

Longreach Oil and Gas Limited
Consolidated Financial Statements
December 31, 2013

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INDEPENDENT AUDITOR'S REPORT

To the Shareholders of Longreach Oil and Gas Limited:

We have audited the accompanying consolidated financial statements of Longreach Oil and Gas Limited and its subsidiaries, which comprise the consolidated statements of financial position as at December 31, 2013 and December 31, 2012, 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 Longreach Oil and Gas Limited and its subsidiaries as at December 31, 2013 and December 31, 2012, and their financial performance and their cash flows for the years then ended in accordance with International Financial Reporting Standards.

Emphasis of Matter

Without qualifying our opinion, we draw attention to Note 2 to the consolidated financial statements which describe matters and conditions that indicate the existence of a material uncertainty that may cast significant doubt about Longreach Oil and Gas Limited's ability to continue as a going concern.

"Deloitte LLP"

Chartered Accountants

April 22, 2014
Calgary, Canada

Longreach Oil and Gas Limited
Consolidated Statements of Financial Position
In United States Dollars

	Notes	December 31, 2013	December 31, 2012
Assets			
Current			
Cash and cash equivalents		\$ 12,305,037	\$ 30,669,483
Other current assets		63,141	353,927
Restricted cash	5	<u>327,163</u>	<u>3,204,109</u>
		<u>12,695,341</u>	<u>34,227,519</u>
Non-current			
Restricted cash	5	3,100,000	-
Investment and advances	6	181,155	181,155
Exploration and evaluation assets	7	25,476,298	7,637,312
Property and equipment	8	<u>114,677</u>	<u>22,157</u>
		<u>28,872,190</u>	<u>7,840,624</u>
		\$ 41,567,471	\$ 42,068,143
Liabilities			
Current			
Accounts payable and accrued liabilities		\$ 8,777,284	\$ 1,260,039
Related party loan and other liabilities	9	<u>-</u>	<u>406,833</u>
		<u>8,777,284</u>	<u>1,666,872</u>
Decommissioning obligations	10	752,051	-
Warrant value attributed in equity financing	12	<u>-</u>	<u>33,779</u>
		<u>9,529,335</u>	<u>1,700,651</u>
Shareholders' Equity			
Share capital	11	50,731,693	50,797,099
Share based payment reserve		4,139,390	2,903,402
Deficit		<u>(22,832,947)</u>	<u>(13,333,009)</u>
		<u>32,038,136</u>	<u>40,367,492</u>
		\$ 41,567,471	\$ 42,068,143

On behalf of the Board:

"Signed Dennis A. Sharp" Director
Director – Dennis A Sharp

"Signed Thomas R. Vukovich" Director
Director – Thomas R. Vukovich

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

Longreach Oil and Gas Limited
Consolidated Statements of Operations and
Comprehensive Loss
In United States Dollars

	Notes	December 31, 2013	December 31, 2012
Expenses			
Administrative	15	\$ 4,453,769	\$ 2,126,324
Acquisition of APIC	4	-	10,397,249
Share based payments		746,250	150,880
Depreciation	8	36,691	8,127
Foreign exchange loss		672,246	69,462
Accretion expense	10	2,051	-
Impairment of exploration and evaluation	7	2,151,594	-
Penalty provision of exploration and evaluation	13(c)	1,500,000	-
		<u>9,562,601</u>	<u>12,752,042</u>
Other income			
Finance income:			
Interest		45,773	107,271
Unrealised gain on warrant fair value adjustment	11	16,890	310,695
		<u>62,663</u>	<u>417,966</u>
Net and comprehensive loss for the year		\$ (9,499,938)	\$ (12,334,076)
Net loss per share			
- Basic and diluted		\$ (0.12)	\$ (0.49)
Weighted average shares outstanding			
- Basic and diluted		81,114,410	25,037,008
<i>(1) The options and warrants have been excluded from the diluted loss per share computation as they are anti-dilutive.</i>			

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

Longreach Oil and Gas Limited
Consolidated Statements of Changes in Shareholders' Equity
In United States Dollars

