the normal background level.

The northern lead at Manambolo (Block 3105) did not indicate elevated hydrocarbon; however, the southern lead contained several areas reflecting elevated hydrocarbon signature. These accumulations currently lack the seismic definition necessary to determine fully the structural continuity, but the micro-seeps suggest that hydrocarbons may be contained in shallower channel sands rather than the structural feature originally identified in the seismic analysis.

Similarly, Morondava (Block 3106) leads in the north of the block indicate very little data suggesting hydrocarbon presence, however the southerly 160 square kilometre area indicated two or three areas of elevated hydrocarbon that do not conform to the shape of the structural high mapped below the survey area. These hydrocarbon readings may also correlate to channel sands in a slightly shallower horizon like those seen on Block 3105.

On both Block 3105 and 3106, there is a need for a more comprehensive survey to tie the data together. Madagascar Oil is proposing to run AGG surveys over these leads in 2012. Preliminary plans for this activity have been reviewed and agreed to by the OMNIS technical team. Commencement of work will depend on approval by the Management Committee. It is also expected that the acquisition of additional seismic will be required in the following year to obtain a more complete assessment.

There were three structural areas sampled with GORE on Manandaza (Block 3107). All three leads generated strong signs of elevated hydrocarbon, with the largest most northerly area being the site of the 1991 Manandaza #1 well that recovered 10 barrels of 41o API light oil on a drill stem test. The Company anticipates undertaking an AGG survey on this area followed by the acquisition of additional seismic to clarify the nature of the accumulation.

Work on these blocks was halted in December 2010 and plans for future work have been formulated in anticipation of the requisite approvals being granted by the Government of Madagascar and OMNIS. The date for the Management Committee Meeting has not yet been set and the blocks remain under force majeure pending a renegotiation of the work requirements and timing. Each of these three Exploration Block PSCs will require modifications to the work programme to allow for the planned airborne surveys and the necessary additional seismic work. These will then be followed by an election to proceed with drilling leads on each block. All of the prior results and future block plans have been reviewed and discussed at Technical Committee Meetings with OMNIS, and full agreement has been reached on the need for a combination of AGG surveys and the acquisition of additional seismic to further define and de-risk any potential drilling prospects.

Corporate Social Responsibility Programme

The Company has an active corporate social responsibility programme (“CSR”) which has demonstrated over the past five years of Company operation in Madagascar our firm commitment to supporting the communities adjacent to our areas of operation. At the core of our CSR is our conviction that we must work together with the country of Madagascar, and specifically with each of the communities, to effectively support key projects and build important infrastructures that contribute to the economic and social well-being of the people of Madagascar.

In 2011, the Board of Directors resolved to strengthen our CSR activities and resources. In so doing, the Company designated the Chief Executive Officer, in conjunction with the Group’s in-country Deputy General Manager, to lead the Company’s CSR strategy as a crucial component of our business activity, fully recognising that our business success will be profoundly linked to the long term societal progress of the country. The Company has clearly demonstrated its commitment to managing this programme by regularly consulting with the appropriate local and national stakeholders to agree fully on programmes which target the highest priority objectives and deliver meaningful and sustainable development projects. These efforts include focus on education, health and economic developments that promote self-sufficiency and serve to raise the standard of living in our area of operations.

The Company has formed a relationship with the Forum for Former African heads of State and Government (“The Africa Forum”) to engage fully their experience and guidance in most effectively meeting our CSR objectives. The African Forum is a non-governmental organisation designed to support the implementation of the broad objectives of the Africa Union. The group was established in 2006 with the purpose of harnessing the experience, moral authority and good offices of former heads of state to advance African development, particularly the promotion of sustainable peace and security, the enhancement and sustenance of democratic governance in Africa and promotion of human rights. The Africa Forum is currently providing consulting services and guidance on the Company’s many CSR opportunities.

Financial Review

LOSS FOR THE FINANCIAL YEAR

The net loss for the year ended 31 December 2011 was \$13.2 million. This compares to a loss of \$11.6 million in 2010, taking account of \$2.8 million of expensed costs associated with the Company's admission to trading on the AIM Market of the London Stock Exchange Plc.

Administrative costs, summarised in the table below, totaled \$12.5 million (2010: \$7.2 million). Employees and headcount-related contractor payments were \$7.2 million (2010: \$3.5 million), including \$3.1 million (2010: \$1.3 million) of IFRS charges related to restricted stock and share options granted to directors, staff and third parties. Production sharing contract-related fees and expenses were \$1.1 million (2010: \$1.1 million). Depreciation, costs of admission to trading on the AIM Market and losses associated with foreign currency exchange, asset disposal and impairments are not included in administrative costs listed below.

Administrative Costs	2011 (US\$ Millions)	2010 (US\$ Millions)
Employee and equivalent contractors	\$4.1	\$2.2
Share based payments	\$3.1	\$1.3
Total employee and headcount – equivalent contractor payments	\$7.2	\$3.5
Production sharing contract - related fees and expenses	\$1.1	\$1.1
Other	\$4.2	\$2.6
Total administrative costs	\$12.5	\$7.2

STATEMENT OF FINANCIAL POSITION

At 31 December 2011 the Group had net assets of \$167 million (2010: \$174 million). The most significant balances are property, plant and equipment of \$14.6 million (2010: \$15.1 million), exploration and evaluation assets of \$104.0 million (2010: \$85.8 million) and cash of \$43.0 million, including restricted cash of \$2.6 million (2010: \$69.2 million, including restricted cash of \$1.8 million).

CAPITAL EXPENDITURES

The Company incurred exploration and evaluation related capital expenditures of \$16.8 million in 2011. This compares to \$12.4 million in capital expenditures in 2010. The Company focused its capital expenditures as follows:

Capital Expenditures	2011 (US\$ Millions)
Airborne Gravity (AGG) and Electrical Resistivity Tomography (ERT) surveys on Tsimiroro	\$2.8
Tsimiroro exploration well drilling	\$2.1
Tsimiroro steam flood pilot	\$11.7
Exploration block prospect testing (GORE)	\$0.2
Total	\$16.8

CASH FLOW

The Group ended the year with \$40.5 million of unrestricted cash and cash equivalents (2010: \$67.5 million) and a further \$2.6 million of restricted cash (2010: \$1.8 million). The Group remains debt free, other than trade payables and accrued expenses in the ordinary course of business, which ended the year at \$5.4 million (2010: \$2.8 million).

The Group's restricted cash at 31 December 2011 supports \$1.5 million of performance guarantees in favor of the Government of Madagascar under the Group's PSCs for Blocks 3105, 3106, and 3107. The guarantees must be renewed through 31 December 2012, which is the end of the current phase of each license. In 2011 the Group set aside \$0.8 million in a restricted account in order to continue the appeals process on disputed VAT payments on foreign services.

Madagascar Oil has diversified its cash holdings amongst several significant financial institutions in 2011. At 31 December 2011, approximately \$15.8 million was held on deposit with Credit Suisse, \$9.8 million was held on deposit with HSBC, and \$16.5 million was held on deposit with Chase. At 31 December 2011, over 95% of the Group's cash was held in US dollars.

The Company's common shares par value US\$0.001 per share (the "Common Shares") trade on the AIM market of the London Stock Exchange through depository interests under the symbol "MOIL". At 31 December 2011, the Company's total outstanding share capital was 192,368,467 shares (excluding 4.3 million restricted shares).

Board of Directors

JOHN LAURIE HUNTER | *Chairman and Chief Executive Officer*

Laurie Hunter, aged 65, has been a director of Madagascar Oil since October 2008, and became CEO in July 2009. Mr. Hunter has served on the board of a number of private North American based E & P companies and has been both a limited and a general partner of a number of private drilling partnerships in the United States. In addition, Mr. Hunter is currently an independent director of Living Cell Technologies Limited (ASX-LCT), a New Zealand based biotechnology company. Mr. Hunter holds an MA in Politics, Philosophy and Economics from Oxford University.

MARK FIELD WELLER | *Chief Operating Officer*

Mark Weller, aged 61, has been with the Company since 2008. He has over 40 years of oil industry experience with an extensive background in domestic and international oil and gas development (both onshore and offshore drilling and production operations), including 15 years direct involvement with the design, initiation and operation of heavy oil steam flood projects in California. Mr. Weller has previously worked with Texaco and Getty Oil in a variety of positions throughout the United States and worked internationally developing projects in West Africa. Mr. Weller has a Bachelor's degree in Mechanical Engineering from the University of California, Davis.

ANDREW JAMES MORRIS | *Non-Executive Director*

Andrew Morris, aged 43, has extensive international business experience and sits on the board of several companies, ranging from early stage resource companies to emerging technology companies. He was founder of Persistency Capital, a private investment company, where he has acted as both investor in, and adviser to, companies across a broad range of sectors and geographies. He became a director of Madagascar Oil in October 2008 and his other current directorships include serving as Executive Chairman of Blake Oil and Gas Limited, which has operations in the country of Georgia, Chairman of Kriisa Research Inc, a venture stage alternative energy company, Director of Southwest Energy Ltd, an oil and gas exploration company in Ethiopia, and Director of Falcon Oil and Gas Ltd, a TSXV listed company with assets in Hungary, Australia and South Africa. Previously, Mr. Morris spent 15 years in the financial services industry, including being a Director of Ernst & Young in London where he advised a broad range of organizations on Enterprise Risk Management including advice on corporate governance, management reporting, financial control, operational risk and process improvement. Mr. Morris holds a BSc (Hons.) degree in Mathematics from Bristol University and is a member of the Institute of Chartered Accountants in England and Wales.

IAN COLIN ORR-EWING | *Non-Executive Director*

Ian Colin Orr-Ewing, aged 70, is a natural resources consultant for Blakeney Management, a fund management company specializing in advising on investment in Africa and the Middle East, with whom he has been associated since 1994. He has over 40 years of oil industry experience with an extensive background in domestic and international oil and gas development, including both onshore and offshore drilling and production operations. Mr. Orr-Ewing has served on the boards of several oil companies, including Stratic Energy Corporation (a Canadian oil company), and is currently on the board of Vatukoula Gold Mines Plc (formerly River Diamonds, a Fijian Gold Mining company), which is listed on AIM and Bacanora Minerals (a TSX quoted company). Mr. Orr-Ewing has a Bachelor's degree in Geography from Oxford University.

IAN CHRISTOPHER SIMON BARBY | *Non-Executive Director*

Ian Barby, aged 67, practised as a Barrister before joining Warburg Investment Management Ltd in 1985, subsequently becoming a vice chairman of Mercury Asset Management plc and latterly, until 2003, a managing director of Merrill Lynch Investment Managers. He is currently chairman of Invesco Perpetual UK Smaller Companies Investment Trust plc and Ecofin Water and Power Opportunities plc, as well as being a director of BlackRock World Mining Trust plc, Schroder Income and Growth Fund plc, Pantheon International Participations plc and SR Europe Investment Trust plc. Mr. Barby holds an M.A. in History & Law from Cambridge University.

JOHN ALEXANDER VAN DER WELLE | *Non-Executive Director*

John van der Welle, aged 56, was a director and Chief Financial Officer of Canadian and AIM listed Stratic Energy Corporation until November 2010. Mr. van der Welle is currently a consultant acting for a number of upstream companies, and is a non-executive director of Groundstar Resources Limited (a Canadian listed oil company). He has extensive senior business and financial experience in the oil industry. Prior to joining Stratic Energy Corporation he was managing director and Head of Oil & Gas at the Royal Bank of Scotland. After qualification as a chartered accountant at Arthur Andersen & Co., Mr. van der Welle joined UK listed Enterprise Oil plc in 1984. He had a number of business development and finance roles there, and was Group Treasurer from 1993 until 1995 following which he joined UK listed Hardy Oil and Gas plc as Finance Director. He subsequently became Finance Director of UK listed Premier Oil plc, and then a director and Chief Financial Officer of First Calgary Petroleum Ltd (a Canadian listed oil company). Mr. van der Welle holds a BSc (Hons) degree in Electronic Engineering from Southampton University, and is a member of the Institute of Chartered Accountants in England and Wales, the Association of Corporate Treasurers and the Chartered Taxation Institute.

The Directors review the composition of the Board on a regular basis and intend to appoint additional executive and/or independent non-executive directors at appropriate stages of the Company's development.

Corporate Management

SETH FAGELMAN | *Chief Financial Officer*

Seth Fagelman has served as the Company's Chief Financial Officer since December 2009. He has significant financial and business experience, having previously held CFO and senior management positions for CyrusOne, Prime Cable and GW Communications. He currently serves as a strategic adviser and board member to several private companies. Mr. Fagelman has helped raise over US\$1.7 billion in debt and equity capital to finance acquisitions and growth in the telecommunications, technology, manufacturing and distribution sectors. Mr. Fagelman graduated with an MBA from the University of Texas, Austin.

GIL MELMAN | *General Counsel*

Gil Melman became the General Counsel of the Company in March 2011. From August 2008 through February 2011, Mr. Melman was seconded to the Company to act as general counsel. During that time, Mr. Melman was a partner at Selman, Munson & Lerner P.C., a Texas based law firm specializing in corporate transactional work. Prior to joining Selman, Munson & Lerner P.C., Mr. Melman was employed as Vice President of Legal at a regional private equity fund and also as Vice President and Assistant General Counsel at a large Fortune 100 energy company. Mr. Melman began his career at Vinson & Elkins LLP, as a lawyer in its Corporate & Securities Group. Mr. Melman obtained his Bachelors of Business Administration and his Juris Doctor Degrees from the University of Texas, Austin.

Operations Management

ALVARO KEMPOWSKY | *General Manager – Madagascar*

Alvaro Kempowsky is the General Manager of Madagascar Oil SA, having joined from Chevron Corporation in early 2007. Mr. Kempowsky spent much of his career as a Project and Operations Manager with Texaco in Colombia and Angola, including responsibility for, inter alia, operations and construction of heavy oil, light oil and natural gas developments. In addition, Mr. Kempowsky spent 14 years as the project manager for a new heavy oil steam project in Columbia for Texaco and Ominex. Mr. Kempowsky has a M.E. in Petroleum Engineering and an M.E. in Engineering Management from the University of Tulsa, Oklahoma. He also has a degree in Electrical Engineering from the National University of Colombia.

DR. EMMA RALIJOHN | *Deputy General Manager – Madagascar*

Dr. Emma Ralijohn is Deputy General Manager of Madagascar Oil SA, having joined in 2007, and is primarily responsible for working with government authorities for contract and environmental requirements. She has been a faculty member for a leading Business School in Madagascar since 1991. She led her country in obtaining the first ever signed Compact with the USA-funded Millennium Challenge Account (MCA) in 2005 when she worked as Finance Adviser to the President of Madagascar. She was named CEO of the entity set up to manage the US\$110 million fund from MCA. She also served as a Director in the Banking and Financial Supervision Board of the Madagascar Central Bank since 2005. She is the President of Upstream Oil Companies Association and a founding member of the American Chamber of Commerce in Madagascar. Dr. Ralijohn has a Ph.D. in Finance and a Doctorat ès Sciences de Gestion in Strategic Management.

JIM LEDERHOS P.E. | *Chief Engineer*

Jim Lederhos is Chief Engineer for the Company, having joined in 2008 from Chevron, where, over a 27 year career, he was involved in all aspects of steam flood design and evaluation of heavy oil projects worldwide, including California and Indonesia. Mr. Lederhos has co-ordinated all aspects of the Tsimiroro Field project design and evaluation for thermal testing. He has also served as a consultant for several heavy oil projects worldwide in the last several years. Mr. Lederhos has B.S. degrees in Engineering and Geology from Oregon State University in Corvallis, Oregon.

