Iona Energy Inc.
Consolidated Financial Statements - Audited
For the years ended December 31, 2012 and 2011

Contents

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL STATEMENTS

The consolidated financial statements and accompanying notes to the consolidated financial statements are the responsibility of the management of the Company. The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS").

Preparation of consolidated financial statements is an integral part of management's broader responsibilities for the ongoing operations of the Company. Management maintains a system of internal accounting controls to ensure that properly approved transactions are accurately recorded on a timely basis and result in reliable consolidated financial statements.

The Board of Directors, through its Audit Committee, monitors management's financial and accounting policies and practices and the preparation of these consolidated financial statements. The Audit Committee meets periodically with external auditors and management to review the financial results and discharge their responsibilities. Specifically, the Audit Committee reviews with management and the external auditors the consolidated financial statements and related management discussion and analysis of the Company prior to submission to the Board of Directors for final approval. The external auditors have full and free access to the Audit Committee to discuss auditing and financial reporting matters.

The shareholders have appointed Deloitte LLP as external auditors of the Company and, in that capacity; they have examined the consolidated financial statements and the accompanying notes to the consolidated financial statements for the years ended December 31, 2012 and 2011. The Independent Auditor's Report to the shareholders follows.

"Neill Carson"
Neill Carson
President and CEO
April 25, 2013

"Graham Heath"
Graham Heath
Interim CFO

Deloitte.

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INDEPENDENT AUDITOR'S REPORT

To the Shareholders of Iona Energy Inc.:

We have audited the accompanying consolidated financial statements of Iona Energy Inc., which comprise the consolidated statements of financial position as at December 31, 2012 and December 31, 2011, and the consolidated statements of operations and comprehensive loss, consolidated statements of changes in shareholders' equity and consolidated statements of cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

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

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

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

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

Opinion
In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Iona Energy Inc. as at December 31, 2012 and December 31, 2011, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards.

Deloitte LLP

Chartered Accountants

April 29, 2013
Calgary, Canada

(In thousands of Canadian dollars)	Notes		December 31, 2012		December 31, 2011
ASSETS					
Current Assets					
Cash		$	**15,500**	$	41,608
Accounts receivable			**3,214**		388
Prepaid expenses			**1,266**		209
Restricted cash	6		**706**		1,293
Total Current Assets			**20,686**		43,498
Restricted cash	6		**9,052**		52
Deferred costs	7		**38,356**		315
Exploration and evaluation assets	7		**135,358**		28,235
Property and equipment	8		**71**		20
Total Non-Current Assets			**182,837**		28,622
Total Assets		$	**203,523**	$	72,120
LIABILITITES AND SHAREHOLDERS' EQUITY					
Current Liabilities					
Accounts payable and accrued liabilities		$	**55,406**	$	7,047
Total Current Liabilities			**55,406**		7,047
Non-Current Liabilities					
Decommissioning liabilities	9		**656**		170
Total Non-Current Liabilities			**656**		170
Total Liabilities			**56,062**		7,217
Shareholders' Equity					
Share capital	10		**155,985**		69,921
Contributed surplus			**6,183**		1,679
Accumulated other comprehensive income			**1,985**		(576)
Deficit			**(16,692)**		(6,121)
Total Shareholders' Equity			**147,461**		64,903
Total Liabilities and Shareholders' Equity		$	**203,523**	$	72,120

The accompanying notes are an integral part of these consolidated financial statements.

Approved by:

"Rod Maxwell"

Rod Maxwell
Director

Approved by:

"Neill Carson"

Neill A. Carson
Director

Iona Energy Inc.
Consolidated Statements of Operations and Comprehensive Loss

(In thousands of Canadian dollars, except for per share amounts)	Notes		Year Ended December 31 2012		Year Ended December 31 2011
Expenses					
General and administrative		$	**10,248**	$	4,800
Exploration and evaluation costs	**7**		**355**		545
Foreign exchange (gain)/loss			**152**		(241)
			10,755		5,104
Other item					
Finance income			**(184)**		(28)
Net loss for the year	**4**		**10,571**		5,076
Unrealized foreign exchange (gain)/ loss on net investments			**(2,561)**		576
Comprehensive loss for the year		$	**8,010**	$	5,652
Net loss per share - basic and diluted		$	**0.04**	$	0.04
Weighted average shares outstanding - basic and diluted (1)			**273,611,114**		117,795,863

(1) Options and warrants have been excluded from the diluted loss per share computation as they are anti-dilutive

The accompanying notes are an integral part of these consolidated financial statements.

(In thousands of Canadian dollars)	Notes	Share Capital	Contributed Surplus	Accumulated other Comprehensive Income	Deficit	Total Equity
Balance December 31, 2011		**$** 69,921	$ 1,679	$ (576)	$ (6,121)	$ 64,903
Net loss for the year		-	-	-	(10,571)	(10,571)
Share based payments		-	4,504	-	-	4,504
Foreign currency translation gain		-	-	2,561	-	2,561
Issue of shares (net of issue costs)	10	86,064	-	-	-	86,064
Balance December 31, 2012		**$** 155,985	$ 6,183	$ 1,985	$ (16,692)	$ 147,461

(In thousands of Canadian dollars)	Notes	Share Capital	Contributed Surplus	Accumulated other Comprehensive Income	Deficit	Total Equity
Balance December 31, 2010		$ 3,780	$ -	$ -	$ (1,045)	$ 2,735
Net loss for the year		-	-	-	(5,076)	(5,076)
Share based payments		-	1,679	-	-	1,679
Foreign currency translation loss		-	-	(576)	-	(576)
Issue of shares (net of issue costs)	10	65,061	-	-	-	65,061
Issued on the acquisition of Northern Lights Acquisition Corp.	1	1,080	-	-	-	1,080
Balance December 31, 2011		$ 69,921	$ 1,679	$ (576)	$ (6,121)	$ 64,903

The accompanying notes are an integral part of these consolidated financial statements.

Iona Energy Inc.
Consolidated Statements of Cash Flows

(In thousands of Canadian dollars)	Notes		Year Ended December 31 2012		Year Ended December 31 2011
Cash flows from/(used in) operating activities					
Net loss for the year		$	(10,571)	$	(5,076)
Items not involving cash:					
Depreciation			28		8
Excess of consideration over net assets acquired on capital transaction	1		-		525
Share based payments			4,504		1,679
			(6,039)		(2,864)
Changes in non-cash working capital balances:					
Accounts receivable			(1,539)		(317)
Prepaid expenses			105		(190)
Accounts payable and accrued liabilities			829		1,761
Cash flow used in operating activities			(6,644)		(1,610)
Cash flows from/(used in) financing activities					
Issue of common shares, net of issue costs			86,285		65,229
Cash acquired on capital transaction	1		-		555
Cash flow from financing activities			86,285		65,784
Cash flows from/(used in) investing activities					
Expenditures on property and equipment			(80)		(28)
Expenditures on exploration and evaluation			(61,631)		(22,131)
Deferred costs			(36,502)		-
Restricted cash			(8,412)		(1,294)
Cash flow used in investing activities			(106,625)		(23,453)
Effect of exchange rate changes on cash			876		(268)
Increase in cash			(26,108)		40,453
Cash, beginning of year			41,608		1,155
Cash, end of year		$	15,500	$	41,608
Supplemental information					
Interest paid		$	-	$	-
Taxes paid		$	-	$	-

The accompanying notes are an integral part of these interim consolidated financial statements.

