ShaMaran Petroleum Corp

Annual Report

For the year ended December 31, 2011

Significant accounting policies

Details of the significant accounting policies and methods adopted, including the criteria for recognition, basis of measurement and the basis on which income and expenses are recognized in respect of each class of financial assets and liability are disclosed in note 3.

Financial risk management objectives

The Company's management monitors and manages the Company's exposure to financial risks facing the operations. These financial risks include market risk (including commodity price, foreign currency and interest rate risks), credit risk and liquidity risk.

The Company does not presently hedge against these risks as the benefits of entering into such agreements is not considered to be significant enough as to outweigh the significant cost and administrative burden associated with such hedging contracts.

Commodity price risk

The prices that the Company receives for its oil and gas production may have a significant impact on the Company's revenues and cash flows provided by operations. World prices for oil and gas are characterized by significant fluctuations that are determined by the global balance of supply and demand and worldwide political developments and in particular the price received for the Company's oil and gas production in Kurdistan is dependent upon the Kurdistan government and its ability to export production outside of Iraq. A significant decline in the price at which the Company can sell future oil and gas production could adversely affect the amount of funds available for capital reinvestment purposes as well as the Company's value in use calculations for impairment test purposes.

The Company does not hedge against commodity price risk, however given that the Company is in the exploration and development stage, it is not exposed to significant commodity price risk.

Foreign currency risk management

The Company maintains a substantial portion of its cash and cash equivalents in Canadian dollars; however, the Company's operations are conducted predominantly in United States dollars. As a result, the Company is exposed to foreign currency risk due to exchange rate fluctuations between the Canadian dollar ("CAD") and the reporting currency of the Company, the United States dollar ("USD").

In addition, Company entities undertake certain transactions denominated in foreign currencies, being any currency other than the functional currency of the Company entity.

The Company has elected not to hedge its exposure to the risk of changes in foreign currency exchange rates.

The carrying amounts of the Company's principal monetary assets and liabilities denominated in foreign currency at the reporting date are as follows:

	Assets		**Liabilities**	
	2011	**2010**	**2011**	**2010**
Canadian dollars in thousands ("CAD 000")	42,165	50,432	618	90
Swiss francs in thousands ("CHF 000")	685	243	346	597

Foreign currency sensitivity analysis:

The Company is exposed primarily to movements in CAD against the USD, the presentational currency of the Company. Funds are raised through the issuance of equity instruments in CAD and are held in CAD until they are required to fund operations at which time they are converted into USD. Sensitivity analyses have been performed to indicate how the profit or loss would have been affected by changes in the exchange rates between the USD and CAD. The analysis below is based on a strengthening of the USD by 1% against the USD in which the Company has significant assets and liabilities at the end of respective period. A movement of 1% reflects a reasonably possible sensitivity when compared to historical movements over a three to five year timeframe. The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjust their translation at the period end for a 1% change in foreign currency rates.

A positive number in the table below indicates an increase in profit where USD weakens 1% against the CAD on the basis of the CAD assets and liabilities held by the Company at the balance sheet dates. For a 1% strengthening of the USD against the CAD there would be an equal and opposite impact on the profit or loss.

	Assets		**Liabilities**	
	2011	**2010**	**2011**	**2010**
Income statement	408	488	(6)	(1)

Interest rate risk management

The Company earns interest income at variable rates on its cash and cash equivalents and is therefore exposed to interest rate risk due to a fluctuation in short-term interest rates.

The Company's policy on interest rate management is to maintain a certain amount of funds in the form of cash and cash equivalents for short-term liabilities and to have the remainder held on relatively short-term deposits.

Interest rate sensitivity analysis:

Based on exposure to the interest rates for cash and cash equivalents at the balance sheet date a 0.5% increase or decrease would not have a material impact on the Company's profit or loss for the year. A rate of 0.5% is used as it represents management's assessment of the reasonably possible changes in interest rates.

Credit risk management

Credit risk is the risk that a counterparty will default on its contractual obligations resulting in financial loss to the Company. The Company is primarily exposed to credit risk on its cash and cash equivalents and trade and other receivables. Trade and other receivables are primarily with joint venture partners in the oil and gas industry and are subject to normal industry credit risks. Joint venture receivables are typically collected within one to two months of the joint venture bill being issued to the partner. The Company mitigates risks arising from joint venture receivables by obtaining partner approval of capital expenditures prior to starting a project.

The Company manages credit risk by monitoring counterparty ratings and credit limits and by maintaining excess cash and cash equivalents on account in instruments having a minimum credit rating of R-1 (mid) or better (as measured by Dominion Bond Rate Services) or the equivalent thereof according to a recognized bond rating service.

The carrying amount of the Company's financial assets recorded in the consolidated financial statements represent the Company's maximum exposure to credit risk.