The Group currently has approximately 101 employees and consultants in total. The majority of personnel are engaged on a contractual basis.

Corporate Governance Statement

The Directors recognise the importance of sound corporate governance commensurate with the size and nature of the Company and the interests of its shareholders. The UK Corporate Governance Code does not apply to companies quoted on AIM and there is no formal alternative for AIM listed companies. The Directors have implemented steps to comply with the UK Corporate Governance Code, so far as it is considered practicable, having regard to the size and current stage of development of the Company. The Quoted Companies Alliance has published a set of corporate governance guidelines for AIM companies, which include a code of best practice for AIM companies, comprising principles intended as a minimum standard, and recommendations for reporting corporate governance matters. The Board considers the Quoted Companies Alliance guidelines when implementing corporate governance policies and internal controls.

Set out below is a description of the Company's corporate governance practices.

THE BOARD

The Board consists of two executive directors and four non-executive directors. In connection with its admission, the Company implemented staggered terms for members of the Board of Directors. Each director serves for a term of three years and there are three classes of directors. Only one class is up for re-election at any given annual general meeting. The Company has populated its Board with directors who either have a depth of experience and/or extensive knowledge in the international oil and gas industry, or who provide expertise in a specific discipline such as finance and accounting. The directors and their biographies are set out on pages 12 and 13 of this Annual Report.

The Board meets regularly and is responsible for setting strategy, monitoring operational and financial performance and reporting, approval of annual budgets for capital, operating and other expenditure and their financing, material transactions, the framework of internal controls and business risk assessment.

The Board also plays a supervisory role in the Company's recent dispute with the Government of Madagascar over its PSCs. Management provides the Board with regular updates on the status of this matter, and schedules meetings of the Board as necessary to allow the Board to provide advice and direction to management in addressing the dispute.

In December 2011, the Board of Directors established the role of senior independent director ("SID") to address certain corporate governance issues that may arise as a result of the Company's combination of the roles of Chairman of the Board of Directors and Chief Executive Officer. The SID acts as a sounding board for the Chairman and Chief Executive Officer. He also serves as an intermediary between the Chairman and Chief Executive Officer and the other directors as needed, and is available to act as a channel of communication for the Company's shareholders and financial brokers where communication with the Chairman and Chief Executive Officer has failed to resolve concerns. Mr. John van der Welle has been appointed to serve as the SID.

The Board has established Audit, Remuneration and Nominations Committees as follows:

AUDIT COMMITTEE

The Audit Committee is comprised of John van der Welle (chairman), Andrew J. Morris and Colin Orr-Ewing. Reporting to the Board, it has primary responsibility for monitoring the quality of internal controls and ensuring that the financial performance of the Group is properly measured and reported on. In addition, it receives and reviews reports from the Company's management and auditors. The Audit Committee meets at least three times a year and has unrestricted access to the Company's auditors, with whom it actively liaises. Meetings of the Audit Committee are attended by members of senior management as and when required.

REMUNERATION COMMITTEE

The Remuneration Committee is comprised of Ian Barby (chairman), Colin Orr-Ewing and John van der Welle and, amongst other things, makes recommendations to the Board on matters relating to the remuneration of the executive directors. The Remuneration Committee reviews the performance of the executive directors and advises on salary, bonus and incentive remuneration for other employees as directed by the Board. In addition, it makes recommendations to the Board on proposals for the granting of share options and other equity incentives pursuant to any share option scheme or equity incentive scheme in operation from time to time. The Remuneration Committee meets at least twice a year. Directors of the Company do not participate in recommendations of the Remuneration Committee regarding their own remuneration. See the Remuneration Committee Statement set out on page 20 of this Annual Report.

NOMINATIONS COMMITTEE

The Nominations Committee was established in December 2011 to enable the Board to delegate its responsibility for nomination of directors. The terms of reference for the Nominations Committee provide for at least three non-executive directors to serve. The Nominations Committee shall meet at least once per year. Generally the Nominations Committee is responsible for identifying and nominating for the approval of the Board candidates to fill vacancies in the Board when they arise.

The Nominations Committee is comprised of Mr. Ian Barby (chairman), Mr. Andrew Morris and Mr. John van der Welle.

The Directors do not consider that, given the small size of the Board and its active involvement in the governance of the Company, it is appropriate to delegate matters of corporate governance to a Corporate Governance Committee. The appropriateness of such a committee will however, be kept under a regular review by the Board.

INTERNAL CONTROL

The Board is responsible for establishing, maintaining and monitoring the Company's system of internal control, and importance is placed on maintaining a robust control environment to the extent practicable given the Company's size and resources. Although no system of internal control can provide absolute assurance against material misstatement or loss, the Company's system is designed to provide the Directors with reasonable assurance that problems are identified on a timely basis and dealt with appropriately. The Board maintains a financial reporting procedure manual that is monitored by the Audit Committee and the Company's financial management. The Company has implemented a Board approved detailed delegation of authority to management covering purchasing, invoice approval and payments. This delegation is reviewed periodically to determine if changes are necessary.

To enable the Board to discharge its duties, all of the directors receive timely information from the Company's management.

The key procedures which the Board has established with a view to providing effective internal financial control include the following:

- The Board meets regularly to discuss all material issues affecting the Company;
- The Board has adopted and reviewed a comprehensive annual budget for the Company. Monthly results are examined against the budget and deviations are monitored closely by the Board;
- The Company has instituted and continues to develop a monthly management reporting process to enable the Board to monitor the performance of the Company;
- The Board is responsible for identifying major business risks faced by the Company and for determining the appropriate courses of action to manage those risks; and
- Fully consolidated management information is prepared on a regular basis, at least half yearly.

No significant control deficiencies have come to light during the year and no weaknesses in internal financial control have resulted in any material losses, contingencies or uncertainties which would require disclosure as recommended by the guidance for directors on reporting on internal financial control. The effectiveness of the system of internal financial control operated by the Company is subject to regular review by the Board and Audit Committee in light of the future growth and development of the Company.

The Board considers that in view of the nature and size of the Company at present it would not be appropriate to establish a separate internal audit function. The Audit Committee will continue to review this decision and make recommendations to the Board on this matter annually.

BUSINESS RISKS MANAGEMENT

The Board regularly reviews the effectiveness of the systems of internal control and considers the major business risks and the control environment. The Company maintains a business risk management policy that is periodically updated based on recommendations from the Audit Committee and senior management. Management is responsible for routinely identifying and evaluating risks.

The Company recognises that the effective management of business risk is critical to the success of the Company. Accordingly, the Company's approach to risk management embodies the following principles:

- Risk management is embedded in all management systems and business processes and is an integral part of the Company's internal control processes;
- The identification and management of risk is not limited to just the Board of Directors, but includes all managers and staff throughout the Company;
- The development by the Board of a comprehensive risk management framework which senior executives are in the process of implementing to ensure that risks are being managed in an efficient, effective, and economic manner. The framework includes risk management standards and risk assessment criteria; and
- The Board is responsible for identifying major business risks faced by the Company and for determining the appropriate courses of action to manage those risks; and
- The Audit Committee reviews the effectiveness of risk management systems and internal controls regularly, and the results are communicated to the Board of Directors.

The Company is exposed to a range of technical, geological, operational, political, environmental, health and safety and financial risks in the conduct of its operations. Key areas include: (a) risks related to Madagascar, specifically political instability, natural disaster and emerging markets risks, governmental delays and expropriation risks; (b) general business risks such as risk of inability to obtain future financing, tax risks and insurance coverage issues; (c) operational risks, such as technical difficulties, weather, risks associated with estimation of hydrocarbons, uncertainty surrounding labor and equipment; volatility in oil and gas prices and health and safety issues; and (d) risks associated with the common shares, such as price volatility and illiquidity, risks of holding depository interests and risks associated with Bermuda law. The risks set out above are not exhaustive and there may be additional risks and uncertainties not presently known by the Company.

THE SHARE DEALING CODE

The Company has adopted a Share Dealing Code for the Directors and employees (as well as certain affiliates and relatives of such persons) that is appropriate for a company whose shares are admitted to trading on AIM (in order to, among other things, ensure compliance with Rule 21 of the AIM Rules).

The Company takes all reasonable steps to ensure compliance with the terms of the Share Dealing Code by the Directors and all other relevant persons.

RELATIONS WITH SHAREHOLDERS

The Chairman and Chief Executive Officer, the Chief Operating Officer and the Chief Financial Officer are the Company's principal spokesmen with investors, analysts, the press and other interested parties. The Senior Independent Director also provides an alternative channel of communication available to shareholders when appropriate. Communications with shareholders are given high priority and there is regular dialogue with institutional investors, as well as general presentations to analysts at the time of the release of the annual and interim results. The Company maintains a website for the purposes of improving information flow to shareholders as well as potential investors. It contains all press releases, reports and accounts and extensive information about the Company's activities. Enquiries from individual shareholders on matters relating to the Company are welcomed. Shareholders are also encouraged to attend the Annual General Meeting at which they are given the opportunity to put questions to the Chairman and Chief Executive Officer and other members of the Board.

The Company intends to hold its next Annual General Meeting in the fourth quarter of 2012.



Remuneration Committee Statement

The This report was prepared by the Remuneration Committee of the Company's Board of Directors and has been approved by the Board. This report addresses the activities of the Remuneration Committee during 2011.

COMPOSITION

The terms of reference of the Remuneration Committee provide for the Remuneration Committee to be composed of at least three non-executive directors. Members of the Remuneration Committee are appointed for a three year term.

The Remuneration Committee currently consists of Mr. Ian Barby (who serves as its chairman), Mr. Colin Orr-Ewing and Mr. John van der Welle. Each is a non-executive director.

The Company's Chairman and Chief Executive Officer is invited to attend the meetings of the Remuneration Committee and the Assistant Secretary of the Board of Directors acts as its secretary, although none are present or involved when his own remuneration is discussed. From time to time the Chief Operating Officer is also invited to attend to provide insight into the compensation levels of other employees.

RESPONSIBILITIES

The Remuneration Committee is responsible for recommending and monitoring the remuneration levels for executive directors and senior executives of the Company, including levels of equity incentive compensation. The role of the Remuneration Committee is advisory in nature. As such, it makes recommendations to the Board on matters within the scope of its authority for ultimate approval by the Board.

- (a) The Remuneration Committee's responsibilities include, among other things:
- (b) determining and agreeing with the Board the framework or broad policy for the remuneration of the Company's Chairman and Chief Executive Officer, Chief Operating Officer, the executive directors, the company secretary and such other members of the executive management of the Company as it is designated to consider;
- (c) determining the total individual remuneration package of each executive director and other senior executives including bonuses, incentive payments, share options, restricted shares and other share awards;
- (d) reviewing the on-going appropriateness and relevance of the remuneration policy;
- (e) administering and designing performance related pay schemes, including share incentive plans and approving payments or awards under such schemes.

- (f) overseeing any major changes in employee benefits structures;
- (g) vetting, authorising and agreeing the policy for authorising claims for expenses from the Chairman and Chief Executive Officer;
- (h) reviewing its terms of reference, its work and effectiveness annually and reporting any recommendations to the Board; and
- (i) considering, determining and approving all service contracts between the Company and its directors or between the Company and any subsidiary and any such senior executive.

The Remuneration Committee is obligated under its terms of reference to meet at least twice per year.

REMUNERATION POLICY

The Company's policy on remuneration of directors and senior management is to ensure that remuneration levels are designed to attract, retain and motivate individuals of the quality required by the Company to effectively achieve its goals. A key component of the Remuneration Committee's policy is to ensure that there is a strong link between executive remuneration and performance of the Company and the achievement of its goals. Performance related elements of remuneration are designed to align the interests of senior management and the shareholders and to give such individuals keen incentives to perform at the highest levels. The Remuneration Committee recommends remuneration packages that are both competitive and aligned to shareholders' interests.

The following comprise the principal elements of the current executive directors' remuneration:

- base salary and benefits
- annual discretionary bonus
- long term share based incentives

The Company does not make pension contributions or provide for post-employment health benefits.

In framing the Company's remuneration policy, the Remuneration Committee has given full consideration to the best practice provisions set out in the committee's terms of reference.

The Remuneration Committee is authorized under its terms of reference to obtain outside legal or other independent professional advice on any matters for which it is responsible.

2011 ACTIVITY OF THE REMUNERATION COMMITTEE

The Remuneration Committee met twice during 2011. All of the members of the Remuneration Committee attended the two formal meetings.

During 2011, the Remuneration Committee approved the payment of the Chairman and Chief Executive Officer's annual bonus for 2010 that had been previously deferred. In addition, the Remuneration Committee approved management's recommendations for 2010 employee bonuses and for interim 2011

bonuses (excluding the CEO and COO) together with the grant of 2 million options to various personnel of the Company in recognition of their service during the Company's dispute with the Government of Madagascar during the first half of 2011. The Remuneration Committee also designed and recommended the 2011 option grants to the Chairman and Chief Executive Officer and the Chief Operating Officer. The Remuneration Committee also approved a grant of 300,000 shares of restricted stock to the Company's Chief Engineer in connection with the renegotiation of his engagement with the Company.

REMUNERATION OF J. LAURIE HUNTER, CHAIRMAN AND CHIEF EXECUTIVE OFFICER OF MADAGASCAR OIL

Pursuant to Mr. Hunter's employment agreement, as amended, Mr. Hunter receives an annual base salary of US\$396,252 plus US\$68,750 in lieu of benefits. Mr. Hunter is entitled, from time to time, to be considered for incentive bonus compensation based upon performance criteria established by the Remuneration Committee. In 2011, the Remuneration Committee approved and recommended a bonus of US\$250,000 in respect of the deferred 2010 bonus. For 2011, Mr. Hunter is eligible to receive a bonus of up to 100 per cent of his base salary. The Committee approved a cash bonus of \$300,000 to Mr. Hunter (approximately 75 per cent. of his 2011 base salary) in February 2012. Effective January 1, 2011, Mr. Hunter's compensation was increased proportionately to reflect his commitment of five days per week to the Company. In August 2011, Mr. Hunter's employment agreement was assigned from Madagascar Oil (USA) LLC to the Company for administrative purposes.

During his employment and for a period of two years following termination, Mr. Hunter has agreed to refrain from competing with the Company's business in Madagascar and from recruiting or soliciting the employment of any person who is an employee of the Company or any of the Group. Mr. Hunter's employment agreement has no specified term as he is considered an employee-at-will, but either party is required to provide six months prior notice with respect to termination of service. Mr. Hunter would be entitled to be paid the remainder of his salary during such six-month period to the extent the Company does not provide prior notice. Mr. Hunter is entitled to 12 months' notice with pay if the Company terminates his employment for any reason other than for "cause" in connection with a change-in-control transaction. Mr. Hunter is also entitled to be considered for a pro-rata portion of any incentive bonus payments or equity-based awards that might be considered appropriate in the event his employment is terminated other than for "cause". Under the employment agreement, Mr. Hunter is also eligible for termination payments as a result of his resignation within 30 days of certain specified circumstances, which include a material change in his position with the Company, reduction in base salary of more than 30 per cent., or the Company's breach of his employment agreement.

Pursuant to the Company's 2010 Omnibus Equity Incentive Plan, he was granted incentive based compensation in the form of (a) 1,000,000 Options vesting in three equal parts over three years and (b) 1,000,000 options which vest upon achievement of continuous steam production at the Company's steam flood pilot in Tsimiroro. Each of the foregoing options has an exercise price of 50 pence and a term of five years.

The Company has agreed to maintain Director and Officer Liability Insurance for the benefit of Mr. Hunter consistent with custom and practice within the industry and in amounts agreed by the Board to be adequate to protect the Company.