(As at December 31, 2012 and December 31, 2011, and years ended December 31, 2012 and 2011, all tabular amounts are expressed in thousands of Canadian dollars, except per share amounts or as otherwise noted.)

1. Corporate Information

Iona Energy Inc. (“Iona” or “the Company”) is a publicly traded junior oil and gas Company on the TSX Venture Exchange (“TSX-V”) under the symbol INA engaged in the evaluation, acquisition, exploration and development of oil and gas properties in the United Kingdom’s North Sea and in Alaska.

The head office of Iona is located at Bankers Hall, West Tower, Suite 1000, 888 - 3rd Street S.W., Calgary, Alberta, T2P 5C5. The registered office of the Company is located at 1600, 333-7th Avenue S.W., Calgary, Alberta, T2P 2Z1.

On April 19, 2011, the Company and Northern Lights Acquisition Corp. (“Northern”) entered into an amalgamation agreement. Pursuant to the exchange ratio in the amalgamation agreement the Northern shareholders held 1,800,412 shares of the amalgamated company and Iona shareholders held 139,060,155 shares of the amalgamated company. The proposed amalgamation agreement was subject to the TSX Venture Exchange and shareholder approval which was received on May 27, 2011. The Company’s shares commenced trading on the TSX Venture Exchange on June 8, 2011.

Iona was formed under the *Business Corporations Act* (Alberta) on May 27, 2011 via the amalgamation of Iona Energy Company Limited (“IECL”) and Northern, a TSX-V Capital Pool Company, which had no operations and therefore does not constitute a business. IECL was incorporated under the *Business Corporations Act* (Alberta) on January 16, 2008 and accordingly, the transaction has been accounted for as a capital transaction with IECL being the continuing entity. The consolidated financial statements of the combined entity are issued under the name of the amalgamated entity, being Iona, but are a continuation of the historical financial statements of IECL. The deemed acquisition of Northern acquired on May 27, 2011 included the following:

Net assets acquired:		
Cash	$	555
Consideration:		
1,800,411 common shares	$	1,080
Excess of consideration over net assets acquired included in General and Administrative Expenses	$	525

The following sets out the subsidiaries of the Company and the Company’s ownership interest in those subsidiaries:

Name of Subsidiary	Jurisdiction of Incorporation	Ownership
Iona Energy Company (US) Limited	Delaware, USA	100%
Iona Energy Company (UK) Limited	United Kingdom	100%

2. Basis of Presentation

Statement of compliance

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board and were prepared using accounting policies consistent with IFRS.

2. Basis of Presentation - continued

A summary of Iona's significant accounting policies under IFRS is presented in note 3. These policies have been retrospectively and consistently applied except where specific exemptions have permitted an alternative treatment upon transition to IFRS in accordance with IFRS 1.

These consolidated financial statements were approved and authorized for issuance by the Board of Directors on April 25, 2013.

Basis of measurement
The consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and liabilities in the normal course of business as they become due, accordingly, these consolidated financial statements have been prepared on the historical cost basis, except for certain financial instruments that have been measured at fair value.

Functional and presentation currency
These consolidated financial statements are presented in Canadian dollars, which is the functional currency of Iona Energy Inc. The functional currencies of the Company's foreign subsidiaries are US dollars for Iona Energy Company (US) Limited and British Pound Sterling ("GBP") for Iona Energy Company (UK) Limited.

Use of estimates and judgments
The preparation of financial statements requires management to make estimates and use judgment regarding the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities as at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the year. By their nature, estimates are subject to measurement uncertainty and changes in such estimates in future periods could require a material change in the financial statements. Accordingly, actual results may differ from the estimated amounts as future confirming events occur. Significant estimates and judgments made by management in the preparation of these consolidated financial statements are as follows:

The operations of the Company are complex, and regulations and legislation affecting the Company are continually changing. With respect to the Trent & Tyne transaction, the Company determined that the risks and rewards of ownership do not pass until it fulfills its contractual drilling obligation to the vendor and at that point in time the Company will record its share of net production revenues during the reporting year. The well did not complete until January 2013.

The financial statements include accruals based on the terms of existing joint venture agreements. Due to varying interpretations of the definition of terms in these agreements the accruals made by management in this regard may be different from those determined by the Corporation's joint venture partners. The effect on the consolidated financial statements resulting from such adjustments, if any, will be reflected prospectively.

Amounts that will be recorded for depletion and depreciation and amounts used for impairment calculations are based on estimates of petroleum and natural gas reserves. By their nature, the estimates of reserves, including the estimates of future prices, costs, discount rates and the related future cash flows, are subject to measurement uncertainty. Accordingly, the impact to the consolidated financial statements in future periods could be material.

Oil and natural gas assets are aggregated into cash-generating units based on their ability to generate largely independent cash flows and are used for impairment testing. The determination of the Company's cash-generating units is subject to Management's judgment.

2. Basis of Presentation - continued

The decision to transfer assets from exploration and evaluation to property, plant and equipment is based on the estimated recoverable reserves used in the determination of an area's technical feasibility and commercial viability. As such there is judgment in determining the timing of these transfers.

Compensation costs recognized for share based compensation plans are subject to the estimation of what the ultimate payout will be using pricing models such as the Black-Scholes model which is based on significant assumptions such as volatility, dividend yield and expected term. These are recognized over the vesting term and the underlying options.

Tax interpretations, regulations and legislation in the various jurisdictions in which the Company operates are subject to change. As such income taxes are subject to measurement uncertainty.

Deferred income tax assets are assessed by management at the end of the reporting period to determine the likelihood that they will be realized from future taxable earnings.

3. Summary of Significant Accounting Policies

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements and in preparing the opening IFRS statement of financial position at January 1, 2010 for the purposes of the transition to IFRS, unless otherwise indicated. The accounting policies have been applied consistently by Company's entities.

Basis of consolidation:

(i) Subsidiaries:

Subsidiaries are entities controlled by the Company. Control exists when the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that currently are exercisable are taken into account. 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 acquisition method of accounting is used to account for acquisitions of subsidiaries and assets that meet the definition of a business under IFRS. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of closing. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The excess of the cost of the acquisition over the fair value of the identifiable assets, liabilities and contingent liabilities acquired is recorded as goodwill when a business is acquired. If the cost of the acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognized immediately in the statement of operations and comprehensive loss.

(ii) Jointly controlled operations and jointly controlled assets:

Many of the Company's oil and natural gas activities involve jointly controlled assets. The consolidated financial statements include the Company's share of these jointly controlled assets and a proportionate share of the relevant revenue and related costs.

(iii) Transactions eliminated on consolidation:

Intercompany balances and transactions, and any unrealized income or loss arising from intercompany transactions, are eliminated in preparing the consolidated financial statements.

3. Summary of Significant Accounting Policies - continued

Financial instruments:

(i) Financial instruments:

Financial instruments comprise of cash, restricted cash, accounts receivable, and accounts payable and accrued liabilities. These financial instruments are recognized initially at fair value net of any directly attributable transaction costs. Subsequent to initial recognition financial instruments are measured as described below.