	Share Capital	Share Based Payment Reserve	Deficit	Total Equity
Balance, December 31, 2012	\$ 50,797,099	\$ 2,903,402	\$ (13,333,009)	\$ 40,367,492
Net loss for the year	-	-	(9,499,938)	(9,499,938)
Expiry of warrants	(294,668)	294,668	-	-
Issue of shares	221,762	-	-	221,762
Exercise of options	7,500	(7,500)	-	-
Share-based payments	-	948,820	-	948,820
Balance, December 31, 2013	\$ 50,731,693	\$ 4,139,390	\$ (22,832,947)	\$ 32,038,136

	Share Capital	Share Based Payment Reserve	Deficit	Total Equity
Balance, December 31, 2011	\$ 10,277,217	\$ 2,265,889	\$ (998,933)	\$ 11,544,173
Net loss for the year	-	-	(12,334,076)	(12,334,076)
Expiry of warrants	(94,080)	94,080	-	-
Issue of shares	40,613,962	-	-	40,613,962
Share-based payments	-	543,433	-	543,433
Balance, December 31, 2012	\$ 50,797,099	\$ 2,903,402	\$ (13,333,009)	\$ 40,367,492

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

Longreach Oil and Gas Limited
Consolidated Statements of Cash Flows
In United States Dollars

For the year ended December 31,	Notes	2013	2012
Cash flows from (used in) operating activities			
Net loss for the year		\$ (9,499,938)	\$ (12,334,076)
Items not involving cash:			
Unrealised foreign exchange loss		4,640	260,493
Share based payments		746,250	150,880
Acquisition of APIC	4	-	10,397,249
Unrealised gain on warrant fair market value adjustment	12	(16,890)	(310,695)
Exploration and evaluation impairment	7	2,151,594	-
Depreciation	8	36,691	8,127
License penalty accrual	13(c)	1,500,000	-
Changes in non-cash working capital balances:			
Accounts receivable		290,786	(159,819)
Accounts payable and accrued liabilities		465,636	374,194
Cash flow used in operating activities		<u>(4,321,231)</u>	<u>(1,613,647)</u>
Cash flows from (used in) financing activities			
Loan payable	9	(406,833)	(813,546)
Net cash acquired on the acquisition	4	-	30,371,841
Issue of common shares		204,972	-
Share issuance costs		-	(147,500)
Cash flow (used in) from financing activities		<u>(201,861)</u>	<u>29,410,795</u>
Cash flows from (used in) investing activities			
Expenditures on property and equipment	8	(129,211)	(20,147)
Expenditures on exploration and evaluation assets	7	(13,486,246)	(4,084,193)
Restricted cash	5	(223,054)	1,250,099
Cash flow used in investing activities		<u>(13,838,511)</u>	<u>(2,854,241)</u>
Effect of exchange rate changes on cash		<u>(2,843)</u>	<u>(242,819)</u>
Increase (decrease) in cash and cash equivalents		(18,364,446)	24,700,088
Cash and cash equivalents, beginning of year		<u>30,669,483</u>	<u>5,969,395</u>
Cash and cash equivalents, end of year		\$ 12,305,037	\$ 30,669,483
Cash and cash equivalents comprised of:			
Cash		\$ 12,305,037	\$ 5,591,983
Short-term deposits		-	25,077,500
		<u>\$ 12,305,037</u>	<u>\$ 30,669,483</u>
Supplemental information			
Interest paid		\$ -	\$ -
Corporate taxes paid		\$ -	\$ -

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

Longreach Oil and Gas Limited
Notes to Consolidated Financial Statements
In United States Dollars

As at and for the years ended December 31, 2013 and 2012

1. Corporate Information

Longreach Oil And Gas Limited ("Longreach" or "the Company") is a publicly traded corporation on the TSX Venture Exchange ("TSX-V") under the trading symbol LOI that is engaged in the evaluation, acquisition, exploration and development of oil and gas properties in Morocco with four exploration licences (*Sidi Moktar onshore, Zag onshore, Sidi Moussa offshore and Foun Draa offshore*).

Longreach is a Jersey limited company governed by the Companies (Jersey) Law 1991 (the "CJL"). The registered office of the Company is located at Queensway House, St Helier, Jersey, Channel Islands, JE1 1ES.