Mr. Hunter is entitled to serve in the capacity of a director to other companies, subject to approval of the Board.

REMUNERATION OF MARK F. WELLER, CHIEF OPERATING OFFICER OF MADAGASCAR OIL

Pursuant to Mr. Weller's employment agreement, Mr. Weller continues to serve as the Company's Chief Operating Officer, responsible for overseeing the day-to-day operations of the Company, and as a member of the Board. Mr. Weller receives an annual base salary of US\$317,000 plus US\$55,000 in lieu of benefits and is entitled, from time to time, to be considered for incentive bonus compensation based upon performance criteria established by the Remuneration Committee of the Board. For 2011, Mr. Weller is eligible to receive a bonus of up to 100 per cent of his base salary. The Committee approved a cash bonus of \$300,000 to Mr. Weller (approximately 95 per cent. of his 2011 base salary) in February 2012. Up to 75 per cent. of the bonus will be paid on the basis of operational targets against time and budget, and 25 per cent of the bonus will be paid at the discretion of the Remuneration Committee or subject to strategic targets.

During his employment and for a period of two years following termination, Mr. Weller has agreed to refrain from competing with the Company's business in Madagascar and from recruiting or soliciting the employment of any person who is an employee of the Company or any of the Group. Mr. Weller's employment agreement has no specified term as he is considered an employee-at-will, but either party is required to provide six months prior notice with respect to termination of service. Mr. Weller is entitled to be paid the remainder of his salary during such six-month period to the extent the Company does not provide prior notice. Mr. Weller is entitled to 12 months' notice with pay if the Company terminates his employment for any reason other than for "cause" in connection with a change-in-control transaction. Mr. Weller is also entitled to be considered for a pro-rata portion of incentive bonus payments or equity-based awards that might be considered appropriate in the event his employment is terminated other than for "cause". Under the employment agreement, Mr. Weller is also eligible for termination payments as a result of his resignation within 30 days of certain specified circumstances, which include a material change in his position with the Company, reduction in base salary of more than 30 per cent., or the Company's breach of his employment agreement.

Pursuant to the Company's 2010 Omnibus Equity Incentive Plan, he was granted incentive based compensation in the form of (a) 1,000,000 Options vesting in three equal parts over three years and (b) 1,000,000 options which vest upon achievement of continuous steam production at the Company's steam flood pilot in Tsimiroro. Each of the foregoing options has an exercise price of 50 pence and a term of five years.

The Company has agreed to maintain Director and Officer Liability Insurance for the benefit of Mr. Weller consistent with custom and practice within the industry and in amounts agreed by the Board to be adequate to protect the Company.

Mr. Weller is entitled to serve in the capacity of a director to other companies, subject to approval of the Board.

2010 OMNIBUS EQUITY INCENTIVE PLAN BY THE COMPANY

The Company's 2010 Omnibus Equity Incentive Plan provides long-term incentives and rewards to the Company's directors, officers, employees and consultants. See Part 6, Section 5 of the Company's Admission Document (a copy of which is available on the Company's website: www.madagascaroil.com under "Investor Relations") for a more detailed description of this plan. In 2011, the Remuneration Committee recommended to the Board for its approval the grant of 6 million options with an exercise price of 50 pence per share and a term of five years. These options vest equally over three years except for 1 million granted to each of the Chairman and Chief Executive Officer and the Chief Operating Officer which vest upon achievement of continuous steam production at the Tsimiroro steam flood pilot project. The Remuneration Committee also approved the grant of 300,000 shares of Restricted Stock to the Company's Chief Engineer vesting over 3 years subject to achievement of certain targeted minimum number of hours worked annually over the contract period.

The table on the following page sets forth the compensation for the directors of the Company for performance of services in 2011. Remuneration matters related to the non-executive directors are addressed by the entire Board of Directors.

2011 REMUNERATION OF DIRECTORS

	Salary & fees	Benefits	Annual Bonus	Other	Total	Long –term Incentives
Executive						
J. Laurie Hunter	\$396,250	\$68,750(1)	\$300,000 (2)		\$765,000	(5)
Mark Weller	\$317,000	\$55,000(1)	\$300,000	—	\$672,000	(5)
Non-Executive						
Ian Christopher Simon Barby	\$60,282 (3); (7)	—	—	—	\$60,282	(6)
Andrew James Morris	\$55,645 (7)	—	—	—	\$55,645	(6)
Ian Colin Orr- Ewing	\$55,645 (7)	—	—	—	\$55,645	(6)
John Alexander van der Welle	\$68,784 (4);(7)	—	—	—	\$68,784	(6)
Non-Executive Total	\$240,356	—	—	—	\$240,356	

(1) Cash in lieu of benefits.

(2) Excludes a \$250,000 bonus paid in 2011 for work performed in 2010.

(3) Includes \$4,637 p.a. in fees for service as Chairman of the Remuneration Committee.

- (4) Includes \$9,274 p.a. in fees for service as Chairman of Audit Committee and \$15,457 p.a. for service as senior independent director from 1 October 2011.
- (5) Mr. Hunter and Mr. Weller's long-term incentives are summarised elsewhere in this report.
- (6) Each of the non-executive directors received options to purchase 78,947 shares at the Company's admission date on 29 November 2010. Such options have a ten-year term with an exercise price equal to 95 pence. These options vest and become exercisable in three equal annual installments upon completion of each year of service following the grant date.
- (7) Fees denominated in GBP are converted at the rate of 1.5457 USD to 1.00 GBP.

GRANTS OF EQUITY INCENTIVES TO DIRECTORS UNDER 2010 EQUITY INCENTIVE PLAN

Executive Director	Grants at 31 December 2010 at 95 pence (1)	2011 Grants at 50 pence	Total
J. Laurie Hunter	500,000 (2)	2,000,000 (4)	2,500,000
Mark Weller	750,000 (2)	2,000,000(4)	2,750,000
Non-Executive			
Ian Christopher Simon Barby	78,947(3)	—	78,947
Andrew James Morris	78,947(3)	—	78,947
Ian Colin Orr-Ewing	78,947(3)	—	78,947
John Alexander van der Welle	78,947(3)	—	78,947
Total	1,565,788	4,000,000	5,565,788

- (1) Does not include grants of restricted shares under prior stock option plan.
- (2) Options granted effective at admission date (29 November 2010) with an exercise price of 95 pence and vesting equally over three years. These options have a term of five years.
- (3) Options granted effective at admission date (29 November 2010) with an exercise price of 95 pence and vesting equally over three years. These options have a term of ten years.
- (4) 1,000,000 options vesting equally over three years and 1,000,000 options vesting upon the condition that the Company achieves continuous steam production at its Tsimiroro Steam flood pilot project. Each of these options has an exercise price of 50 pence and a term of five years.

See "Directors' Report" elsewhere in this Annual Report for a table setting forth the directors' ownership interests in the Company.

DIRECTORS' REPORT

The Directors submit their report together with the audited consolidated financial statements of Madagascar Oil Limited for the year ended 31 December 2011.

BUSINESS REVIEW

The principal activity of the Company and its subsidiary undertakings (the Group) during the year continued to be exploration and development of heavy oil and conventional oil deposits which have been discovered on five contiguous onshore blocks in Madagascar. Information on the Company's principal subsidiary undertakings appears in note 2 of the Company's financial statements.

The information that fulfills the requirements of the business review and future developments can be found within the Report of the Chairman and Chief Executive Officer, the Operational Review, and the Corporate Governance Statement included in this Annual Report.

RESULTS AND DIVIDENDS

The loss on ordinary activities after taxation for 2011 amounted to \$13.2 million (2010: \$11.6 million).

The directors have not recommended payment of a dividend.

DIRECTORS

The directors of the Company at the date of this Annual Report and their biographical details are set out on pages 12 and 13 of this Annual Report.

In December 2011, Mr. Colin Orr-Ewing was re-elected to the Board for a three year term.

In accordance with our Bye-Laws and in keeping with best corporate governance practice of AIM-listed companies the current Class II Directors, Mr. Mark Weller and Mr. Andrew Morris, will retire by rotation and may seek re-appointment to the Board of Directors of the Company at this year's Annual General Meeting.

The interests of the Directors and persons connected with them in the issued share capital of the Company at 31 December 2011, all of which are beneficial, are as follows:

	No. of Common Shares	No. of Options, Warrants and Restricted Shares(1)	Total
J. Laurie Hunter	1,766,667	2,833,333	4,600,000
Andrew J. Morris(2)	225,700	78,947	304,647
Colin Orr-Ewing(3)	—	78,947	78,947
Mark Weller	600,000	2,750,000	3,350,000
John van der Welle	28,347	78,947	107,294
Ian Barby	30,000	78,947	108,947

Notes:

- (1) See the Report of the Remuneration Committee included elsewhere in this Annual Report for details regarding the options and restricted shares granted to these individuals.
- (2) Includes 225,700 Common Shares held by CLMS Management, LLC, as nominee on behalf of Mr. Morris and does not include an aggregate of 22,792,150 Common Shares held by Persistency Private Equity Limited with which Mr. Morris serves as an investment advisor.
- (3) Does not include 11,990,670 Common Shares held by various affiliated entities of Blakeney General Partners III, Blakeney General Partners IV and Blakeney LP, of which Mr. Orr-Ewing has served as a consultant.

INSURANCE COVER

The Company maintains directors' and officers' liability insurance cover, the level of which is reviewed annually.

SHARE CAPITAL

At the date of this report 192,368,467 Common Shares are issued and fully paid (excluding 4.3 million restricted shares).

SIGNIFICANT INTERESTS

As of 31 December 2011 the Company has been notified of the following interests of 3% or more in the Company's ordinary share capital.

Touradji Group	29,356,680	15.3%
Persistency	22,792,150	11.8%
MSD	18,789,000	9.8%
The John Paul DeJoria Family Trust	12,830,000	6.7%

RAB Special Situations (Master) Fund Limited	12,347,000	6.4%
Blakeney Group	11,990,670	6.2%
Outrider Management, LLC	11,681,790	6.1%
Carmignac	8,649,000	4.4%
Norges	6,649,000	3.5%
Henderson	6,649,000	3.5%

The Company has not been notified of any other person who has an interest in three per cent or more in the Company's share capital.

SHAREHOLDER INFORMATION

The common shares of the Company are listed on the AIM market under the symbol MOIL. On 17 December 2010 the Company suspended trading in its common shares due to a dispute with the Government of Madagascar. The Company resumed trading in its common shares on 27 June 2011 based on the resolution of the dispute around its Tsimororo Block.

FINANCIAL INSTRUMENTS

Details of cash holdings are shown in notes 21 and 31 to the financial statements. Details of the Group's exposure to credit risk, foreign currency risk and interest rate risk are shown in note 31 to the financial statements.

POST REPORTING DATE EVENTS

In January 2012, the Company filed an appeal of its VAT assessment by the Madagascar Tax Administration with the Council of State, the judiciary body in Madagascar responsible for hearing final appeals of tax matters in Madagascar. See note 33 to the Company's financial statements.

In February 2012, the Company completed a US\$26.5 million placing of Common Shares at 28 pence per share. The placing consisted of two tranches: 57.7 million shares were issued on 27 February 2012 and 2.2 million shares will be issued in March 2012 pending a special general meeting of the shareholders to approve the Board's additional authority for the issuance of the additional shares without pre-emptive rights.

SUPPLIER PAYMENT POLICY

The Company's policy is to agree on payment terms with individual suppliers and to abide by those terms. Trade payables of the Group as at 31 December 2011 and 2010 were approximately 30 to 40 days.

DONATIONS

During the year ending 31 December 2011 the Company made no political contributions and a de minimis amount of charitable contributions.

AUDITORS

A resolution to re-appoint BDO USA, LLP as auditors of the Company will be proposed at the Annual General Meeting.

GOING CONCERN

The financial statements have been prepared on a going concern basis.

DISCLOSURE OF INFORMATION TO THE AUDITORS

Each person who is a Director at the date of approval of this Annual Report confirms that:

- So far as the Director is aware, there is no relevant audit information of which the Company's auditors are unaware; and
- Each Director has taken all the steps that he ought to have taken as a Director in order to make himself aware of any relevant audit information and to establish that the Company's auditors are aware of that information.



Statement of Directors' Responsibilities

Bermuda Company law requires the Directors to prepare financial statements for each financial year that give a true and fair view of the state of affairs of the Company and its subsidiaries and the profit or loss for that year. The Directors are required to prepare the financial statements of the Company and its subsidiaries on the going concern basis unless it is inappropriate to presume that the Company and its subsidiaries will continue in business.

The Directors confirm that suitable accounting policies have been used and applied consistently. They also confirm that reasonable and prudent judgments and estimates have been made in preparing the financial statements for the year ended 31 December 2011 and that applicable standards have been followed.

The Directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Company and for ensuring that the financial statements comply with International Financial Accounting Standards. Legislation in Bermuda governing the financial statements and other information included in the Annual Reports may differ from legislation in other jurisdictions. They are also responsible for safeguarding the assets for the prevention and detection of fraud and other irregularities.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website.

J. Laurie Hunter
Chairman of the Board



Madagascar Oil Limited

Consolidated Financial Statements

Years Ended 31 December 2011 and 2010

TABLE OF CONTENTS:

Independent Auditors' Report	1
Consolidated Financial Statements	
■ Statements of Financial Position _____	2
■ Statements of Comprehensive Income _____	3
■ Statements of Cash Flows _____	4
■ Statements of Changes in Equity _____	5
■ Notes to Consolidated Financial Statements _____	6



INDEPENDENT AUDITORS' REPORT

Board of Directors and shareholders of Madagascar Oil Limited
Madagascar Oil Limited
Houston, Texas

We have audited the accompanying consolidated statements of financial position of Madagascar Oil Limited and subsidiaries ("the Company") as of 31 December 2011 and 2010 and the related consolidated statements of comprehensive income, changes in equity and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and in accordance with International Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As described in Note 33, uncertainty exists related to the status of certain of the Company's production sharing contracts in Madagascar.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Madagascar Oil Limited at 31 December 2011 and 2010, and the results of its operations and its cash flows for the years then ended in conformity with International Financial Reporting Standards as issued by the International Accounting Standards Board.

BDO USA, LLP

07 March 2012



Madagascar Oil Limited
Consolidated Statements of Financial Position

<i>As of 31 December</i>	2011	2010
	<i>\$(000)</i>	<i>\$(000)</i>
Assets		
Non-Current Assets		
Property, plant and equipment (Note 15)	\$ 14,610	15,171
Exploration and evaluation assets (Note 16)	103,971	85,830
Other intangible assets (Note 17)	175	172
Non-current tax assets (Note 14)	2,559	1,802
Financial assets (Note 20)	18	16
Restricted cash (Note 21)	2,560	1,765
Total non-current assets	123,893	104,756
Current Assets		
Other assets (Note 19)	2,851	1,386
Cash and cash equivalents (Note 21)	40,459	67,523
Total current assets	43,310	68,909
	\$ 167,203	173,665
Equity and Liabilities		
Capital and reserves		
Issued capital (Note 22)	\$ 195,087	195,087
Equity-settled transactions reserve (Note 27)	4,470	3,049
Accumulated deficit (Note 23)	(39,139)	(27,567)
Total equity	160,418	170,569
Non-Current Liabilities		
Provisions (Note 24)	341	246
Total non-current liabilities	341	246
Current Liabilities		
Trade and other payables (Note 25)	5,366	2,800
Provisions (Note 24)	1,078	50
Total current liabilities	6,444	2,850
	\$ 167,203	173,665

See accompanying notes to consolidated financial statements.