Financial assets at fair value through earnings:
An instrument is classified at fair value through earnings if it is held for trading or is designated as such upon initial recognition. Financial instruments are designated at fair value through earnings if the Company manages such investments and makes purchase and sale decisions based on their fair value in accordance with the Company's risk management or investment strategy. Upon initial recognition, attributable transaction costs are recognized in earnings when incurred. Financial instruments at fair value through earnings are measured at fair value, and changes therein are recognized in earnings.

Other:
Other financial instruments, such as cash, restricted cash, cash calls, accounts receivable, and accounts payable and accrued liabilities are measured at amortized cost using the effective interest method, less any impairment losses.

(ii) Derivative financial instruments:

The Company may in the future enter into certain financial derivative contracts in order to manage the exposure to market risks from fluctuations in commodity prices or foreign exchange. These instruments will not be used for trading or speculative purposes. Financial derivative contracts, not designated as effective hedges are classified as fair value through earnings and are recorded on the statement of financial position at fair value. Transaction costs are recognized in earnings when incurred.

The Company does not currently have any embedded derivatives. If the Company does have embedded derivatives in the future they will be separated from the host contract and accounted for separately if the economic characteristics and risks of the host contract and the embedded derivative are not closely related, a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative, and the combined instrument is not measured at fair value through earnings. Changes in the fair value of separable embedded derivatives are recognized immediately in earnings.

(iii) Share capital

Common shares are classified as equity. Incremental costs directly attributable to the issue of common shares and share options are recognized as a deduction from equity, net of any tax effects.

(iv) Cash and cash equivalents include cash on hand and deposits held with banks with maturities of less than 90 days.

3. Summary of Significant Accounting Policies - continued

Property and equipment and exploration and evaluation assets:

Exploration and evaluation expenditures (E&E):
Exploration and evaluation (pre-license) costs are recognized in the consolidated statement of operations and comprehensive loss as incurred. E&E costs, including the costs of acquiring undeveloped land and drilling costs are initially capitalized until the drilling of the well is complete and the results have been evaluated. The costs are accumulated in cost centers by well, field or exploration area pending determination of technical feasibility and commercial viability. The technical feasibility and commercial viability of extracting a mineral resource is considered to be determinable when proved or probable reserves are determined to exist. If proved and or probable reserves are found, the drilling costs and associated undeveloped land are transferred to development and production assets once the Company has obtained Field Development approval ("FDP") and after completing an impairment assessment. The cost of undeveloped land that expires or any impairment of capitalized E&E expenditures recognized during a period is charged to the consolidated statement of operations and comprehensive loss.

E&E assets are assessed for impairment if (i) sufficient data exists to determine technical feasibility and commercial viability, and (ii) facts and circumstances suggest that the carrying amount exceeds the recoverable amount. For purposes of impairment testing, exploration and evaluation assets are allocated to cash-generating units ("CGU's").

Property and Equipment:
Items of property and equipment currently consists of office equipment but in the future will also include oil and gas development and production assets. Property & equipment assets are measured at cost less accumulated depletion and depreciation and accumulated impairment losses. The cost of development and production assets will include; transfers from E&E assets, which generally include the cost to drill the well and the cost of the associated land upon determination of technical feasibility and commercial viability; the cost to complete and tie-in the wells; facility costs; the cost of recognizing provisions for future restoration and decommissioning; geological and geophysical costs; and directly attributable overheads.

Development and production assets are grouped into CGU's for impairment testing.

When significant parts of an item of property, and equipment, including oil and natural gas interests, have different useful lives, they are accounted for as separate items (major components).

Gains and losses on disposal of an item of property and equipment, including oil and natural gas interests, are determined by comparing the proceeds from disposal with the carrying amount of property and equipment and are recognized in the statement of operations and comprehensive loss.

Subsequent costs of development and production assets:
Costs incurred subsequent to the determination of technical feasibility and commercial viability and the costs of replacing parts of development and production assets are recognized as oil and natural gas interests only when they increase the future economic benefits embodied in the specific asset to which they relate. All other expenditures are recognized in earnings as incurred. Such capitalized oil and natural gas interests generally represent costs incurred in developing proved and/or probable reserves and bringing in or enhancing production from such reserves, and are accumulated on a field or geotechnical area basis. The carrying amount of any replaced or sold component is derecognized. The costs of the day-to-day servicing of property and equipment are recognized in operating expenses as incurred.

3. Summary of Significant Accounting Policies - continued

Depletion and depreciation:
The net carrying value of development and production assets will be depleted using the unit of production method by reference to the ratio of production in the period to the related estimate of recoverable reserves, taking into account estimated future development costs necessary to bring those reserves into production and the estimated salvage value of the assets at the end of their useful lives. Future development costs are estimated taking into account the level of development required to produce the reserves.

Recoverable reserves will be estimated annually by independent qualified reserve evaluators and represent the estimated quantities of crude oil, natural gas and natural gas liquids which geological, geophysical and engineering data demonstrate with a specified degree of certainty to be recoverable in future years from known reservoirs and which are considered commercially producible.

Leased assets will be depreciated over the shorter of the lease term and their useful lives unless it is reasonably certain that the Company will obtain ownership by the end of the lease term.

Depreciation methods, useful lives and residual values are reviewed at each reporting date.

Deferred Costs:
For expenditures that have been incurred for property acquisitions where conditions have yet to be completed the expenditures are held in deferred costs and transferred to E&E or property and equipment.

Farmouts:
Under IFRS, farmouts are considered a disposition of a partial interest in a property. The proceeds on the disposition is generally the capital spent, or estimated to be spent, by the farmee in order to earn the interest. Farmout transactions in the exploration stage do not have any gain or losses recorded. A gain or loss would be recognized for farmout transactions on developed properties where the proceeds would be measured at fair value unless the transaction lacks commercial substance or the fair value of neither the asset received nor the asset given up is reliably measurable.

Impairment:
(i) Financial assets:
A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset. An impairment loss in respect of a financial asset measured at amortized cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate.

Individually significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in groups that share similar credit risk characteristics. All impairment losses are recognized in the statement of operations and comprehensive loss.

An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognized. For financial assets measured at amortized cost the reversal is recognized in the statement of operations and comprehensive loss.

(ii) Non-financial assets:
The carrying amounts of the Company's non-financial assets, other than deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. For goodwill and other intangible assets that have indefinite lives or that are not yet available for use an impairment test is completed annually. E&E assets are assessed for impairment when they are transferred to property and equipment, and also if facts and circumstances suggest that the carrying amount exceeds the recoverable amount.

3. Summary of Significant Accounting Policies - continued

For the purpose of impairment testing, assets are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (CGU). The recoverable amount of an asset or a CGU is the greater of its value in use and its fair value less costs to sell.

Fair value less cost to sell is determined as the amount that would be obtained from the sale of a CGU in an arm's length transaction between knowledgeable and willing parties. The fair value less cost to sell of oil and gas assets is generally determined as the net present value of the estimated future cash flows expected to arise from the continued use of the CGU, including any expansion prospects, and its eventual disposal, using assumptions that an independent market participant may take into account. These cash flows are discounted by an appropriate discount rate which would be applied by such a market participant to arrive at a net present value of the CGU.