(Expressed in thousands of United States Dollars unless otherwise stated)

Liquidity risk management

Liquidity risk is the risk that the Company will have difficulties meeting its financial obligations as they become due. In common with many oil and gas exploration companies, the Company raises financing for its exploration and appraisal activities in discrete tranches in order to finance its activities for limited periods. The Company seeks to raise additional funding as and when required. The Company anticipates making substantial capital expenditures in the future for the acquisition, exploration, development and production of oil and gas reserves and as the Company's projects move into the development stage, specific financing, including the possibility of debt, may be required to enable future development to take place. The financial results of the Company will impact its access to the capital markets necessary to undertake or complete future drilling and development programs. There can be no assurance that debt or equity financing, or future cash generated by operations, would be available or sufficient to meet these requirements or, if debt or equity financing is available, that it will be on terms acceptable to the Company.

It is presently the Company's policy to finance its business by means of internally generated funds and external share capital. The Company manages liquidity risk by maintaining adequate cash reserves and by continuously monitoring forecast and actual cash flows. Annual capital expenditure budgets are prepared, which are regularly monitored and updated as considered necessary. In addition, the Company requires authorizations for expenditure on both operating and non-operating projects to further manage capital expenditures.

The maturity profile of the Company's financial liabilities are indicated by their classification in the consolidated balance sheet as "current" or "non-current", and further information relevant to the Company's liquidity position is disclosed in the Company's going concern assessment in note 2.

22. Related party transactions

	Purchases of services during the year		Amounts owing at the reporting dates	
	2011	**2010**	**2011**	**2010**
Namdo Management Services Ltd.	361	185	7	-
Mile High Holdings Ltd.	103	152	19	12
McCullough O'Connor Irwin LLP	56	41	14	-
Vostok Naphta Investment Ltd.	24	-	-	-
Lundin Petroleum AB	2,176	2,673	78	214
Total	**2,720**	**3,051**	**118**	**226**

Namdo Management Services Ltd. is a private corporation owned by a shareholder of the Company which has provided corporate administrative support and investor relation services to the Company.

Mile High Holdings Ltd. is a private corporation associated with a shareholder of the Company which has provided transportation services to the Company in relation to its fundraising activities.

McCullough O'Connor Irwin LLP is a law firm in which an officer of the Company is a partner which has provided legal services to the Company.

Vostok Naphta Investment Ltd. is a corporation traded on the NASDAQ OMX Nordic Exchange in Stockholm (trading symbol VNIL SDB) associated with a shareholder of the Company and which has provided investor relations services to the Company in relation to its fundraising activities in Sweden.

The Company receives services from various subsidiary companies of Lundin Petroleum AB ("Lundin"), a shareholder of the Company. Lundin charges during the year ended December 31, 2011 of $2,176 (2010: $2,673) were comprised of G&G and other technical service costs of $195 (2010: $382), reimbursement for Company travel and related expenses of $611 (2010: $601), office rental, administrative and building services of $455 (2010: $328) and $915 (2010: $1,362) relating to a guarantee provided to the KRG on behalf of the Company in respect of its minimum financial commitments, payable semi-annually and charged at a rate of 1.5 % per annum (3.0% prior to July 1, 2010).

Included within general and administrative expenses are contributions totalling $1,025 made in the year 2011 (2010: $485) to a charitable foundation whose Chairman is a major shareholder of the Company. Funds from this charity, in part, are used for community investment activity in Kurdistan.

All transactions with related parties are in the normal course of business and are made on the same terms and conditions as with parties at arm's length.

Refer also to note 23.

23. Events after the balance sheet date

On January 17, 2012 the Company signed a final binding agreement with the KRG to relinquish to the KRG the 60% working interests previously held in each of the Arbat and Pulkhana Production Sharing Contracts ("PSC"). Under the terms of the agreement the PSC for each of the Pulkhana and Arbat blocks was terminated whereby ShaMaran's interests in both PSCs were relinquished. On January 25, 2012 the Company paid a total of USD 25 million to the KRG, which will be expensed in 2012, in accordance with the terms of the agreement and relieving the Company of all further obligations under the PSCs.

On April 2, 2012 the Company entered into a debenture financing from two related parties (the "Lenders") in the principal amount of US$10,000,000 (the "Loan") on the following terms and conditions. The Loan will mature and be payable six months after closing of the Loan transaction (the "Maturity Date") and can be prepaid up to the Maturity Date without interest or penalty. Subsequent to the Maturity date interest will accrue on any unpaid Loan balance at 5% per annum commencing on the earlier of the Maturity Date or an event of default under the Debenture, and will be payable semi-annually thereafter. The Debenture is secured against the shares of the Company's operating subsidiaries. In connection with the Loan the Company has issued to the Lenders an aggregate of 3,000,000 common shares of the Company.

SHAMARAN PETROLEUM CORP.

DIRECTORS

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Director
Calgary, Alberta

Alexandre Schneiter
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J. Cameron Bailey
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STOCK EXCHANGE LISTINGS
TSX Venture Exchange and
NASDAQ OMX First North Exchange
Trading Symbol: SNM

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