Madagascar Oil Limited
Consolidated Statements of Comprehensive Income

<i>For the Years Ended 31 December</i>	2011	2010
	<i>\$(000)</i>	<i>\$(000)</i>
Revenue	\$ —	—
Operating Expenses		
Salaries and employee benefits expense (Note 11)	(7,227)	(3,471)
Depreciation and amortization expense (Note 12)	(199)	(322)
Consulting expense (Note 9)	(1,772)	(559)
Production sharing and contractual fees (Note 10)	(1,127)	(1,127)
IPO transaction expense (Note 22)	—	(2,763)
Other expenses (Note 8)	(2,436)	(2,068)
Net foreign exchange loss (Note 5)	(194)	(290)
Loss on disposals	(57)	(298)
Oil activities loss (Note 32)	(291)	(105)
Operating Loss	(13,303)	(11,003)
Finance Income (Note 6)	97	9
Finance Expense (Note 6)	—	(518)
Loss Before Taxes	(13,206)	(11,512)
Income Tax Expense (Note 7)	(42)	(62)
Net Loss and Total Comprehensive Loss Attributable to Owners of Parent	\$ (13,248)	(11,574)
Loss per share attributable to the equity owners (Note 13)		
Basic and diluted	\$ (0.07)	(0.08)

See accompanying notes to consolidated financial statements.

Madagascar Oil Limited
Consolidated Statements of Cash Flow

<i>For the Years Ended 31 December</i>	2011	2010
	<i>\$(000)</i>	<i>\$(000)</i>
Cash Flows From Operating Activities:		
Net Loss	\$ (13,248)	(11,574)
Income tax expense recognised in net loss	42	62
Finance (income) expense, net	(97)	509
Loss on disposals	57	298
Depreciation and amortization of non-current assets	199	322
Oil activities (income) loss, net	291	105
Net foreign exchange loss	194	462
Expense recognised in loss in respect of equity-settled share-based payments	3,097	1,304
	(9,465)	(8,512)
Movements in working capital		
(Increase) decrease in other assets	(2,055)	(1,635)
Increase (decrease) in trade and other payables	2,204	2,031
Increase (decrease) in provisions	28	(42)
Income taxes paid	(42)	(14)
Net cash used in operating activities	(9,330)	(8,172)
Cash Flows From Investing Activities		
Interest received	97	—
Payments for intangible assets	(178)	—
Payments for property, plant and equipment	(1,692)	(57)
Proceeds from disposal of property, plant and equipment	—	7
Exploration and evaluation costs paid	(15,166)	(12,436)
Net cash used in investing activities	(16,939)	(12,486)
Cash Flows From Financing Activities		
Proceeds from issues of equity shares	—	83,657
Proceeds from debt	—	2,873
Repayment of debt	—	(2,868)
Interest paid	—	(125)
Restricted cash	(795)	1,743
Net cash provided by financing activities	(795)	85,280
Net (Decrease) Increase in Cash and Cash Equivalents	(27,064)	64,622
Cash and Cash Equivalents at Beginning of Year	67,523	2,901
Cash and Cash Equivalents at End of Year	\$ 40,459	67,523
Non-cash Investing and Financing Activities:		
Warrants liability reclassified to equity	\$ —	—
Conversion of debt to equity	—	5
Depreciation capitalized in exploration and evaluation assets	2,880	2,932

See accompanying notes to consolidated financial statements.



Madagascar Oil Limited

Consolidated Statements of Changes in Equity

<i>For the Years Ended 31 December 2011</i>	Share Capital	Share Premium	Equity-Settled Transactions Reserves	Accumulated Deficit	Total
	<i>\$(000)</i>	<i>\$(000)</i>	<i>\$(000)</i>	<i>\$(000)</i>	<i>\$(000)</i>
Balance at 31 December 2009	\$ 131	\$ 111,288	\$ 141,911	\$ (156,540)	\$ 96,790
Loss for the period	—	—	—	(11,574)	(11,574)
Transfer of equity settled transaction reserve	—	—	(140,547)	140,547	—
Issue of ordinary shares to shareholders	60	83,597	—	—	83,657
Recognition of equity-settled transactions under employee share option plan	—	—	709	—	709
Issue of ordinary shares under employee share option plan	2	—	478	—	480
Issue of ordinary shares to Directors	1	—	114	—	115
Issue of ordinary shares to Credit Suisse and conversion of convertible debt	3	5	384	—	392
Balance at 31 December 2010	\$ 197	\$ 194,890	\$ 3,049	\$ (27,567)	\$ 170,569
Loss for the period	—	—	—	(13,248)	(13,248)
Transfer of equity settled transaction reserve	—	—	(1,676)	1,676	—
Recognition of equity-settled transactions under employee share option plan	—	—	3,097	—	3,097
Balance at 31 December 2011	\$ 197	\$ 194,890	\$ 4,470	\$ (39,139)	\$ 160,418

	Voting Shares	Non-Voting Shares	Total
Balance at 31 December 2009	118,658,270	13,040,000	131,698,270
Shares granted to Directors	1,100,000	—	1,100,000
Shares granted to personnel	1,003,300	—	1,003,300
Shares granted to shareholders	72,829,947	(13,040,000)	59,789,947
Shares granted to others	2,773,640	—	2,773,640
Balance at 31 December 2010	196,365,157	—	196,365,157
Shares granted to others	303,310	—	303,310
Balance at 31 December 2011	196,668,467	—	196,668,467

See accompanying notes to consolidated financial statements.



1. GENERAL INFORMATION

Madagascar Oil Limited (Bermuda) (the “Company”) is an exempted limited liability company incorporated in Bermuda with registration number 37901. The address of its registered office is Canon’s Court 22 Victoria Street – Hamilton HM12 Bermuda.

Madagascar Oil Limited and its affiliates (collectively, the “Group”) commenced business in 2004 by entering into six production sharing contracts (“PSCs”) for oil exploration and production in Madagascar with the Republic of Madagascar. The production sharing contracts were held in one wholly owned subsidiaries, Madagascar Oil SA (“MOSA”) and Majunga Oil SARL (“Majunga”) registered under the Laws of the Republic of Madagascar. In November 2011 the Majunga subsidiary was liquidated and all production sharing contracts are held in MOSA.

The principal activities of the Group are described in Note 5.

MOSA holds Production Sharing Contracts for the onshore license blocks 3102, 3104, 3105, 3106 and 3107 all of which are geographically contiguous on the west part of the island:

- Block 3102 Bemolanga is 5,463km² in size and hosts the Bemolanga ultra heavy oil field. It was granted on 17 August 2004.
- Block 3104 Tsimiroro is 6,670 km² in size and hosts the Tsimiroro heavy oil field. It was granted on 17 August 2004.
- Block 3105 Manambolo is 3,995 km² in size and was granted on 14 December 2004.
- Block 3106 Morondava is 6,825 km² in size and was granted on 14 December 2004.
- Block 3107 Manandaza is 6,580 km² in size and was granted on 14 December 2004.

On 17 September 2008, the Malagasy government approved a 60% farm out and transfer of operatorship of Block 3102 Bemolanga to an affiliate of TOTAL S.A. (“TOTAL”). MOSA has also transferred to TOTAL the operatorship of the license.

In addition to the 4 blocks held 100% and operated by the Group and the 40% non-operated share in the 3102 Bemolanga block, the Group entered into an Agreement in December 2005 with Tullow Oil, Plc (“Tullow”) for the exploration of the onshore block 3109 Mandabe (11,050 km² in size). The Office des Mines Nationales et des Industries Strategiques (“OMNIS”) approved the transfer to Majunga on 20 December 2006 of a 50% interest in the block. Tullow is operating the block. In September 2008 Majunga withdrew from the Joint Operating Agreement and the Production Sharing Contract as of 31 October 2008. See Note 19.

The exploration period under the PSCs generally consist of 3 phases of 2 years, 2 years and 4 years respectively. An extension of 2 years maximum can also be granted by the OMNIS at the end of the 3rd phase of the Exploration Period specified in the PSC.

Per amendments to the applicable PSCs in June 2009, the split of the different phases composing the exploration period has been modified for the licenses 3105, 3106, 3107. The total duration of the Exploration Period was not modified.

At 31 December 2011, the:

- 3102 and 3104 blocks held by Madagascar Oil SA are in the 3rd of the 3 phases constituting the Exploration Period
- 3105, 3106, 3107 blocks held by Madagascar Oil SA are in the 2nd of the 3 phases constituting the Exploration Period. (See discussion in note 33)



2. SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied from those used in prior years, unless otherwise stated.

STANDARDS, AMENDMENTS AND INTERPRETATIONS EFFECTIVE IN 2011

IFRS 2 'Share-Based Payments (Amendment)' – The amendment clarifies that where a parent (or another group entity) has an obligation to make a cash-settled share-based payment to another group entity's employees or suppliers, the entity receiving the goods or services should account for the transaction as equity-settled.

IAS 24 'Related Party Disclosures' – The revised standard simplifies the disclosure requirements for government-related entities by focusing disclosures on significant transactions, and clarifies the definition of a related party.

IAS 27 'Consolidated and Separate Financial Statements (Amendment)' – The amendment affects the acquisition of subsidiaries achieved in stages and disposals of interests. Amendment does not require the restatement of previous transactions.

STANDARDS, AMENDMENTS AND INTERPRETATIONS TO EXISTING STANDARDS THAT ARE NOT YET EFFECTIVE AND HAVE NOT BEEN EARLY ADOPTED BY THE GROUP.

The following standards, amendments and interpretations to existing standards have been published and are mandatory for the Group's accounting periods beginning on or after 1 January 2012 or later periods, but the Group has not early adopted them. The Company is evaluating whether the implementation of these statements will have a material impact on future financial results.

- IAS 1 Presentation of Items of Other Comprehensive Income (as amended in 2011)
- IFRS 9 Financial Instruments
- IFRS 10 Consolidated Financial Statements
- IFRS 11 Joint Arrangements
- IFRS 13 Fair value measurement (applied for annual periods beginning or after 1 January 2013)

BASIS OF PREPARATION

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS). They have been prepared on the historical cost basis.

Management has concluded that the US dollar is the functional currency of each entity of the Group due mainly to the fact that:

- Most of the expenses of the entities of the Group are denominated in US dollars
- Oil sales are always denominated in US dollars on the international markets and
- Funds from financing activities (debt or equity instruments) are generated in US dollars, other than its November 2010 IPO, which was denominated in Great British pounds before subsequent conversion into US dollars.

The consolidated financial statements are presented in US dollars.

BASIS OF CONSOLIDATION

Subsidiaries

The consolidated financial statements incorporate the financial statements of the Company and its wholly-owned subsidiaries. Subsidiaries are those entities controlled by the Company. Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

The following companies have been consolidated within the Group financial statements:

Name of Subsidiary	Registered	Holding	Voting Power Held	Principal Activity
		%	%	
Madagascar Oil Ltd	Mauritius	100	100	Investment
Madagascar Oil SA	Madagascar	100	100	Oil exploration and production
Majunga Oil SARL ⁽ⁱ⁾	Madagascar	100	100	Oil exploration and production
Madagascar Oil (USA) LLC	United States of America	100	100	Administration and Technical Support

⁽ⁱ⁾ Majunga Oil SARL was liquidated in November 2011.

Transactions eliminated upon consolidation

Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with those used by other members of the Group. All intra-group transactions, balances, income and expenses are eliminated in full on consolidation. There is no non-controlling interest in any of the subsidiaries of the Group.

JOINT VENTURE OPERATIONS

It is standard industry practice to conduct petroleum operations jointly with other exploration and production companies.

A joint venture is a contractual arrangement whereby the Group and other parties undertake an economic activity that is subject to joint control, that is when the strategic financial and operating policy decisions relating to the activities of the joint venture require the unanimous consent of the parties sharing control (venturers).

Where a group entity undertakes its activities under joint venture arrangements directly, the Group's share of jointly controlled assets and any liabilities incurred jointly with other venturers are recognised in the financial statements of the relevant entity and classified according to their nature. Liabilities and expenses incurred directly in respect of interests in jointly controlled assets are accounted for on an accrual basis. Income from the sale or use of the Group's share of the output of jointly controlled assets, and its share of joint venture expenses, are recognised when it is probable that the economic benefits associated with the transactions will flow to/from the Group and their amount can be measured reliably.

REVENUE RECOGNITION

Revenue is measured at the fair value of the consideration received or receivable and is recognized at time of delivery of the product to the purchaser. Revenue is reduced for estimated customer returns, rebates and other similar allowances.



Sale of Goods

Since its creation, the Group has recognised no revenue due to the fact that the Group is in the exploration phase of its projects and has not reached commercial operations as of 31 December 2011.

Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Assets held under finance leases are initially recognised as assets of the Group at their fair value at the inception of the lease or, if lower, at the present value of the minimum lease payments. The corresponding liability to the lessor is included in the statement of financial position as a finance lease obligation.

Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are related to non-qualifying assets and charged directly to profit and loss. Contingent rentals are recognised as expenses in the periods in which they are incurred.

Operating lease payments are recognised as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed. Contingent rentals arising under operating leases are recognised as an expense in the period in which they are incurred.

FOREIGN CURRENCIES

The individual financial statements of each entity of the Group are presented in the currency of the primary economic environment that the entity operates (its functional currency). On consolidation the results and financial position of each entity are expressed in US dollar (USD).

In preparing the financial statements of the individual entities, transactions in currencies other than the entity's functional currency (foreign currencies) are recorded at the average of the official bid and offered exchange rates as published by the Central Bank of Madagascar on the first day of the month in which the expenses are recorded in order to comply with the regulation stated in the Production Sharing Contracts signed by the Group with Malagasy authorities. At each statement of financial position date, monetary items denominated in foreign currencies are retranslated at the rates prevailing at the statement of financial position date.

Actual exchange differences are recognised in profit or loss in the period in which they arise. Exchange differences resulting from the retranslation of monetary items at the rates prevailing at the statement of financial position date are recognised in profit or loss at each statement of financial position date.

SHARE-BASED PAYMENTS

The Group issues equity-settled share-based payments to some of their employees and directors through stock options plans, restricted shares or warrants. According to IFRS 2, these plans are measured at fair value on the grant date and are accounted for as an employee expense on a straight-line or graduated vesting for each tranche basis over the vesting period of the plans. The fair value of granted options is determined based on a lattice model in order to take into account all the characteristics of these instruments.

The Group may also issue equity instruments as a counterpart of goods and services received from financial institutions and other intermediaries. According to IFRS 2, these instruments (warrants) are accounted for as an expense on the basis of the market value of goods and services received.

For cash-settled share-based payments, a liability equal to the portion of the goods or services received is recognised at the current fair value determined at each statement of financial position date.

The proceeds received net of any directly attributable costs are credited to share capital (nominal value) and share premium.

NON CURRENT TAX ASSET

The non-current tax asset corresponds to VAT receivable which shall be recovered when the Company begins collecting VAT on sales of crude oil. The VAT receivable has not been discounted.

INCOME TAX

The tax expense represents the sum of the tax currently payable and deferred tax.

Current tax

The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the statement of financial position date.

Deferred Tax

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax basis used in the computation of taxable profit and is accounted for using the statement of financial position liability method.

Deferred tax liabilities are generally recognised for all taxable temporary differences, and deferred tax assets are generally recognised for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilized. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences associated with investments in subsidiaries and associates, and interests in joint ventures, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at each statement of financial position date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered. Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realized, based on tax rates (and tax laws) that have been enacted or substantively enacted by the statement of financial position date. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the reporting date, to recover or to settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

Current and Deferred Tax for the Period

Current and deferred tax are recognised as an expense or income in profit or loss, except when they relate to items credited or debited directly to equity or other comprehensive income, in which case the tax is also recognised directly in equity or other comprehensive income, as appropriate.