Value in use is determined as the net present value of the estimated future cash flows expected to arise from the continued use of the asset in its present form and its eventual disposal. Value in use is determined by applying assumptions specific to the Company's continued use and can only take into account approved future development costs. Estimates of future cash flows used in the evaluation of impairment of assets are made using management's forecasts of commodity prices and expected production volumes. The latter takes into account assessments of field reservoir performance and includes expectations about proved and unproved volumes, which are risk-weighted utilizing geological, production, recovery and economic projections.

The goodwill acquired in a business combination, for the purpose of impairment testing, is allocated to the CGU's that are expected to benefit from the synergies of the combination. E&E assets are allocated to related operating units when they are assessed for impairment, both at the time of any triggering facts and circumstances as well as upon their eventual reclassification to producing assets (oil and natural gas interests in property and equipment).

An impairment loss is recognized if the carrying amount exceeds its estimated recoverable amount. Impairment losses are recognized in depletion and depreciation expense in the statement of operations and comprehensive loss. Impairment losses recognized in CGU's are allocated first to reduce the carrying amount of any goodwill allocated to the CGU and then to reduce the carrying amounts of the other assets in the CGU on a pro rata basis.

An impairment loss in respect of goodwill is not reversed. In respect of other assets, impairment losses recognized in prior years are assessed at each reporting date, if facts and circumstances indicate that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depletion and depreciation, if no impairment loss had been recognized.

Share based compensation:
The Company has established a share based compensation plan (the "Plan") comprised of a Stock Option Plan (refer to note 10 (c) for further details of the Plan). The Company uses the fair value method for valuing share based compensation. Under this method, the compensation cost attributed to stock options granted are measured at the fair value at the grant date and expensed over the vesting period with a corresponding increase to a category within equity referred to as contributed surplus. A forfeiture rate is estimated on the grant date and is adjusted to reflect the actual number of option or units that vest. Upon the settlement of the stock options the previously recognized value in contributed surplus is recorded as an increase to shareholders' capital.

(As at December 31, 2012 and December 31, 2011, and years ended December 31, 2012 and 2011, all tabular amounts are expressed in thousands of Canadian dollars, except per share amounts or as otherwise noted.)

3. Summary of Significant Accounting Policies - continued

Provisions:
A provision is recognized if, as a result of a past event, the Company has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax "risk-free" rate that reflects current market assessments of the time value of money and the risks specific to the liability. Provisions are not recognized for future operating losses.

Decommissioning obligations:
The Company's activities give rise to dismantling, decommissioning and site disturbance remediation activities. Provision is made for the estimated cost of abandonment and site restoration and capitalized in the relevant asset category.

Decommissioning obligations are measured at the present value of management's best estimate of the expenditure required to settle the present obligation as at the reporting date using a risk free interest rate. Subsequent to the initial measurement, the obligation is adjusted at the end of each period to reflect the passage of time and changes in the estimated future cash flows underlying the obligation. The increase in the provision due to the passage of time is recognized as accretion (within finance expense) whereas increases/decreases due to changes in the estimated future cash flows or changes in the discount rate are capitalized. Actual costs incurred upon settlement of the decommissioning obligations are charged against the provision to the extent the provision was established.

Foreign currencies:
The functional currency for each entity is the currency of the primary economic environment in which it operates. Foreign currency denominated transactions are translated into the entity's functional currency as follows; monetary items denominated in foreign currencies are translated into its functional currency at the rates of exchange at the period end date. Non-monetary items are translated to the functional currency at the historical exchange rate. Any gains or losses are recorded in the consolidated statement of net income (loss).

For the purpose of the consolidated financial statements, the results and financial position of each group entity are expressed in Canadian dollars. For the accounts of foreign operations, assets and liabilities are translated to Canadian dollars at rates prevailing at the period end date. Revenues and expenses are translated to Canadian dollars using the average rate over the period. Translation gains or losses relating to the foreign operations are included in the consolidated statement of comprehensive income (loss) and accumulated in shareholders' equity on the balance sheet.

Income tax:
Income tax expense is comprised of current and deferred tax. Income tax expense is recognized in the statement of operations and comprehensive loss except to the extent that it relates to items recognized directly in equity, in which case it is recognized in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years. Deferred tax is recognized on the temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognized on the initial recognition of assets or liabilities in a transaction that is not a business combination. In addition, deferred tax is not recognized for taxable temporary differences arising on the initial recognition of goodwill.

Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

3. Summary of Significant Accounting Policies - continued

A deferred tax asset is recognized to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

Earnings per share:
Basic earnings per share is calculated by dividing the net earnings or loss attributable to common shares of the Company by the weighted average number of common shares outstanding during the period. Diluted earnings per share is determined by adjusting the net earnings or loss attributable to common shareholders and the weighted average number of common shares outstanding for the effects of dilutive instruments such as options granted.

Future Changes in Accounting Policies:
Iona has reviewed new and revised accounting pronouncements that have been issued but are not yet effective. The Company is currently evaluating the impact of the adoption of these standards and amendments. The adoption of these standards and amendments are not expected to significantly impact the Company.

The following standards and interpretations have not been adopted as they apply to future periods.

They may result in future changes to our existing accounting policies and other note disclosures.

IFRS 9 *Financial Instruments* –the International Accounting Standards Board (IASB) issued IFRS 9 to address classification and measurement of financial assets. In October 2010, the IASB revised the standard to include financial liabilities. The standard is required to be adopted for periods beginning January 1, 2015. We are evaluating the impact that this standard may have on our results of operations and financial position.

IFRS 10 *Consolidated Financial Statements* –the IASB issued IFRS 10 which provides additional guidance to determine whether an investee should be consolidated. The guidance applies to all investees, including special purpose entities. The standard is required to be adopted for periods beginning January 1, 2013.

IFRS 11 *Joint Arrangements* –the IASB issued IFRS 11 which presents a new model for determining whether an entity should account for joint arrangements using proportionate consolidation or the equity method. An entity will have to follow the substance rather than legal form of a joint arrangement and will no longer have a choice of accounting method. The standard is required to be adopted for periods beginning January 1, 2013.

IFRS 12 *Disclosure of Interests in Other Entities* –the IASB issued IFRS 12 which aggregates and amends disclosure requirements included within other standards. The standard requires a company to provide disclosures about subsidiaries, joint arrangements, associates and unconsolidated structured entities. The standard is required to be adopted for periods beginning January 1, 2013.

IFRS 13 *Fair Value Measurement* –the IASB issued IFRS 13 to provide comprehensive guidance for instances where IFRS requires fair value to be used. The standard provides guidance on determining fair value and requires disclosures about those measurements. The standard is required to be adopted for periods beginning January 1, 2013.

IAS 27 *Separate Financial Statements* - the Company will be required to adopt the amendments to IAS 27 to focus solely on accounting and disclosure requirements when an entity presents separate financial statements, due to the issuance of the new IFRS 10, which is specific to consolidated financial statements. The adoption of these amendments is not expected to impact the Company. The amendments are required to be adopted for periods beginning January 1, 2013.