**PROPERTY, PLANT AND EQUIPMENT**

Fixtures and equipment are stated at cost less accumulated depreciation and any accumulated impairment losses. Depreciation is charged so as to write off the cost or valuation of assets over their estimated useful lives, using the straight-line method. The estimated useful lives, residual values and depreciation method are reviewed at each year end, with the effect of any changes in estimate accounted for on a prospective basis.

Assets held under finance leases are depreciated over their expected useful lives on the same basis as owned assets or, where shorter, the term of the relevant lease. Useful lives used by the Group are the following:

	Useful Lives (Years)
Drilling and Exploration Equipment	5-10
Vehicles	5
Equipment	5-10
Other	5

The gain or loss arising on the disposal or retirement of an item of property, plant and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in profit or loss.

INTANGIBLE ASSETS

Intangible assets acquired separately are reported at cost less accumulated amortization and accumulated impairment losses. Amortization is charged on a straight-line basis over their estimated useful lives of 4 years and recorded in the statement of comprehensive income as depreciation and amortization expense. The estimated useful life and amortization method are reviewed at the end of each annual reporting period, with the effect of any changes in estimate being accounted for on a prospective basis.

EXPLORATION AND EVALUATION ASSETS

The Group applies the full cost method of accounting for exploration and evaluation costs. Under the full cost method, costs directly associated with exploring for and evaluating oil and gas properties are accumulated and capitalized. However, they do not include costs incurred prior to having obtained the legal rights to explore an area, which are expensed directly to the income statement of operations as they are incurred. Once commercial reserves are found, exploration and evaluation assets are tested for impairment. Depreciation of property, plant and equipment assets utilized in exploration and evaluation activities is capitalized within exploration and evaluation costs. No amortization or depletion is charged during the Exploration and Evaluation Phase. Management believes that the carrying value of these costs will be recovered from future operations.

If the exploration and development is ceased or if it is determined that the carrying value cannot be supported by future production or sale, the excess of the carrying value above recoverable value will be charged against operations in the period that the determination of an impairment is made. Where an impairment 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 asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognised immediately in profit or loss.

At the completion of the Exploration and Evaluation Phase, if technical feasibility is demonstrated and commercial reserves are discovered, then, following the decision to continue into the development phase, the carrying value of the relevant E&E asset will be reclassified as a Development and Production ("D&P") asset, but only after the carrying value of the asset has been assessed for impairment.



IMPAIRMENT

Property, plant and equipment and intangible assets excluding exploration and evaluation assets

At each statement of financial position date, the Group 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. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any).

Intangible assets with indefinite useful lives and intangible assets not yet available for use are tested for impairment annually, and whenever there is an indication that the asset may be impaired.

The recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted. If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised immediately in profit or loss.

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 asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognised immediately in the statement of comprehensive income as non-current activities income.

Exploration and Evaluation Assets

Impairment tests are performed when the Group identifies facts or circumstances implying a possible impairment in accordance with IFRS 6.

DECOMMISSIONING COSTS

When the Group is legally, contractually or constructively required to restore a site, the estimated costs of site restoration are accrued. The estimated future costs for known restoration requirements are determined on a field by field basis and are calculated based on the present value of estimated future costs. When the Group does not have a reliable reversal time or when the effect of the passage of time is not material, the provision is calculated based on undiscounted cash flows.

PROVISIONS

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that the Group will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the statement of financial position date, taking into account the risks and uncertainties surrounding the obligation.

Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, the receivable is recognised as an asset if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably.

CASH AND CASH EQUIVALENTS

Restricted Cash

Cash and cash equivalents consist of cash and time deposits. Restricted cash consists of bank deposits used to guarantee the Bank Letters of Guarantee submitted to the Malagasy State as per Production Sharing Contracts' requirements during the Exploration Period. In 2011 the Group set aside \$0.8 million in a restricted account in order to continue the appeals process on disputed VAT payments on foreign services.

Other Financial Assets

Other financial assets consist of deposits paid under lease agreements. These assets are stated at the carrying value, as it approximates fair-value due to the short-term maturity of these instruments.

Impairment of Financial Assets

Financial assets are assessed for indicators of impairment at each statement of financial position date. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been impacted.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables where the carrying amount is reduced through the use of an allowance account.

When a trade receivable is uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognised in profit or loss.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be rebated objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed through profit or loss to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortized cost would have been had the impairment not been recognised.

FINANCIAL LIABILITIES AND EQUITY INSTRUMENTS ISSUED BY THE GROUP

Classification as Debt or Equity

Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangement.

The Company has classified the convertible debt in issue as a compound financial instrument. Accordingly, the Company presents the liability and equity components separately on the balance sheet. The classification of the liability and equity components is not reversed as a result of a change in the likelihood that the conversion option will be exercised. No gain or loss arises from initially recognizing the components of the instrument separately. Interest on the debt element of the loan is accreted over the term of the loan. Costs associated with the raising of debt are set off against the gross value of monies received.

Equity Instruments

An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities.

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

Trade Payables

Trade payables are stated at their carrying value, as it approximates fair value due to the short-term maturity of these instruments.



Financial Liabilities

Financial liabilities consist of trade and other payables and borrowings.

Financial liabilities, including borrowings, are initially measured at fair value, net of transaction costs. Financial liabilities are subsequently measured at amortized cost using the effective interest method, with interest expense recognised on an effective yield basis. The effective interest method is a method of calculating the amortized cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or, where appropriate, a shorter period. The effective interest method is always considered but not applied when its impact is negligible.

Borrowing Costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale.

All other borrowing costs are recognised in profit or loss in the period in which they are incurred.

3. CRITICAL ACCOUNTING JUDGMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

In the application of the Group's accounting policies, which are described in Note 2, management is required to make judgments, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods. Such disclosures are included in the relevant asset and liability notes or as part of the relevant accounting policy disclosures. The estimates used by management relate to the decommissioning costs, impairments and share-based transactions.

The estimates and underlying assumptions are based on the best possible review and interpretation of the petroleum and general regulations applicable to the Group in the countries where it operates in accordance with international industry standards.

Critical accounting judgements and key sources of estimation uncertainty:

In the process of applying the Group's accounting policies, which are described in Note 1, Management has made the following judgements that have the most significant effect on the amounts recognised in the financial statements:

Recoverability of Exploration and Evaluation Costs – Under the full cost accounting method of accounting for exploration costs, such costs are capitalized as intangible assets and assessed for impairment on a cost pool basis when circumstances suggest that the carrying amount off the costs pool may exceed its recoverable value and, therefore, there is a potential risk of an impairment adjustment. This assessment involves judgement as to the likely future commerciality of the asset and when such commerciality should be determined based on future revenue and costs pertaining to any concession based on proved plus probable, prospective and contingent resources and the discount rate to be applied to such revenues and cost for the purpose of deriving a recoverable value. Management has reviewed the recoverability of the assets and consider this to be greater than the current net book value.

Share Options – Provisions for share-based payment costs requires the selection of an appropriate valuation model, consideration as to the inputs necessary for the valuation model chosen and the estimation of the number of awards that will ultimately vest, inputs for which arise from judgements relating to the continuing participation of employees.

Impairment Review - While conducting an impairment review of its assets, the Group makes certain judgements in making assumptions about the likelihood of license conversion, the future prices, reserve levels and future development and production costs. Changes in the estimates used can result in significant charges to the statement of comprehensive income. This is performed solely for the purposes of considering the carrying value of the Group's assets.

Legal Proceedings and Commercial Disputes - In accordance with IFRS, the Group only recognises a provision where there is a present obligation from a past event, a transfer of economic benefit is probable and the amount of cost of the transfer can be estimated reliably. In instances where the criteria are not met, a contingent liability may be disclosed in the notes to the financial statements. Realisation of any contingent liabilities not currently recognised or disclosed in the financial statements could have a material effect on the Group's financial position. Application of this accounting principle requires the Group's management to make determinations about various factual and legal matters beyond their control. Among the factors considered in making decisions on provisions are the nature of the disputes and litigations, the progress of the cases, the opinions of legal advisers, experience of similar cases and any decision of the Group's management as to how it will respond to any such claim or litigation.

4. BUSINESS AND GEOGRAPHICAL SEGMENTS

BUSINESS SEGMENT

The Group operated in one principle operating segment, the exploration for and production of oil and gas in the country of Madagascar. The Group is engaged in oil and gas exploration and production which represents its only activity as of 31 December 2011; all its operations are in the Exploration Period of the Production Sharing Contracts signed by its subsidiaries with the Republic of Madagascar.

No revenues have been generated by the Group. Non-current assets located in Madagascar total \$121.1 million as of 31 December 2011.

The Group will evaluate the need for multiple operating segments in the future as production of oil and gas commences.

GEOGRAPHICAL SEGMENT

The Group only operates in Madagascar where it holds all its licenses. The primary segment of the Group is the business segment and its secondary segment is the geographical segment.

5. NET FOREIGN EXCHANGE LOSSES

The net foreign exchange loss booked is not significant and mainly the consequence of the erratic movements of the Malagasy currency (MGA) as well as the ones of other currencies against the US dollar during the years 2010 and 2011. For information 1 USD = 2,203.74 MGA as of 31 December 2011 and 1 USD = 2,146.12 MGA as of 31 December 2010.

6. FINANCE INCOME (EXPENSE)

<i>Year Ended 31 December</i>	2011	2010
	<i>\$(000)</i>	<i>\$(000)</i>
Time deposits investments ⁽ⁱ⁾	97	9
Interest on borrowings ⁽ⁱⁱ⁾	—	(374)
Convertible debt warrants ⁽ⁱⁱⁱ⁾	—	(144)
Total finance income (loss), net	97	(509)

⁽ⁱ⁾ Available cash represents the amount of funds raised by the Company to finance its operations but not yet used. This cash is invested in time deposits with international banks of first rank at short term.

⁽ⁱⁱ⁾ Interests on borrowings are composed of the value of shares issued to Credit Suisse in settlement of terms of a warrant contract (Note 27). At 31 December 2010, interests on borrowings were composed of costs associated with the modification of the Credit Suisse warrants and of interest paid on interim financing.

⁽ⁱⁱⁱ⁾ The Company incurred expense due to the issuance of convertible debt with warrants in 2010 (Note 26).

**7. INCOME TAXES**

The tax expense for the Group is:

<i>Year Ended 31 December</i>	2011	2010
	<i>\$(000)</i>	<i>\$(000)</i>
The minimum tax liability payable by Madagascar Oil SA	—	—
The minimum tax liability payable by Majunga Oil SARL	—	—
The tax liability due by Madagascar Oil (USA) LLC	42	62
	42	62

As of 31 December 2010 the Group had \$9.7 million in operating losses in the Madagascar subsidiaries, MOSA and Majunga. With the dissolution of the Majunga subsidiary in November 2011 the Group has no operating losses remaining in these subsidiaries to apply to future operating income for income tax purposes. The Group did not recognize any deferred tax in accordance with IAS 12 for 2010 or 2011 as the deferred tax assets related to the operating losses were fully provided with a valuation allowance.

<i>Year Ended 31 December</i>	2011	2010
	<i>\$(000)</i>	<i>\$(000)</i>
Deferred tax credit	—	—
The charge for the year can be reconciled per the statement of comprehensive income as follows:		
Loss on ordinary activities before taxes	(13,206)	(11,512)
Tax benefit on ordinary activities at the combined federal and state rates of corporation tax in the US of 28%	(3,698)	(3,223)
Less tax charges attributable to non-taxable overseas jurisdictions	3,740	3,285
Income/expenses disallowed for tax	—	—
Tax losses carried forward	—	—
Movements in deferred taxation	—	—
Tax charge for the year	42	62

8. OTHER EXPENSES

<i>Year Ended 31 December</i>	2011	2010
	<i>\$(000)</i>	<i>\$(000)</i>
Rentals	330	249
Auditors Fees and Expenses	226	194
Services from related parties ⁽ⁱ⁾	267	658
Travel and telecommunications	941	502
Other general and administrative expenses ⁽ⁱⁱ⁾	672	465
	2,436	2,068

⁽ⁱ⁾ Services from related parties in 2010 constitute contracts with Mark Weller, Jim Lederhos, Jim Collins, Gil Melman and Seth Fagelman. Services from related parties in 2011 represent board fees and reimbursed expenses. See Note 28 Related Parties.

⁽ⁱⁱ⁾ Other general and administrative expenses are constituted of recruitment fees, public relations, insurance, contracted personnel, security expenses, office running costs and bank commissions.

9. CONSULTING EXPENSES

The consulting expenses relate to the legal, fiscal and financial advices provided to the Group related to its activities in Bermuda, Madagascar and Mauritius. See Note 28 about legal advisors from related parties.

<i>Year Ended 31 December</i>	2011	2010
	<i>\$(000)</i>	<i>\$(000)</i>
Legal and fiscal advisors- Bermuda & Mauritius	1,673	427
Legal and fiscal advisors –Madagascar	86	67
Legal and fiscal advisors-USA	13	65
	1,772	559

**10. PRODUCTION SHARING CONTRACTUAL FEES**

<i>Year Ended 31 December</i>	2011	2010
	<i>\$(000)</i>	<i>\$(000)</i>
Administrative fees	837	837
Training fees	290	290
	1,127	1,127

Amounts represent the contractual charges for all licenses under the Production Sharing Contracts signed with the Republic of Madagascar.

11. SALARIES AND EMPLOYEE BENEFITS EXPENSES

<i>Year Ended 31 December</i>	2011	2010
	<i>\$(000)</i>	<i>\$(000)</i>
Wages, salaries and incentives	3,797	2,144
Social security costs	333	23
Share-based payments	3,097	1,304
	7,227	3,471

See Note 27 Share-based payments for more details.

12. DEPRECIATION AND AMORTIZATION EXPENSES

<i>Year Ended 31 December</i>	2011	2010
	<i>\$(000)</i>	<i>\$(000)</i>
Depreciation of property, plant and equipment assets	74	136
Amortization of intangible assets	125	186
	199	322

13. LOSS PER SHARE (LPS)

Basic loss per share amounts are calculated by dividing the loss for the years attributable to ordinary equity holders by the weighted average number of ordinary shares outstanding during the year.

Diluted loss per share amounts are calculated by dividing the loss for the years attributable to ordinary holders by the weighted average number of ordinary shares outstanding during the year, plus the weighted average number of shares that would be issued on the conversion of dilutive potential ordinary shares into ordinary shares. The effect of the warrants and options are anti-dilutive in 2011 and 2010.

<i>Year Ended 31 December</i>	2011	2010
	<i>\$(000)</i>	<i>\$(000)</i>
Net loss attributable to equity holders used in basic calculation	(13,248)	(11,574)
Net loss attributable to equity holders used in dilutive calculation	(13,248)	(11,574)
Basic weighted average number of shares	196,490,910	139,461,480
Dilutive potential ordinary shares		
Shares related to warrants	1,801,879	3,984,945
Shares related to options	4,776,884	364,150
Diluted weighted average number of shares	203,069,673	143,810,575
Loss Per Share		
Basic	<i>\$(0.07)</i>	<i>\$(0.08)</i>
Dilutive	<i>\$(0.07)</i>	<i>\$(0.08)</i>

14. NON-CURRENT TAX ASSETS

<i>As of 31 December</i>	2011	2010
	<i>\$(000)</i>	<i>\$(000)</i>
VAT Credit	2,559	1,802
	2,559	1,802

The amount corresponds to the VAT receivable and shall be recovered when the Company begins collecting VAT on sales of crude oil.