(As at December 31, 2012 and December 31, 2011, and years ended December 31, 2012 and 2011, all tabular amounts are expressed in thousands of Canadian dollars, except per share amounts or as otherwise noted.)

3. Summary of Significant Accounting Policies - continued

IAS 28 *Investments in Associates and Joint Ventures - t*he Company will be required to adopt the amendments to IAS 28 which conform to changes made in IFRS 10 and IFRS 11. The amendments are required to be adopted for periods beginning January 1, 2013.

4. Net Loss for the Year

Net loss is stated after charging/(crediting):

	2012	2011
Share based payments	$ 4,504	$ 1,679
Net foreign exchange loss/(gain)	152	(241)
Depreciation	28	8
Exploration and evaluation costs		
Cost of licences relinquished	$ 25	$ 197
Pre licence expenditure	56	345
Licence round application costs	274	3
	$ 355	$ 545

5. Segmented Information

The Company's reportable segments and geographical segments are the United Kingdom (North Sea) and the United States. The corporate reportable segment includes the Company's corporate and financing activities.

The accounting policies used for the reportable segments are the same as the Company's accounting policies. For the purposes of monitoring segment performance and allocating resources between segments, the Company's executive officers monitor the tangible, intangible and financial assets attributable to each segment. All assets are allocated to reportable segments. The following tables show information regarding the Company's segments.

	Year ended December 31, 2012			
	United Kingdom	United States	Corporate	**Total**
Depreciation	$ 28	$ -	$ -	**$ 28**
Expenses before finance income	(6,347)	-	(4,408)	**(10,755)**
Net finance income	95	-	89	**184**
Net (loss)/ income	(6,252)	-	(4,319)	**(10,571)**
	As at December 31, 2012			
Total assets	193,838	927	8,758	**203,523**
Total liabilities	$ 55,646	$ -	$ 416	**$ 56,062**

	Year ended December 31, 2011			
	United Kingdom	United States	Corporate	Total
Depreciation	$ 8	$ -	$ -	$ 8
Expenses before finance income	(1,391)	32	(3,745)	(5,104)
Net Finance income	3	-	25	28
Net (loss)/ income	(1,388)	32	(3,720)	(5,076)
	As at December 31, 2011			
Total assets	59,869	894	11,357	72,120
Total liabilities	$ 6,587	$ -	$ 630	$ 7,217

(As at December 31, 2012 and December 31, 2011, and years ended December 31, 2012 and 2011, all tabular amounts are expressed in thousands of Canadian dollars, except per share amounts or as otherwise noted.)

6. Restricted Cash

Current
At December 31, 2012, the Company had $706,000 of restricted cash (Dec 31, 2011 - $1,293,000), which will be held in trust until the Company completes its drilling commitment on the Trent and Tyne properties in the United Kingdom (note 7).

Non-Current
At December 31, 2012 and 2011, the Company had $52,000 of cash held as deposits for work commitment guarantees contained in exploration contracts in Alaska in the United States.

At December 31, 2012, the Company had $6,893,000 of restricted cash (December 31, 2011 - $Nil) held for the Company's decommissioning liabilities on the Trent & Tyne properties, $2,002,000 (December 31, 2011 - $Nil) held until the completion of long lead items and $105,000 (December 31, 2011 - $Nil) held as security against Company credit cards.

7. Exploration and Evaluation Assets and Deferred Costs

	General E&E	Property Payments	Drilling Costs	Total - United Kingdom Segment	United States Segment	Total – E&E	Deferred Costs
Balance, December 31, 2010	511	-	-	511	961	1,472	-
Additions	5,388	6,086	15,793	27,267	-	27,267	315
Effect of changes in exchange rates	(1)	(67)	(172)	(240)	(67)	(307)	-
Unsuccessful Exploration and Evaluation	(197)	-	-	(197)	-	(197)	-
Balance, December 31, 2011	**5,701**	**6,019**	**15,621**	**27,341**	**894**	**28,235**	**315**
Additions	**28,695**	**61,016**	**15,973**	**105,684**	**14**	**105,698**	**37,702**
Effect of changes in exchange rates	**560**	**325**	**521**	**1,406**	**19**	**1,425**	**339**
Balance, December 30, 2012	**34,956**	**67,360**	**32,115**	**134,431**	**927**	**135,358**	**38,356**

The Company's exploration and evaluation assets consist of costs pertaining to Alaska and the United Kingdom.

General E&E

During the year, the Company expensed $355,000 (2011 - $348,000) of exploration and evaluation costs. Also, following completion of geotechnical evaluation activity, the decision was made post year end to relinquish the Solway Firth license and therefore the carrying value of the license of $197,000 was expensed in the year ended December 31, 2011.

The additions to general E&E relates to development expenditure on both the Orlando and Kells fields.

7. Exploration and Evaluation Assets and Deferred Costs - continued

Property payments

On January 19, 2012, the Company's UK Subsidiary, Iona Energy Company (UK) Limited ("IEUKL"), acquired full ownership and operatorship from Fairfield Cedrus Limited ("Fairfield") of a 100% interest in Block 3/8d containing the Kells Oil Field. IEUKL reimbursed Fairfield on closing for USD$8.5 million in pre-development expenditures related to the Kells field. In addition, upon the approval by DECC of a field development plan in respect of Kells, Iona will be obligated to make a cash payment of USD$5.0 million to Fairfield and pay a net royalty of USD$2.50 per barrel of production from the Kells Oil Field. Refer to Note 16 for subsequent events.

On February 3, 2012, IEUKL entered into a sale and purchase agreement to acquire from Centrica Venture Production Company ("CVPC") a 58.73 % interest in Block 13/21a of the West Wick Oil Field. Under the terms of the agreement IEUKL paid CVPC a holding deposit of USD$3.15 million on April 15, 2011 and on completion paid USD$5.0 million on September 13, 2012.

On July 9, 2012, the IEUKL completed the purchase of its partners' interests, MPX North Sea Limited ("MPX") (30%) and Sorgenia E&P (UK) Ltd ("Sorgenia") (35%), in the Orlando Oil field in exchange for the payment of historical costs and future payments out of production. Pursuant to the terms of the sale and purchase agreements with MPX and Sorgenia, payment of GBP29.3 million (CAD$47.4 million) became payable on December 30, 2012 and was paid in Q1 2013. Additionally, future staged payments will be made by Iona to Sorgenia and MPX commencing six months after first production from Orlando. The first payment will be USD$7.0 million with additional payments of USD$7.0 million, USD$7.0 million, USD$4.0 million, and USD$4.0 million made every six months thereafter respectively, amounting to a total payment of USD$29.0 million over 3 years. Refer to Note 16 for subsequent events

Drilling Costs

The additions to drilling costs in 2012 relates to the appraisal well and side-track drilled on Orlando (Q1 2012).