15. PROPERTY, PLANT AND EQUIPMENT

Cost	Vehicles	Equipment	Other	Drilling & Exploration Equipment	Total
	<i>\$(000)</i>	<i>\$(000)</i>	<i>\$(000)</i>	<i>\$(000)</i>	<i>\$(000)</i>
Balance at 1 January 2010	143	756	110	25,833	26,842
Additions	—	22	—	57	79
Disposals	—	(360)	(58)	(72)	(490)
Balance at 31 December 2010	143	418	52	25,818	26,431
Additions	—	16	—	1,639	1,655
Disposals	(7)	(14)	(4)	—	(25)
Balance at 31 December 2011	136	420	48	27,457	28,061

Accumulated Depreciation	Vehicles	Equipment	Other	Drilling & Exploration Equipment	Total
	<i>\$(000)</i>	<i>\$(000)</i>	<i>\$(000)</i>	<i>\$(000)</i>	<i>\$(000)</i>
Balance at 1 January 2010	(109)	(418)	(26)	(7,749)	(8,302)
Depreciation expense	(29)	(94)	(13)	(2,932)	(3,068)
Impairment ⁽ⁱ⁾	—	—	—	(105)	(105)
Disposals	—	199	16	—	215
Balance at 31 December 2010	(138)	(313)	(23)	(10,786)	(11,260)
Depreciation expense	(5)	(65)	(4)	(2,880)	(2,954)
Impairment ⁽ⁱ⁾	—	—	—	743	743
Disposals	7	11	2	—	20
Balance at 31 December 2011	(136)	(367)	(25)	(12,923)	(13,451)

Net	Vehicles	Equipment	Other	Drilling & Exploration Equipment	Total
	<i>\$(000)</i>	<i>\$(000)</i>	<i>\$(000)</i>	<i>\$(000)</i>	<i>\$(000)</i>
Balance at 1 January 2010	34	338	84	18,084	18,540
Balance at 31 December 2010	5	105	29	15,032	15,171
Balance at 31 December 2011	0	53	23	14,534	14,610

⁽ⁱ⁾ The Group recorded \$105,000 as impairment of exploration works for the license 3104 Tsimiroro during 2010. A 2008 impairment of camp costs of \$743,000 for the license 3104 Tsimiroro was reversed in 2011 due to the restoration and refurbishment of the camp in 2011 for use in upcoming pilot projects.

16. EXPLORATION AND EVALUATION ASSETS

During the Exploration Period of the existing Production Sharing Contracts the Group considers as intangible assets:

- The exploration works performed in the licenses 3102 Bemolanga, 3104 Tsimiroro, 3105 Manambolo, 3106 Morondava and 3107 Manandaza
- The consumable costs included in the pilot project costs implemented in the license 3104 Tsimiroro

During the Exploration Period of the Production Sharing Contracts the Group considers as tangible assets the capital costs included in the licenses.

Cost	Total
	<i>\$(000)</i>
Balance at 1 January 2010	70,857
Movements	12,398
Capitalization of depreciation	2,932
Asset retirement discount ⁽ⁱⁱⁱ⁾	(357)
Balance at 31 December 2010	85,830
Movements	15,167
Capitalization of depreciation	2,880
Asset retirement costs	207
Asset retirement discount ⁽ⁱⁱⁱ⁾	(113)
Balance at 31 December 2011	103,971

The detail of the exploration works by license as explained in Note 1 is:

<i>As of 31 December</i>	2011	2010
	<i>\$(000)</i>	<i>\$(000)</i>
License 3102 Bemolanga (operated by TOTAL) ⁽ⁱⁱ⁾	—	—
License 3104 Tsimiroro (operated)	94,869	76,978
Environmental assessment	1,392	872
Pilot project	66,508	56,973
Studies and other exploration expenses	8,823	6,039
Exploration wells	5,593	3,514
E&E capitalization of depreciation	12,816	9,937
Asset retirement costs	207	—
Asset retirement discount ⁽ⁱⁱⁱ⁾	(470)	(357)
License 3105 Manambolo (operated)	2,692	2,606
Geochemistry	344	344
Environmental assessment	95	95
Studies and other exploration expenses	1,178	1,092
Seismic acquisition	1,075	1,075
Impairment ⁽ⁱ⁾	—	—
License 3106 Morondava (operated)	3,318	3,235
Environmental assessment	148	148
Geochemistry	380	380
Seismic acquisitions	1,104	1,104
Rock physics	199	199
Studies and other exploration expenses	1,484	1,402
E&E capitalization of depreciation	3	2
Impairment ⁽ⁱ⁾	—	—
License 3107 Manandaza (operated)	3,092	3,011
Airborne magnetic	214	214
Environmental assessment	132	132
Seismic acquisitions	1,241	1,241
Rock physics	198	198
Studies and other exploration expenses	1,307	1,226
Impairment ⁽ⁱ⁾	—	—
Total of exploration works	103,971	85,830

⁽ⁱ⁾ Management reversed the 2008 impairment of these assets in accordance with decisions of the Board made in 2009 and instead to pursue additional work in these blocks in 2009, 2010 and 2011.

⁽ⁱⁱ⁾ All historical costs related to the Bemolanga block were recovered through the sale of 60% of the interest to TOTAL in 2008.

⁽ⁱⁱⁱ⁾ The Company recorded a discount on the provision for the retirement of wells of \$113,000 in 2011 and \$357,000 in 2010.

The Group has the intention to continue to operate Tsimiroro block and has no reason to believe that any impairment other than the impairment related to the VSAT equipment that is provided in property, plant and equipment should be considered on the related Tsimiroro assets recorded by the Company.

Management believes that it is not currently necessary to record any impairment charge on the exploration and evaluation assets for license blocks 3105, 3106 and 3107, and that they are properly reflected in the Company's financial statements. Management believes that there is no basis on which the Madagascar Government can make any adverse claim against the Group regarding its exploration blocks. In addition, the Government and the Group have successfully addressed the Tsimiroro and Bemolanga Blocks in 2011 which evidences a willingness on the part of the Madagascar Government to resolve outstanding delays. Finally the Madagascar Government has never formally articulated any position in writing that is hostile to the Group. During 2011, technical teams have met and approved the proposed work programmes on the exploration blocks.

17. OTHER INTANGIBLE ASSETS

Cost	Software
	\$(000)
Balance at 1 January 2010	869
Additions	—
Disposals	(33)
Balance at 31 December 2010	836
Additions	178
Disposals	(90)
Balance at 31 December 2011	924

Accumulated Amortisation	Software
	\$(000)
Balance at 1 January 2010	(499)
Depreciation expense	(186)
Disposals	21
Balance at 31 December 2010	(664)
Depreciation expense	(125)
Impairment ⁽ⁱ⁾	(34)
Disposals	74
Balance at 31 December 2011	(749)

Net	Software
	\$(000)
Balance at 1 January 2010	370
Balance at 31 December 2010	172
Balance at 31 December 2011	175

⁽ⁱ⁾ The Group recorded \$34,000 as impairment on software in 2011.

18. JOINT VENTURE OPERATIONS

License 3102 Bemolanga

Since 17 September 2008 the Group has held a 40% interest in a joint venture with the group TOTAL for the license 3102 Bemolanga. Under the farm-out agreement TOTAL has become the operator.

The Group is entitled to a proportionate share of the rental income received and bears a proportionate share of the expenses. All expenditures through 2011 were carried by the operator.

License 3109 Mandabe

Majunga and Tullow were 50/50 parties to a joint operating agreement dated 7 December 2005 for Production Sharing Contract No. 3109 (the "Tullow JOA"). In January 2011, Majunga S.A.R.L., a subsidiary of Madagascar Oil Ltd., entered into a settlement agreement with Tullow Madagascar Limited, a subsidiary of Tullow, covering their joint operating agreement for Block 3109 (Mandabe), of which Tullow was the operator. Majunga had withdrawn from the Mandabe block in September 2008. Under the settlement agreement, Majunga paid Tullow approximately US\$127,000, which reflected Majunga's share of costs incurred for joint operations prior to its withdrawal. As part of the settlement agreement, the parties entered into mutual releases in connection with the joint operations.

The following amounts are included in the consolidated financial statements as a result of the share of the Group in the joint venture operations:

<i>Year Ended 31 December</i>	2011	2010
	<i>\$(000)</i>	<i>\$(000)</i>
Current liability (Note 25)	(71)	(140)
Expenses	(90)	(29)

19. OTHER ASSETS

Prepayments correspond to payments made to OMNIS as per Production Sharing Contracts signed for periods covering 2011 and 2010, down payments to suppliers, and payments for insurance policies.

20. FINANCIAL ASSETS

Deposits are for the rental of offices and equipment.

21. CASH AND CASH EQUIVALENTS

For the purposes of the cash flow statement, cash and cash equivalents include cash on hand and in banks and investments in time deposits, net of outstanding bank overdrafts. Cash and cash equivalents at the end of the financial year as shown in the cash flow statement can be reconciled to the related items in the statement of financial position as follows:

<i>As of 31 December</i>	2011	2010
	<i>\$(000)</i>	<i>\$(000)</i>
Cash and bank balances	43,019	69,288
Restricted cash ⁽ⁱ⁾	(2,560)	(1,765)
Net cash available	40,459	67,523

⁽ⁱ⁾Cash collateral of \$1,765,000 in 2011 and 2010, corresponds to 111% of guarantees provided by the bank on the behalf of the Group. See Note 30 Commitments for expenditure – bank guarantees for more details about the guarantees provided. In 2011 the Company reserved \$795,000 in a segregated account to continue the appeals process on disputed VAT taxes. (See Note 33)

22. ISSUED CAPITAL

The Group manages its capital to ensure that entities in the Group will be able to continue as a going concern while maximizing the return to stockholders through the optimization of the debt and equity balance. The Group's overall strategy remains unchanged from 2010.

The capital structure of the Group consists of debt (when any), cash and cash equivalents and equity attributable to equity holders of the parent, comprising issued capital, reserves and accumulated deficit as disclosed in Notes 22, 23 and 27 respectively.

The gearing ratio at the year-end was as follows:

<i>As of 31 December</i>	2011	2010
	<i>\$(000)</i>	<i>\$(000)</i>
Debt ⁽ⁱ⁾	—	—
Cash and cash equivalents ⁽ⁱⁱ⁾	(40,459)	(67,523)
Net debt	(40,459)	(67,523)
Equity ⁽ⁱⁱⁱ⁾	160,418	170,569
Net debt to equity ratio	—%	—%

⁽ⁱ⁾ Debt is defined as long- and short-term borrowings from financial institutions.

⁽ⁱⁱ⁾ Only non-restricted cash and cash equivalents.

⁽ⁱⁱⁱ⁾ Equity includes all capital and reserves of the Group including accumulated deficit.

In 2009 the Company completed a consolidation of its stock of 1:100. All share, option and warrant amounts, prices and fair values have been adjusted retrospectively accordingly. In 2010 the Company completed a 10:1 stock split. All share, option and warrant amounts, prices and fair values have been adjusted retrospectively accordingly.

In August 2010, the Company issued Blakeney LLP 6,666,670 common shares at a price of \$1.50 per share for an aggregate price of \$10,000,005. The Company raised funds from the Blakeney financing for general corporate purposes.

On 29 November 2010, the Company's common shares were admitted for listing on the Alternative Investment Market ("AIM") of the London Stock Exchange. The Company's common shares trade on the exchange through depository interests under the AIM symbol "MOIL". In its initial public offering ("IPO") the Company issued and sold 53,197,000 shares at 95 pence per share for total gross proceeds to the Company of \$78.3 million. Net proceeds to the Company after payment of IPO related expenses were \$70.4 million. At the time of admission, the Company's total outstanding share capital was 192,365,157 shares. The Company incurred \$7.9 million in IPO related costs of which \$5.1 million is offset against the share premium.

Details of the Share Capital of the Company as of 31 December 2011 and 2010 are:

<i>As of 31 December</i>	2011	2010
Total number of shares authorised (post 2010 split)	1,200,000,000	1,200,000,000
Fully paid common shares	196,668,467	196,365,157
Fully paid non-voting shares	—	—
Total number of shares fully paid	196,668,467	196,365,157
Par value per share in USD	0.001	0.001

<i>As of 31 December</i>	2011	2010
	<i>\$(000)</i>	<i>\$(000)</i>
Share capital	197	197
Share premium	194,890	194,890
Total issued capital	195,087	195,087



	Number of Shares	Share Capital \$(000)	Share Premium \$(000)
Balance, 1 January 2010	131,698,270	131	111,288
Issue of shares	60,119,967	60	83,597
Shares issued - conversion of debt and warrants	2,443,620	3	5
Shares granted to personnel for free (Note 27)	1,003,300	2	—
Shares granted to Directors for free (Note 27)	1,100,000	1	—
Balance, 31 December 2010	196,365,157	197	194,890
Shares granted to personnel for free (Note 27)	300,000	—	—
Shares issued - conversion of debt (Note 26)	3,310	—	—
Balance, 31 December 2011	196,668,467	197	194,890

In 2010, all 13 million of the Company's non-voting shares were converted into voting shares. Approximately 5.6 million non-voting shares, held by existing shareholders, were exchanged for voting shares under the terms of contractual agreements between the Company and the holders of such shares. Approximately 7.4 million non-voting shares automatically converted, pursuant to their terms, into voting shares when they were sold to other shareholders.

At 31 December 2011 the detail of financial instruments in issue is:

Total number of warrants in issue		1,420,060
Warrants at \$15 per share	30,000	
Warrants at \$10 per share	1,390,060	
Total number of options in issue		7,725,788
Options at \$13 per share	60,000	
Options at \$10 per share	100,000	
Options at .95 GBP per share	1,565,788	
Options at .50 GBP per share	6,000,000	

The valuation of the warrants and options granted is described in Note 27 Share-based payments except:

1.3 million warrants granted to shareholders in connection with equity investment in the Company: Under IAS 32.22 these warrants are an equity instrument booked for its selling value at its grant date which is zero. Because these warrants are equity instruments their change in fair value over time is not recognised in the financial statements.

23. ACCUMULATED DEFICIT AND DIVIDENDS

Year Ended 31 December	2011 \$(000)	2010 \$(000)
Balance at beginning of the year	(27,567)	(156,540)
Transfer of equity settled transaction reserve	1,676	140,547
Net loss	(13,248)	(11,574)
	(39,139)	(27,567)

Since its creation no member of the Group has proposed, declared or distributed any dividend.

24. PROVISIONS

	Current \$(000)	Non-Current \$(000)
Employee Benefits ⁽ⁱ⁾		
Balance at 31 December 2010	50	—
Increase in vacation provision	28	—
Balance at 31 December 2011	78	—
Decommissioning costs ⁽ⁱⁱ⁾		
Balance at 31 December 2010	—	246
Asset retirement costs	—	207
Asset retirement discount	—	(112)
Balance at 31 December 2011	—	341
Tax settlement ⁽ⁱⁱⁱ⁾		
Balance at 31 December 2010	—	—
Tax settlement provision	1,000	—
Balance at 31 December 2011	1,000	—
	1,078	341

(i) Provision for employee benefits represents annual leave accrued.

(ii) The provision for decommissioning costs represents management's best estimate for the plugging and abandonment costs associated with the core holes drilled to date on the license 3102 Bemolanga, with the cores holes, the cyclical steam simulation (CSS) wells and the exploration wells drilled to date on the license 3104 Tsimiroro and with the production facilities installed in relation with the production test conducted on the license 3104 Tsimiroro.

(iii) Provision for settlement of value added taxes. No discount is recorded on the tax provision. (See discussion in footnote 33)

25. TRADE AND OTHER PAYABLES

<i>As of 31 December</i>	2011	2010
	\$(000)	\$(000)
Trade payables ⁽ⁱ⁾	4,008	2,358
Other payables ⁽ⁱⁱ⁾	1,287	182
Partner operator ⁽ⁱⁱⁱ⁾	71	260
	5,366	2,800

(i) Trade payables include Malagasy suppliers for US \$1,451,000 and \$2,256,000 and non-Malagasy suppliers for US \$1,546,000 and \$189,000 as of 31 December 2011 and 2010 respectively.

(ii) Other payables include compensation due to personnel and other taxes.

(iii) Amount due to TOTAL and Tullow under the joint venture agreements in place at year end.

26. DEBT

In July and August 2010, the Company offered 12% convertible notes due 31 December 2010 to its shareholders to fund operations during the second half of 2010 in contemplation of a strategic transaction. Investor groups led by the Company's three largest shareholders (Grafton Resource Investments Limited, Touradji Capital Management LP and Persistency Capital) subscribed for \$2,868,453 of notes with other shareholders subscribing for an aggregate of \$4,903. The notes were convertible at a conversion price of \$15.00 (\$1.50 on a post 2010 split).

The notes were subject to mandatory prepayment upon aggregate financing by the Company during 2010 exceeding US\$75 million or upon consummation of a merger or similar strategic transaction. Purchasers of the notes received 718,370 warrants with a term of one year in an amount equal to fifty per cent of the principal amount of the notes. The warrants have a strike price of \$20.00 per common share (\$2.00 per share on a post 2010 split). The Company recognised \$144K in expense due to the warrants in 2010.

Total notes in principal amount of \$2,873,356 were issued. \$4,903 of the notes were converted into 3,310 shares. The remainder of the notes were paid in full with proceeds from the Company's initial public offering.

The Company has no outstanding debt at year-end 2011.

27. SHARE-BASED PAYMENTS

All amounts stated are after consideration of the Company's 10:1 stock split which took place in 2010.

Credit Suisse Agreement

In July 2009, the Company issued Credit Suisse International 6,135,771 common shares in settlement of a dispute over whether certain share issuances during 2008 constituted dilutive events under Credit Suisse's warrant agreement. In November 2010 Credit Suisse exercised outstanding warrants for 2,440,310 common shares. The expense recognised related to the 2010 exercised warrants was \$240,600 due to the modification of the exercise price from \$1.00 to \$.001 per share.

Bank Julius Baer Agreement

In November 2010, the Company issued Bank Julius Baer & Co. 333,330 common shares at a price of \$1.50 per share for an aggregate value of \$499,995 for services rendered in connection with the Blakeney financing (Note 23).

Stock Options Granted to Management and Employees

The Group issued several stock options in 2006 and 2007 but no options were granted in 2008 and 2009. In 2010 the Group issued 1,565,788 stock options to its Chairman and CEO, Chief Operating Officer, and Non-Executive Directors in conjunction with its IPO. In 2011 the Group issued 6,000,000 options to its Chairman and CEO, Chief Operating Officer and certain employees. The main characteristic of the options are summarised in the following table:

Option	Grant Dates	Exercise Price	First Exercise Date	Last Exercise Date	Estimated Fair Value of Option	Options Granted	Options Cancelled	Options Exercised	Outstanding Options
SO2	27/03/2006	13 USD	27/03/2006	27/03/2012	6 USD	120,000	(60,000)	0	60,000
SO8	15/06/2006	15 USD	15/06/2007	14/06/2011	5 USD	35,000	(35,000)	0	0
SO9	17/07/2007	10 USD	17/07/2007	17/07/2010	3 USD	10,000	(10,000)	0	0
SO10	27/07/2007	10 USD	27/07/2008	27/07/2017	5 USD	100,000	0	0	100,000
SO11	18/11/2010	.95 GBP	29/11/2011	18/11/2015	0.62 USD	1,250,000	0	0	1,250,000
SO12	18/11/2010	.95 GBP	29/11/2011	18/11/2020	0.90 USD	315,788	0	0	315,788
SO13	30/06/2011	.50 GBP	30/06/2012	30/06/2017	0.17 USD	4,000,000	0	0	4,000,000
SO14	30/06/2011	.50 GBP	31/12/2012	30/06/2017	0.17 USD	2,000,000	0	0	2,000,000

Plans SO2 and SO8 were partially surrendered in 2007. Plan SO9 expired in 2010. Plan SO8 expired in 2011. No options were exercised in 2010 or 2011.

In order to determine the fair value of each option granted, the following parameters were considered:

- Share prices at grant date were determined based on the last known share price for capital increase. 2011 options were valued on a trading price of .345 GBP at the date of grant. 2010 options were valued on the initial public offering price of .95 GBP.
- Volatility was estimated based on a suitable peer group of companies listed in the AIM market of the London exchange. This analysis led to volatility estimate of 46%
- Risk free rates based on US government bonds for the option term No forfeiture rate was recognised
- No expected dividends were considered



The expense recognised related to outstanding stock options plans granted to management and employees was \$41,595 in 2010 and \$963,677 in 2011.

The weighted average exercise price at 31 December 2011 was \$11.23 for USD options and for .65 GBP options (2010: \$11.35 and .95 GBP).

The weighted average fair value for options at 31 December 2011 was \$0.50 (2010: \$2.77).

Shares granted to management and employees

The Group granted restricted shares in 2006, 2007, 2008, 2009, 2010 and 2011. The main features of the plans are summarised in the following table.

Plan	Grant Dates	Vested Date	Estimated Fair Value of Shares	Shares Granted	Shares Cancelled	Shares Vested	Shares Non-Vested or Locked
S1	27/07/2006	31/12/2006	15 USD	70,000	0	70,000	0
S1	27/07/2006	27/07/2007	15 USD	100,000	0	100,000	0
S1	27/07/2006	27/07/2009	15 USD	100,000	0	100,000	0
S2	18/12/2006	31/12/2006	17.5 USD	26,230	0	26,230	0
S2	18/12/2006	31/12/2007	17.5 USD	26,230	(10,260)	15,970	0
S2	18/12/2006	31/12/2008	17.5 USD	26,230	(14,770)	11,460	0
S3	07/02/2007	29/11/2010	10 USD	675,000	(157,500)	517,500	0
S4	19/01/2007	19/01/2007	10 USD	25,005	0	25,005	0
S5	28/02/2007	28/02/2007	10 USD	16,888	0	16,888	0
S6	11/05/2007	11/05/2007	10 USD	6,667	0	6,667	0
S7	01/06/2007	01/06/2007	10 USD	10,000	0	10,000	0
S8	16/08/2007	16/08/2007	10 USD	15,000	0	15,000	0
S11	01/06/2007	01/06/2007	10 USD	20,000	(10,000)	10,000	0
S12	27/11/2007	27/11/2007	4 USD	33,330	0	33,330	0
S13	05/11/2007	05/11/2009	4 USD	25,000	0	25,000	0
S15	18/01/2008	18/01/2011	4 USD	568,820	(97,980)	470,840	0
S16	07/08/2008	07/08/2011	1 USD	5,947,250	(714,588)	5,232,662	0
S17	07/10/2008	07/10/2008	.2 USD	65,000	0	65,000	0
S18	10/07/2008	10/07/2011	1 USD	60,513	(60,513)	0	0
S19	22/02/2008	22/02/2008	4 USD	3,000	0	3,000	0
S20	16/07/2008	16/07/2008	1 USD	3,675	0	3,675	0
S20	16/07/2008	16/07/2011	1 USD	22,500	(22,500)	0	0
S21	14/10/2008	14/10/2011	.2 USD	1,000,000	0	700,000	300,000
S22	28/10/2008	28/10/2009	.2 USD	1,500,000	0	1,500,000	0
S23	31/12/2008	31/12/2008	.2 USD	49,080	0	49,080	0
S24	20/01/2009	20/01/2012	.2 USD	1,375,000	0	1,375,000	0
S25	19/06/2009	19/06/2010	.5 USD	500,000	0	500,000	0
S26	18/12/2009	29/11/2010	.5 USD	548,000	0	348,000	200,000
S27	18/11/2010	29/01/2011	1.5 USD	20,000	0	20,000	0
S28	18/11/2010	29/01/2011	1.5 USD	300,000	0	300,000	0
S29	18/11/2010	28/02/2012	1.5 USD	780,000	0	780,000	0
S30	18/11/2010	02/01/2012	1.5 USD	100,000	0	0	100,000
S31	18/11/2010	02/01/2012	1.5 USD	666,670	0	0	666,670
S31	18/11/2010	29/11/2013	1.5 USD	333,330	0	0	333,330
S32	01/08/2011	01/08/2012	.57 USD	100,000	0	100,000	0
S32	01/08/2011	01/08/2013	.57 USD	100,000	0	0	100,000
S32	01/08/2011	01/08/2014	.57 USD	100,000	0	0	100,000

The Group granted restricted shares to Management (plan S1), on 27 July 2006: 270,000 shares were granted at a per share value of USD 15 (post 2010 split). Of these, 70,000 vested in 2006, 100,000 in July 2007 and 100,000 vested in July 2009. Share price at grant date was determined based on the last known share price for capital increase.

The Group also granted a total of 78,690 shares (plan S2) to some employees on 18 December 2006 as a bonus for the year 2006. The share price at grant date was determined based on the managements' best estimate of fair value. These shares vested by third until 31 December 2008.

Some options (780,000) and warrants (120,000) granted in 2006 (post 2010 split) were surrendered in 2007 and replaced by restricted shares (plan S3) vested at the Company's admission date to a recognised stock exchange. The share price at grant date was determined based on management best estimate of fair value. The total fair value of options and warrants surrendered and the increase in fair value for the restricted shares granted were recognised at the date of surrender.

Other shares (plans S4 to S14) were granted in 2007 to management and employees: The fair value of these plans was determined based on the estimated share price at grant date.

Plans S15 to S23 were granted in 2008: some plans vested at grant date, others were due to vest after 3 years. Furthermore, several beneficiaries left the Company as "good leavers" under the plan, thus they vested immediately. Vesting of certain shares in Plans S15, S16 and S21 were locked-in for 60 days at the November 2010 IPO. At 31 December 2011 300,000 shares in Plan S21 were locked until January 2012.

Plans S24 to S26 were granted in 2009. Vesting periods ranged from one to three years with certain shares vesting upon an initial public offering or a change of control. Vesting of certain shares in Plan S26 were locked-in for 60 days at the November 2010 IPO. At 31 December 2011 200,000 shares in Plan S26 were locked until January 2012.

Plans S27 to S31 were granted in 2010. Vesting periods ranged from one to three years with certain shares vesting upon an initial public offering or a change of control. Vesting of certain shares in Plan S27 and S28 were locked-in for 60 days at the November 2010 IPO. At 31 December 2011 1,100,000 shares in Plans S30 and S31 were locked until January 2012.

Plan S32 was granted in 2011. Vesting of one-third of the shares was effective 31 December 2011 with the remaining shares vesting over the next two years. These shares were valued based on the trading price of .35 GBP at date of grant.

The expense recognised in the 2010 and 2011 consolidated statement of operations related to shares granted to management and employees is \$1.3 million and \$2.1 million, respectively. During 2010 and 2011, the Company reclassified certain amounts within the equity accounts in order to reflect only unvested restricted shares, warrants and options in the equity settled transaction reserve account.

The weighted average fair value for restricted shares at 31 December 2011 was \$1.08 (2010: \$0.74).

Warrants plans issued to management

The Group issued several warrants in 2006 and 2007 but no warrants were issued in 2008, 2009, 2010 or 2011. The primary terms of such warrants are summarised in the following table:

Plan	Grant Dates	Exercise Price	First Exercise Date	Last Exercise Date	Estimated Fair Value of Warrant	Warrants Granted	Warrants Cancelled	Warrants Exercised	Outstanding Warrants
W2	15/06/2006	13 USD	15/06/2006	15/06/2012	6 USD	30,000	0	0	30,000
W6	30/06/2007	10 USD	30/06/2007	30/06/2012	3 USD	40,020	0	0	40,020

No warrants were exercised in 2008, 2009, 2010 or 2011.

In order to determine the fair value of each warrant granted, following parameters were considered:

- Share prices at grant date were determined based on the last known share price for capital increase. Warrants issued in 2010 were valued based on \$.20 at the date of grant.
- Volatility was estimated based on a suitable peer group of companies listed in the AIM market of the London exchange. This analysis led to volatility estimate of 46%
- Risk free rates based on US government bonds
- No forfeiture rate was considered
- No expected dividends were considered

No expense was recognised in 2010 or 2011.

The weighted average exercise price for warrants at 31 December 2011 was \$8.39 (2010: \$8.51).

The weighted average fair value for warrants at 31 December 2011 was \$0.06 (2010: \$0.25).

Other Share Based Payments

The Group issued in 2007 and 2010 equity instruments (warrants and options) for the payment of goods and services to financial institutions and debt holders. In 2010, 2,440,300 of previously issued warrants held by the Credit Suisse consortium were converted into common shares. In 2011 the warrants issued under plan TP8 expired. Main features of the plans are summarised in the following table:

Plan	Grant Dates	Number of Options and Warrants	Exercise Price	First Exercise Date	Last Exercise Date	Estimated Fair Value of Warrant	Options and Warrants Cancelled	Options and Warrants Exercised	Outstanding Options and Warrants
TP7	28/03/2007	2,440,300	.001 USD	28/03/2007	03/28/2012	4 USD	0	2,440,300	0
TP8	15/07/2010	718,370	2 USD	15/07/2010	07/15/2011	0.2 USD	718,370	0	0

For plans TP7 and TP8, the fair value was determined based on a lattice model using the assumptions applied for options and warrants granted to management and employees.

In 2010 the finance expense recognised related to the modification of the Credit Suisse exercised warrants and the warrants issued with convertible debt equaled \$240,600 and \$143,674, respectively. No expense was recorded in 2011 related to share based payments granted to third parties.

28. RELATED PARTY TRANSACTIONS

Transactions between the Company and its subsidiaries which are related parties of the Company have been eliminated on consolidation and are not disclosed in this note. Details of transactions between the Company and other related parties are disclosed below.

Trading Transactions

During the years ended 31 December 2011 and 2010, Group entities entered into the following trading transactions with related parties that are not members of the Group:

Party	Transaction/Contract	Term	2011 Payments in USD \$(000)	2010 Payments in USD \$(000)
Laurie Hunter – Fees and Salary	Board Acceptance Letter	28/10/2008 to Present	—	259
Laurie Hunter – Business Expenses	Board Acceptance Letter	28/10/2008 to Present	—	206
Gene Davis-Pirinate Consulting ⁽ⁱ⁾	Consulting Agreement	28/10/2008 to 30/04/10	—	60
Ian Barby	Board Acceptance Letter	19/10/2010 to Present	67	12
John van der Welle	Board Acceptance Letter	06/11/2010 to Present	79	10
Colin Orr-Ewing	Board Acceptance Letter	19/10/2010 to Present	58	11
Andrew Morris	Board Acceptance Letter	Present	64	11
Gil Melman	Consulting Agreement	On request	70	—
Gil Melman-Selman Munson & Lerner	Selman Munson	On request	—	527
Jim Collins ⁽ⁱ⁾	Consulting Agreement	On request	323	268
Jim Dorman-Dtex ⁽ⁱ⁾	Consulting Agreement	On request	4	71
Jim Lederhos ⁽ⁱ⁾	Consulting Agreement	On request	206	155
Tim Whitacre-Red Moose Resources ⁽ⁱ⁾	Consulting Agreement	On request	255	—
Tim Whitacre-Red Moose Resources, Business Expenses ⁽ⁱ⁾	Consulting Agreement	On request	51	—
Mark Weller – Fees and Salary	Consulting Agreement	On request	—	416
Mark Weller – Business Expenses			—	106
Matthew Meyer ⁽ⁱ⁾	Consulting Agreement	On request	46	38
Seth Fagelman-Fees and Business Expenses	Consulting Agreement	On request	302	156

⁽ⁱ⁾ Member of operations personnel.