Deferred Costs

On December 28, 2012 IEUKL entered into a definitive Sale and Purchase Agreement with Carrizo Oil & Gas, Inc. ("Carrizo") to acquire the entire share capital of its wholly owned subsidiary, Carrizo UK Huntington Limited ("Carrizo UK"), including its interest in the Huntington Field. Under the terms of the agreement, IEUKL paid to Carrizo a USD$6 million non-refundable deposit upon signing the Sale and Purchase Agreement. On completion of the deal in February 2013, IEUKL paid a cash consideration of USD$174.9 million. A deferred payment of USD$18 million will also be paid to Carrizo from first producing field revenues being received from the Huntington field. As the deal did not complete until 2013, the non-refundable deposit of USD$6m is reflected in deferred costs.

The remaining additions to deferred costs relates to the net production revenue and T6 drilling costs on the Trent and Tyne assets. The costs are held in deferred costs as the Trent and Tyne acquisition is not considered complete until the drilling of the T6 well is complete and the risk and rewards have passed to Iona. The T6 well was completed in January 2013.

(As at December 31, 2012 and December 31, 2011, and years ended December 31, 2012 and 2011, all tabular amounts are expressed in thousands of Canadian dollars, except per share amounts or as otherwise noted.)

8. Property and Equipment

Cost or deemed cost:		Office Equipment/ Computers/ Other
Balance, December 31, 2010	$	-
Additions		28
Balance, December 31, 2011	$	28
Additions		79
Balance December 31, 2012	$	107

Depreciation and Impairment losses:		Office Equipment/ Computers/ Other
Balance, December 31, 2010	$	-
Depreciation for the period		8
Balance, December 31, 2011	$	8
Depreciation for the period		28
Balance December 31, 2012	$	36

Net book value		Office Equipment/ Computers/ Other
Balance, December 31, 2011	$	20
Balance December 31, 2012	$	71

All of the Company’s property and equipment consists of office equipment and is located in the United Kingdom.

9. Decommissioning Liabilities

Balance, December 31, 2010	$	-
Additions		170
Balance December 31, 2011	$	170
Additions		479
Accretion		7
Balance December 31, 2012	$	656

The total future decommissioning liability was calculated by management based on its net ownership interest in the Orlando field and the estimated costs to be incurred in future periods to reclaim and abandon the well. The decommissioning liability was measured at the end of the year using a pre-tax, risk-free discount rate of 4.15% percent and an inflation rate of 2.00% percent over the estimated life of the asset to calculate the present value of the decommissioning liability. The costs are expected to be incurred in 18 years.

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10. Share Capital

(a) Authorized
Unlimited number of Common Shares without nominal or par value
Unlimited number of Preferred shares, issuable in series

(b) Issued

	2012				2011			
Common shares	**Shares**		**Amounts**		Shares		Amounts	
Opening balance	**140,860,566**	**$**	**69,892**		22,575,065	$	3,751	
Issued for cash *(i)*	**184,044,400**		**92,015**		-		-	
Conversion of subscription receipts *(iii)*	**-**		**-**		116,485,090		69,891	
Issued on Northern amalgamation (note 1)	**-**		**-**		1,800,411		1,080	
Share issue costs	**-**		**(5,946)**		-		(4,830)	
Balance end of period	**324,904,966**	**$**	**155,961**		140,860,566	$	69,892	
Warrants								
Opening balance*(ii)*	**264,500**	**$**	**29**		264,500	$	29	
Exercised *(ii)*	**(44,400)**		**(5)**		-		-	
Balance end of period	**220,100**	**$**	**24**		264,500	$	29	
Subscription Receipts								
Opening balance	**-**	**$**	**-**		-		-	
Issued *(iii)*	**-**		**-**		116,485,090	$	69,891	
Share issue costs*(iii)*	**-**		**-**		-		(4,831)	
Converted into common shares *(iii)*	**-**		**-**		(116,485,090)		(65,060)	
		$	**155,985**			$	69,921	

(i) *On April 11, 2012 the Company issued 184,000,000 common shares pursuant to a public offering at a price of $0.50 per share for gross proceed of $92,000,000.*

(ii) *The Company also issued 264,500 warrants to brokers who assisted with the private placements in 2010. The warrants are exercisable into a common share of the Company at a strike price of $0.22 per warrant and expire in 2013. The warrants were valued at $29,000 using the Black Scholes option pricing model, recorded as a share issuance costs with the following assumptions: dividend yield – Nil, expected volatility 75%, risk free rate of return 1.53%, weighted average life – 3 years, forfeiture rate – Nil. On May 15, 2012 the Company had 44,400 warrants exercised for gross proceeds of $10,000.*

(iii) *On March 10, 2011, the Company entered into a Subscription Receipt Agreement (the "Agreement") to issue 116,485,090 subscription receipts for $69,891,000 less $4,830,000 of share issue costs, which were converted into common shares in conjunction with the Company completing its initial public offering. Under the terms of the Agreement, each subscription receipt will entitle the holder to 1 common share and 0.2 liquidity warrants (assuming certain conditions are not met) where each liquidity warrant entitles the holder to receive 1 common share if the Corporation does not complete a going public transaction by June 30, 2011. Pursuant to the Agreement, $23,000,000 (net of share issue costs) was released and 38,333,333 subscription receipts were automatically converted into common shares upon closing of the acquisition of certain exploration rights in the North Sea (note 7 - the non-producing Orlando lease) on March 10, 2011 with the remainder being released on May 31, 2011 and 78,151,757 subscription receipts being converted into common shares with the successful closing of the Trent and Tyne acquisition. The liquidity warrants expired as a result of the closing of the Northern transaction (note1).*

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10. Share Capital - continued

(c) Stock options

The Company has a stock option plan, approved by its Board of Directors on May 27, 2011, that provides for the issuance to its directors, officers, employees and consultants options to purchase from treasury a number of common shares not exceeding 10% of the common shares that are outstanding from time to time which is the number of shares reserved for issuance under the plan. The options are non-transferable if not exercised. The exercise price can be no less than the market price of the Company's common shares prior to the day of the grant, which may be different from the closing price of such shares on the day of grant for options granted to date. Pursuant to the plan, the vesting provisions of the stock options are determined by the Board of Directors at the date of grant. All of the options granted to date under the plan vest as follows: 25% immediately and 25% vesting on the first, second and third anniversary dates. A summary of the status of the Company's stock option plan as at December 31, 2012 and December 31, 2011 and changes during the respective periods ended on those dates is presented below:

	December 31, 2012			December 31, 2011		
Stock Options	**Number of Options**		**Weighted Average Exercise Price**	Number of Options		Weighted Average Exercise Price
Beginning of year	**9,650,000**	**$**	**0.60**	-	$	-
Granted	**17,430,000**		**0.57**	9,650,000		$0.60
Exercised	**-**		**-**	-		-
Forfeited	**-**		**-**	-		-
End of year	**27,080,000**	**$**	**0.58**	9,650,000	$	-
Exercisable, end of year	**9,182,500**	**$**	**0.58**	2,412,500	$	-

Date of Grant	**Number Outstanding**	**Exercise Price**	**Weighted Average Remaining Contractual Life**	**Date of Expiry**	**Number Exercisable Dec 31, 2012**
May 31, 2011	9,550,000	$0.60	2.42 years	May 31, 2015	4,775,000
November 25, 2011	100,000	$0.60	2.92 years	Nov 25, 2015	50,000
April 13, 2012	17,070,000	$0.57	4.29 years	April 12, 2017	4,267,500
June 18, 2012	210,000	$0.47	4.46 years	June 18, 2017	52,500
August 29, 2012	150,000	$0.38	4.67 years	August 29, 2017	37,500

The fair value of the options was estimated using the Black Scholes option pricing model with the following assumptions:

	Year ended December 31, 2012		**Year ended December 31, 2011**	
Fair value at grant date:	$	0.24 - 0.36	$	0.17 - 0.35
Exercise price	$	0.38 - 0.57	$	0.60
Dividend yield		Nil		Nil
Expected volatility		75%		75%
Risk-free rate		3.5%		3.5%
Expected life		5 years		4 years

An estimated forfeiture rate of 5% (2011 – 5%) is used when recording share-based payments. The expected volatility was determined via a peer comparison due to the Company's limited trading history.

(d) Escrowed shares

Pursuant to an Escrow Agreement, all of the 13,342,392 common shares held by "principals" prior to the Northern transaction, were deposited in trust and held in escrow. 10% of these shares were released on May 27, 2011 upon completion of the Northern transaction and 15% were released on each six-month anniversary of that date. The Company has 6,004,099

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(2011 - 10,006,807) common shares remaining in escrow on December 31, 2012.

11. Taxation

Reconciliation of effective tax rate for the years ended December 31:

	2012	2011
Loss before tax from continuing operations	$ (10,571)	$ (5,076)
Rate of corporation tax (parent)	25.0%	26.5%
	$ (2,643)	$ (1,345)
Non deductible stock based compensation	$ 710	$ 330
Other permanent differences	-	22
Foreign tax rate difference	(2,313)	(490)
Unrecognized deferred tax asset	4,246	1,483
Tax Expense	**$ -**	**$ -**

Unrecognized Deferred Tax Assets

Deferred tax assets have not been recognized in respect of the following items:

Year ended December 31, 2012

	United Kingdom	United States	Canada	Total
Other temporary differences	$ 1,177	$ (313)	$ 2,054	$ 2,918
Tax losses	14,797	302	1,988	17,087
Total unrecognized deferred tax asset	**$ 15,974**	**$ (11)**	**$ 4,042**	**$ 20,005**

Year ended December 31, 2011

	United Kingdom	United States	Canada	Total
Other temporary differences	$ 269	$ (235)	$ 79	$ 113
Tax losses	2,054	224	772	3,050
Total unrecognized deferred tax asset	$ 2,323	$ (11)	$ 851	$ 3,163

A deferred tax asset has not been recognized as it is not probable at the year end that the asset is recoverable. The asset is recoverable if there are future suitable taxable profits from which the future reversal of the underlying temporary differences can be deducted. It is likely that with further development of the assets in the United Kingdom that a deferred tax asset will be recognized. The probability of recoverability will be reviewed at the end of each reporting period.

The Company has incurred cumulative non-capital losses at December 31, 2012 of approximately $7,502,000 (December 31, 2011 - $2,913,000) for Canadian income tax purposes, which are available to reduce taxable income in future years. If not utilized, these losses will expire in the years ending December 31, 2026 to 2032. The unrecognized UK deferred tax asset relates to pre-trading expenditure which if capital in nature can be carried on indefinitely. Currently all pre-trading expenditure in the UK is considered capital in nature.

(As at December 31, 2012 and December 31, 2011, and years ended December 31, 2012 and 2011, all tabular amounts are expressed in thousands of Canadian dollars, except per share amounts or as otherwise noted.)

12. Related Party Transactions

Except as disclosed elsewhere in these consolidated financial statements the Company had the following related party transactions:

(a) During the year ended December 31, 2012, the Company was charged $391,000 (2011 - $373,000), respectively in legal fees of which $220,000 (2011 - $98,000) related to share issuance costs by a law firm where a director of the Company is a partner, of which $70,000 (2011 - $190,000) is included in accounts payable and accrued liabilities as at December 31, 2012.

(b) Compensation of key management personnel:

Key management personnel include all Directors, the Chief Executive Officer and the Chief Financial Officer. Compensation paid to and share-based compensation attributable to the key management personnel consists of the following:

	Year ended December 31, 2012	Year ended December 31, 2011
Short-term benefits	$ 720	$ 561
Share based payments (1)	$ 2,495	$ 1,087
Termination benefits	$ -	$ -

(1) Represents amount of the non-cash share-based compensation expense estimated on grant date associated with share options (note 10). This amount may not be equal to the fair value ultimately received on exercise.

(c) Included in accounts receivable is $265,013 (2011 - $Nil) due from an office and director of the Company who resigned from the Company's management team and Board subsequent to December 31, 2012. Of this amount $117,366 remains to be collected as at April 25, 2013. The amounts owing are non-interest bearing and secured. The Company expects full repayment of the remaining balances.

Except as disclosed, all related party transactions are in the normal course of operations and have been measured at the agreed to exchange amounts, which is the amount of consideration established and agreed to by the related parties and approximates fair value.

(As at December 31, 2012 and December 31, 2011, and years ended December 31, 2012 and 2011, all tabular amounts are expressed in thousands of Canadian dollars, except per share amounts or as otherwise noted.)

13. Commitments and Contingencies

In addition to accounts payable and accrued liabilities, and based on management's best estimate, the Company has the following contractual obligations:

	December 31, 2012				
	Payments Due in Period				
Contractual Obligations	**Total**	**Less than 1 Year**	**1 to 3 Years**	**3 to 5 Years**	**More than 5 Years**
U.S. Segment					
Exploration leases	**227**	17	48	71	91
UK Segment					
Office lease	**240**	96	144	-	-
Decommissioning obligations	**6,999**	-	-	-	6,999
Drilling, completion, facility construction	**8,262**	8,262	-	-	-
Total UK Segment	**15,501**	8,358	144	-	6,999
Corporate Segment					
Office lease	**12**	12	-	-	-
Total Contractual Obligations	**15,740**	8,387	192	71	7,090

The above table does not include property payments due pursuant to property acquisition agreements as disclosed in Note 7.

14. Financial Instruments

The Company holds various forms of financial instruments. The nature of these instruments and the Company's operations expose the Company to, credit, and foreign exchange risks. The Company manages its exposure to these risks by operating in a manner that minimizes its exposure to the extent practical.

(a) Commodity Price Risk
The Company will be subject to commodity price risk for the sale of its production. The Company may enter into contracts for risk management purposes only, in order to protect a portion of its future cash flow from the volatility of petroleum commodity prices. To date the Company has no production and has not entered into any forward commodity contracts.

(b) Credit Risk
Credit risk is the risk that arises when a party to a financial instrument will be unable to discharge cash, restricted cash and accounts receivable. Cash and restricted cash is placed with major financial institutions. The maximum exposure to credit risk is approximate to the carrying value of such financial instruments. The Company does not have an allowance for doubtful accounts as at December 31, 2012, and did not provide for any doubtful accounts nor was it required to write-off any receivables during the year ended December 31, 2012 or 2011. All third party receivables have been settled subsequent to the year end.

14. Financial Instruments - continued

(c) Interest Risk
Interest rate risk refers to the risk that the value of a financial instrument or cash flows associated with the instrument will fluctuate due to changes in market interest rates. The Company currently does not use interest rate hedges or fixed interest rate contracts to manage the Company's exposure to interest rate fluctuations.