Amounts listed above include reimbursed business expenses and fees for services provided under the contract by individuals other than the identified related party. Fees payable to Mr. Melman in 2010 include legal fees paid to Mr. Melman's firm for additional work by other attorneys in connection with the IPO. Outstanding amounts are unsecured. No guarantees have been given or received. No expense has been recognised in the period for bad or doubtful debts in respect of the amounts owed to related parties.

Compensation of Key Management Personnel

Key management personnel of the Group is composed of the Chairman and Chief Executive Officer, the Chief Financial Officer, the Chief Operating Officer, General Counsel and the members of the Board.

The remuneration of directors and other members of key management during the year was as follows:

<i>Years Ended 31 December</i>	2011	2010
	<i>\$(000)</i>	<i>\$(000)</i>
Board fees	247	44
Service fees	277	813
Salaries	1,106	68
Bonuses	1,226	10
Share-based payments	2,301	419
	5,157	1,354

29. OPERATING LEASE ARRANGEMENTS

Leasing Arrangements

Operating leases relate to:

- Office facilities and equipments with lease terms not over 5 years with options to renew for up to 5 years
- Housing facilities and equipments for expatriates with lease terms not over 1 year with monthly renewal options
- Air charter with lease term not over 1 year with option for annual renewal

All operating lease contracts contain market review clauses in the event that the Company exercises its option to renew. The Company does not have an option to purchase the leased assets at the expiry of the lease period.

Payments recognised as an expense

<i>For the years ended 31 December</i>	2011	2010
	<i>\$(000)</i>	<i>\$(000)</i>
Minimum lease payments	276	151

Non-cancellable operating lease commitments

<i>As of 31 December</i>	2011	2010
	<i>\$(000)</i>	<i>\$(000)</i>
Not longer than 1 year	263	54
Longer than 1 year and not longer than 5 years	25	83
	288	137

The Group has no contingent rentals and does not receive any sublease payments as of 31 December 2011 & 2010.

30. COMMITMENTS FOR EXPENDITURE

Commitments

The Group has no commitment for expenditures with any of its consultants and advisors except in the case of fund raising (equity and debt) for which agreements have been signed with its usual financial institution advisor and other intermediaries.

Except for the finance lease and the operating leases mentioned in this document, the Group has no other multi-year commitment with private companies that are not cancelable within a twelve month period.

The Production Sharing Contracts signed with the Malagasy authorities with respect to blocks 3015, 3106 and 3107 state that the Group is obligated to drill an exploratory test well and perform additional seismic work (if needed) at each of the sites before 31 December 2011. Approvals of the requisite extensions are pending as discussed in Note 33. As of 31 December 2011 both the financial and physical obligations for license 3104 Tsimiroro had been fulfilled. The contracts include the following annual fees:

- Administrative fees
 - * Licenses 3102 (no longer operated since 17 September 2008) and 3104: \$250,000 per year per license as of second phase of Exploration Period only during Exploration Period
 - * Other operated licenses: \$162,500 per year per license only during Exploration Period
- Training fees
 - * Licenses 3102 and 3104: \$100,000 per year for the life of the contract
 - * All other licenses: \$50,000 per year for the life of the contract

Bank Guarantees

A bank guarantee exists in favor of OMNIS in respect of the Group's obligation for the execution of the minimum exploration works as under the terms of the Production Sharing Contracts.

Expiration Date	Guarantor	Beneficiary	In Force at 31 December 2011
1 June 2012	Madagascar Oil Ltd (Bermuda)	OMNIS	\$1,500,000
			\$1,500,000

These guarantees are subject to forfeiture in certain circumstances if the Group does not fulfill its minimum work obligations.

31. FINANCIAL INSTRUMENTS

(A) Fair Value of Financial Instruments

Recognition and measurement principles regarding financial assets and liabilities are defined in IAS 32 and IAS 39. The classification of financial instruments into specific categories is described in Note 2.

	2010 Carrying Amount	Amortized Cost	Loans and Receivables	Cash at Bank	2010 Fair Value
Assets	\$(000)	\$(000)	\$(000)	\$(000)	\$(000)
Non-current financial assets	16	—	16	—	16
Restricted cash	1,765	—	—	1,765	1,765
Current financial assets	—	—	—	—	—
Cash and cash equivalents	67,523	—	—	67,523	67,523
Liabilities					
Accounts and other payables	2,800	2,800	—	—	2,800
	2011 Carrying Amount	Amortized Cost	Loans and Receivables	Cash at Bank	2011 Fair Value
Assets	\$(000)	\$(000)	\$(000)	\$(000)	\$(000)
Non-current financial assets	18	—	18	—	18
Restricted cash	2,560	—	—	2,560	2,560
Current financial assets	—	—	—	—	—
Cash and cash equivalents	40,459	—	—	40,459	40,459
Liabilities					
Accounts and other payables	5,366	5,366	—	—	5,366

**(B) Risk Management Policy**

In the context of its business activity, the Group operates in an international environment in which it is confronted with market risks, specifically foreign currency risk and interest rate risk. It does not use derivatives to manage and reduce its exposure to changes in foreign exchange rates and interest rates.

Cash and cash equivalents are kept in the Group's functional currency except for an amount corresponding to the needs of the local subsidiaries. The policy of the Group is to have a balance in the currency of the local subsidiaries not higher than the expected needs in local currency for one month.

In addition to market risks, the Group is also exposed to liquidity risk and financial instrument counterparty risk.

Exposure to foreign currency risk

The Group has a very limited exposure to foreign exchange risk arising from transactions in currencies other than its functional currency since such transactions are either not material or very short term transactions.

Based on notional amounts, most of the Group's net exposure to foreign currency risk arises on the following currencies (excluding entities functional currencies):

As of 31 December 2010	USD	GBP	CAD	EUR	MGA	2010
	\$(000)	\$(000)	\$(000)	\$(000)	\$(000)	\$(000)
Financial Assets	—	—	—	—	16	16
Restricted cash equivalents	1,765	—	—	—	—	1,765
Cash	67,357	89	—	—	77	67,523
Exposure (Assets)	69,122	89	—	—	93	69,304
Trade and other payables	2,046	—	46	—	708	2,800
Exposure (Liability)	2,046	—	46	—	708	2,800
Gross exposure in statement of financial position	67,076	89	(46)	—	(615)	66,504
Forecasted disbursements	—	—	—	—	—	—
Forecasted sales	—	—	—	—	—	—
Net Exposure	67,076	89	(46)	—	(615)	66,504

As of 31 December 2011	USD	GBP	CAD	EUR	MGA	2011
	\$(000)	\$(000)	\$(000)	\$(000)	\$(000)	\$(000)
Financial Assets	—	—	—	—	18	18
Restricted cash equivalents	2,560	—	—	—	—	2,560
Cash	40,320	23	—	—	116	40,459
Exposure (Assets)	42,880	23	—	—	134	43,037
Trade and other payables	3,836	—	31	15	1,484	5,366
Exposure (Liability)	3,836	—	31	15	1,484	5,366
Gross exposure in statement of financial position	39,044	23	(31)	(15)	(1,350)	37,671
Forecasted disbursements	—	—	—	—	—	—
Forecasted sales	—	—	—	—	—	—
Net Exposure	39,044	23	(31)	(15)	(1,350)	37,671

Interest Rate Risk

Exposure to interest rate risk – Cash and cash equivalents are invested in short-term variable-rate instruments. There is no long-term debt at 31 December 2011.

Analysis of the sensitivity to interest rate risk – At 31 December 2011 100% of short-term investments is at variable rates.

Liquidity Risk

The Group aims to maximize operating cash flows in order to be in a position to finance the investments required for its development.

The Group's strategy also aims to ensure that it has the cash resources necessary to meet all circumstances. See discussion in Note 2.

Residual contractual maturities of financial liabilities can be analyzed as follows:

	2010	Less than 1 Year	1 to 5 Years	More than 5 years
	\$(000)	\$(000)	\$(000)	\$(000)
Non-derivatives	(2,800)	(2,800)	—	—
Credit facilities	—	—	—	—
Trade and other payables	(2,800)	(2,800)	—	—
Derivatives	—	—	—	—
Total	(2,800)	(2,800)	—	—

	2011	Less than 1 Year	1 to 5 Years	More than 5 years
	\$(000)	\$(000)	\$(000)	\$(000)
Non-derivatives	(5,366)	(5,366)	—	—
Credit facilities	—	—	—	—
Trade and other payables	(5,366)	(5,366)	—	—
Derivatives	—	—	—	—
Total	(5,366)	(5,366)	—	—

32. OIL ACTIVITY OPERATIONS

The Group recorded \$105K as an impairment of exploration works for the license 3104 Tsimiroro during 2010. A 2008 impairment of camp cost of \$743k for the license 3104 Tsimiroro was reversed in 2011.

33. CONTINGENT LIABILITIES AND CONTINGENT ASSETS

Dispute with Government of Madagascar

In June 2011, MOSA and OMNIS resolved their outstanding dispute on the Tsimiroro Block (3104), and MOSA has had its 2011-2012 annual work programme and budget for the Tsimiroro Block approved by the management committee. In addition, MOSA was able to obtain assurances from OMNIS as to the validity of the Tsimiroro production sharing contract and the potential for an extension of the contract term to address the delays caused by the force majeure event. In December 2011, the Tsimiroro management committee approved the work programme for the Steamflood pilot project and ratified the budget for 2012.

With respect to MOSA's three Exploration Blocks (blocks 3105, 3106 and 3107), MOSA has not been granted a management committee meeting since the dispute began in December 2010. The production sharing contracts for these blocks each require additional seismic work (if needed) and the drilling of one well in 2011. The Company intends to request an extension of the terms of these blocks to account for



the 2011 delay and for the additional time required to conduct the assessment of prospective drilling locations. The Company will continue to maintain the force majeure declaration and the claim in arbitration for these blocks until the dispute is resolved. Although management does not believe that the impact of these exploration blocks on the Company's business is material, a continued failure on the part of the government of Madagascar to allow MOSA to proceed under these production sharing contracts could have an adverse effect on the Company's assets.

The dispute with the Government of Madagascar over the Company's blocks stemmed from a 16 December 2010 meeting between the Company's management and the Minister of Mines and Hydrocarbons of the State of Madagascar in which he stated that Madagascar may be interested in acquiring MOSA's interest in the production sharing contracts for blocks 3104, 3105, 3106 and 3107 at a price based on historic costs. OMNIS cancelled the semi-annual management committee meeting that was to be held on 17 December 2010 and did not reschedule such meeting until 20 May 2011 (as discussed above). The Company had significantly curtailed operations and expenditures, pending resolution of these issues. On 21 March 2011, MOSA declared force majeure under production sharing contracts for the Tsimiroro Block (3104) (subsequently resolved as discussed above), and the Exploration Blocks (3105, 3106 and 3107) based on statements made by the Minister in December 2010 and OMNIS' failure to hold requisite management committee meetings for the blocks. On 29 April 2011, MOSA filed a request for arbitration under the rules of the International Chamber of Commerce ("ICC") for breach of contract under these production sharing contracts based on the government's lack of response to the force majeure declaration. Such request claimed, among other things, breach of contract based on the earlier actions by OMNIS and the Ministry of Mines and Hydrocarbons. Simultaneously the Company also submitted a notice of dispute to the government of Madagascar under the rules of the International Centre for Settlement of Investment Disputes ("ICSID") with regard to the government's threatened expropriation of the Company's assets.

There can be no assurance that MOSA will be granted the requisite extensions and approvals by OMNIS in a timely fashion in order to proceed with contemplated operations on the Exploration Blocks for 2012 or that OMNIS or the Government of Madagascar will not take actions in the future that are adverse to the Company's ownership of its assets and its ability to operate in the country.

Management believes that it is not currently necessary to record any impairment charge on the exploration and evaluation assets, and that they are properly reflected in the Company's financial statements. Management believes that there is no basis on which the Madagascar Government can make any adverse claim against the Group regarding the Exploration Blocks. In addition, the Government and the Group have successfully addressed the Tsimiroro and Bemolanga Blocks in 2011 which evidences a willingness on the part of the Madagascar Government to resolve outstanding delays. Finally the Madagascar Government has never formally articulated any position in writing that is hostile to the Group. During 2011, technical teams have met and approved the proposed work programmes on the exploration blocks.

Taxe Forfaitaire sur les Transferts (TFT)

During 2006 the Group received a notification from the Malagasy tax administration that it should apply the TFT to the services rendered by foreign suppliers. The Group believed that it was exempted from this tax as per applicable regulations. The Group challenged this interpretation of the Tax Administration which was contradicting the implementation of the TFT for many years and received confirmation in 2007 from the Minister of Finance that TFT was not applicable to petroleum industry transactions. Accordingly, TFT has been cancelled in subsequent Malagasy budgets.



In July 2010, the Group received a notification from the Malagasy Tax Administration claiming the payment of VAT and income tax on services rendered by foreign suppliers, with interests on delayed payment and penalties. The adjustments relate to fiscal year 2007 and 2008. The tax administration dismissed the claims on income tax in 2010, but maintained its position on the VAT adjustment. The amount claimed relating to VAT for 2007 and 2008 is US \$6,790K (consisting of VAT of US \$3,990K, interest on delayed payment of US \$980K and penalty of US \$1,820K).

The Group believes it complied with the applicable regulations and the practice of all oil companies in Madagascar. The Group has challenged the proposed tax adjustment through the appeals process at the Malagasy tax administration without success. In order to proceed with the appeals process, the Group was obligated to reserve, in a segregated account, \$795,000, reflecting its estimate of 50% of the claimed tax. In January 2012, the Group filed an appeal with the Counsel of State of Madagascar, which is the judiciary body responsible for hearing final appeals on tax matters. The Group has taken a \$1 million reserve based on management's estimate of the potential exposure. Management also continues to discuss with the Tax Administration options for an administrative settlement.

Efforts have been underway to modify the Madagascar Petroleum Code to clarify the Malagasy law to specifically exempt oil and gas development projects from incurring the disputed taxes. This effort appears to be on hold pending Madagascar elections and the appointment of an internationally recognized government. Management believes that the tax authority's position would be highly punitive to potential future industrial development and that the future government will be amenable to effecting the necessary changes, as the Company's disputed handling has been followed by all petroleum companies since 2006 and has never been previously challenged by the tax authority.

There can be no assurance that the Group will ultimately prevail in its appeal at the Counsel of State.

34. EVENTS AFTER REPORTING DATE

In January 2012, the Group filed an appeal with the Counsel of State of Madagascar pursuant to a required deadline for preserving its rights to appeal the Malagasy Tax Administration's claims for VAT due by the Group on foreign services rendered. See note 33.

In February 2012, the Company completed a US\$26.5 million placing of the Common Shares at 28 pence per share. The placing consisted of two tranches: 57.7 million shares were issued on 27 February 2012 and 2.2 million shares will be issued in March 2012 pending a special general meeting of the shareholders to approve the Board's additional authority for the issuance of the additional shares without pre-emptive rights.

35. APPROVAL OF FINANCIAL STATEMENTS

The financial statements were reviewed by the Audit Committee, approved by the Board of Directors and authorised for issue on 7 March 2012.



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