Assuming all other variables remain constant, a 1% increase or decrease in interest rates would have had an immaterial impact on the cashflows of the Company.

(d) Foreign Currency Exchange Risk
The Company operates on an international basis and therefore foreign exchange risk exposures arise from transactions denominated in currency other than the Canadian Dollar. The Company is exposed to foreign currency fluctuations as it holds cash and incurs expenditures in property and equipment in foreign currencies. The Company incurs expenditures in Pound sterling, Euros, United States dollars and Canadian dollars and is exposed to fluctuations in exchange rates in these currencies. There are no exchange rate contracts in place as at or during the period ended December 31, 2012, December 31, 2011, or thereafter.

Assuming all other variables remain constant, a 1% increase or decrease in foreign exchange rates on the foreign cash and restricted cash balances at December 31, 2012 would have impacted the comprehensive loss of the Company for the year ended December 31, 2012 by approximately $169,000 (2011 - $316,000).

In addition at December 31, 2012, the Company held approximately $55,990,000 (£33,991,000) (2011- $6,321,847 (£4,008,272)) of accounts payable and unearned revenue in Pound Sterling. Assuming all other variables remain constant, a 1% increase or decrease in foreign exchange rates as at December 31, 2012 would impact the comprehensive loss of the Company for the year ended December 31, 2012 by approximately $550,000 (2011 - $63,000).

(e) Fair Value of Financial Instrument
The Company classifies the fair value of these financial instruments according to the following hierarchy based on the amount of observable inputs used to value the instruments.

All financial assets are classified as loans and receivables and are accounted for on an amortized cost basis. All financial liabilities are classified as other liabilities. There have been no changes to the aforementioned classifications during the year ended December 31, 2012.

(f) Liquidity Risk
Liquidity risk includes the risk that, as a result of the Company's operational liquidity requirements:

- The Company will not have sufficient funds to settle commitments as they become due;
- The Company will be forced to sell financial assets at a value which is less than what they are worth; or
- The Company may be unable to settle or recover a financial asset.

As the Company's industry is very capital intensive, the majority of the spending is related to the Company's capital programs. The Company's goal is to prudently spend its capital. As circumstances change, liquidity risks may necessitate the Company to issue equity, obtain debt financing, or sell assets. The Company's contractual obligations are included in Note 13 and further details of liquidity is discussed in note 15.

(As at December 31, 2012 and December 31, 2011, and years ended December 31, 2012 and 2011, all tabular amounts are expressed in thousands of Canadian dollars, except per share amounts or as otherwise noted.)

15. Capital Risk Management

The Company manages its capital with the prime objectives of safeguarding the business as a going concern, creating investor confidence, maximizing long-term returns and maintaining an optimal structure to meet its financial commitments and to strengthen its working capital position. At present, the capital structure of the Company is primarily composed of shareholders' equity. The Company's strategy is to access capital, primarily through equity issuances, reserve based lending, and other alternative forms of debt financing. The Company actively manages its capital structure and makes adjustments relative to changes in economic conditions and the Company's risk profile.

In order to maintain the capital structure, the Company will from time to time issue shares and adjust its capital spending to manage current working capital levels. As at December 31, 2012, the Group has a working capital deficiency of $34,720,000 and capital commitments of $15,740,000. Subsequent to December 31, 2012 the Company entered into a USD$250 million Senior Secured Borrowing Base Facility ("BBF") of which there is USD$150 million currently available. The Company has drawn down $139,000,000 of the debt available under the facility. In addition, the Company closed a CDN$23 million private placement of common shares (see note 16). Although the cashflow generated from BBF and private placement has assisted the Company to meet its liabilities and commitments, the Company is still working with its lenders and suppliers to manage its current working capital levels on the Orlando and Kells projects to ensure the Company meets its liquidity test under the Borrowing Base Facility.

At December 31, 2012 the Company was not subject to any externally imposed covenants.

The Company's capital includes the following:

	December 31, 2012	December 31, 2011
Shareholder's equity	**$ 147,461,000**	$ 64,903,000

16. Subsequent Events

Other than as disclosed in Note 7, the company has had the following subsequent events:

On February 21, 2013, the Company announced that:

- The Company has closed its previously announced bought-deal private placement of 41,818,600 common shares (the "Offering") at a price of $0.55 per share. An aggregate gross amount of CAD$23 million was raised pursuant to the Offering. Casimir Capital Ltd. acted as lead underwriter with National Bank Financial as a syndicate member;
- Iona received USD$60 million on completion of a structured energy derivative transaction with Britannic Trading Ltd. a subsidiary of BP International Limited for notional quantities of 1,360,072 and 6,746,231 barrels of Brent blend crude oil over the period April 1, 2013 to March 31, 2014 and April 1, 2014 to March 31, 2018 and strike prices of USD$100 and USD$95, respectively;
- The Company has also entered into a Marketing and Off-take Agreement with BP Oil International Limited to sell its entire future crude oil produced from the Orlando and Kells fields;
- Iona sold a 25% working interest in its UK North Sea Orlando and Kells fields to an industry participant for total gross proceeds of USD$34 million on close and pro-rata share of future staged payment obligations.

16. Subsequent Events – continued

On February 22, 2013, the Company announced the closing of its previously announced Senior Secured Borrowing Base Facility for up to USD$250 million of which USD$150 million is currently available with the Bank of America Merrill Lynch, Lloyds TSB Bank plc and BNP Paribas and entered into hedging contracts with these banks for a total of 1,330,791 barrels of oil over the period April 1, 2013 to March 31, 2014 at a strike price of USD$100.

Also on February 22, 2013, the Company announced the closing of its acquisition of Carrizo UK Huntington Limited ("Carrizo UK"). The acquisition of Carrizo UK consisted of:

- A 15% non-operated working interest in License P1114 of UK North Sea Block 22/14b covering the near-producing Huntington oil field development ("Huntington");
- Royalties equivalent to 2.55% of total gross oil and gas production payable to Carrizo UK from the other Huntington Joint Venture Partners;
- A 100% interest in that part of Block 22/14d that contains the 3D seismically mapped extension of the Jurassic discovery which underlies Huntington; and
- Carrizo UK's ring-fenced tax losses totaling approximately USD$125 million as at the transaction effective date of July 1st, 2012.

On March 5, 2013, the Company announced that pursuant to the terms of its stock option plan, its Board of Directors had approved the granting of options to purchase an aggregate of 7,420,000 common shares at a price of $0.63 per share, of which, 5,970,000 options were granted to insiders. The options will have a term of five years and time vesting provisions with 25% vesting immediately and a further 25% vesting on the first, second and third anniversaries of the date of grant.

CORPORATE INFORMATION

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Calgary, Alberta

Rod Maxwell [1][3]
Calgary, Alberta

Jay Zammit [1][2][4]
Calgary, Alberta

[1]Member of Audit Committee
[2]Member of Compensation Committee
[3]Member of Reserve Committee
[4]Member of the Governance Committee
[5]Member of the Health, Safety and Environment Committee

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Graham A. Heath
Interim Chief Financial Officer

Alan Curran[5]
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Peter F. Campbell[5]
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