The Company's business is the business carried on by its wholly-owned subsidiary, Ventures, and that carried on by Longreach Oil and Gas Limited. Ventures was incorporated as a Jersey limited company under the CJL on April 4, 2006. Chairman Capital Corp., a capital pool company and predecessor of Longreach, was incorporated under the Business Corporations Act (Ontario) on May 31, 2006. On August 12, 2010, in connection with a proposed reverse takeover by Ventures, Chairman Capital Corp. changed its name to "Longreach Oil and Gas Limited", and consolidated its outstanding securities on a 5-to-1 basis. On September 24, 2010, the Company completed a reverse takeover with Ventures (the "Transaction"), which constituted the Company's qualifying transaction under the Exchange policies governing capital pool companies.

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

<u>Name of Subsidiary</u>	<u>Jurisdiction of Incorporation</u>	<u>Ownership</u>
Longreach Oil and Gas Ventures Limited	Jersey, Channel Islands	100%
Longreach Oil and Gas (Canada) Limited	Canada	100%
Longreach Oil and Gas (UK) Ltd.	United Kingdom	100%

2. Basis of Presentation

Statement of compliance

The Company prepares its consolidated financial statements in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board (IASB).

The policies applied in these consolidated financial statements are based on IFRS issued and outstanding as of April 22, 2014, the date they were approved and authorised for issuance by the Board of Directors ("the Board").

Going concern assumption

The Company is in the process of exploring its oil and gas properties and has not yet established whether the properties contain reserves that are economically recoverable. The recovery of amounts capitalised for property interests on the consolidated statement of financial position are dependent upon the existence of economically recoverable hydrocarbons, the ability of the Company to complete exploration and/or development of the properties, including related financing requirements and upon future profitable production or, alternatively, upon proceeds from the disposition of the properties. To date, the Company has not earned revenues relative to its costs incurred for exploration activities. These consolidated financial statements have been prepared on a going concern basis, under which the Company is assumed to be able to realise its assets and discharge its liabilities in the normal course of operations. The Company's ongoing activities are dependent upon its ability to obtain sufficient financing to fund its current and future operations and future acquisition costs. There is no certainty that such financing will be obtained on terms acceptable to management which may cast significant doubt about the Company's

Longreach Oil and Gas Limited
Notes to Consolidated Financial Statements
In United States Dollars

As at and for the years ended December 31, 2013 and 2012

2. Basis of Presentation - continued

ability to continue as a going concern. The consolidated financial statements do not reflect adjustments that would be necessary if the going concern assumptions were not appropriate. If the going concern basis was not appropriate for these consolidated financial statements, then adjustments would be necessary in the carrying value of property and equipment, liabilities, the reported expenses, and the classifications used in the consolidated statement of financial position. Such adjustments could be material. In order to fund Longreach's near term exploration programme and administrative expenditures the Company completed an interim debenture financing of \$9.7 Million (Canadian) in April 2014 (Note 17(b)) and intends to obtain further financing in 2014 which may include a rights offering or private placement.

Functional and presentation currency

These consolidated financial statements are presented in United States ("US") Dollars, which is also the Company and its subsidiaries functional currency. The following are the US Dollar foreign exchange rates at the respective years:

Currency	December 31, 2013	December 31, 2012
Average rates for the year:		
Pounds Sterling	0.6395	0.6310
Canadian Dollar	1.0298	0.9996
Euro	0.7532	0.7781
Moroccan Dirhams	8.3287	-
Year end rates:		
Pounds Sterling	0.6064	0.6185
Canadian Dollar	1.0694	0.9966
Euro	0.7263	0.7565
Moroccan Dirhams	8.0589	-

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 period. 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 the directors in the preparation of these consolidated financial statements are as follows:

- i. The consolidated financial statements include accruals and provisions based on management's interpretation of the terms of existing license terms and commitments. Best available information is used to determine the accruals at each period end. The Company is at varying stages of negotiations with certain partners to settle differences in opinion of the obligations of each party under existing agreements. The accruals made by management in this regard may be significantly different from those determined by the Company's partners or amounts agreed to as a result of negotiations. The effect on the consolidated financial statements resulting from such adjustments, if any, may be material and will be reflected prospectively.
- ii. Costs associated with acquiring oil and natural gas licenses and exploratory drilling are accumulated as exploration and evaluation ("E&E") assets pending determination of technical feasibility and commercial viability. Establishment of technical feasibility and commercial viability is subject to judgment which management has determined to be based on the allocation of commercial reserves to the exploration area. Upon determination of commercial reserves, E&E assets attributable to those reserves are first tested for impairment and then reclassified from E&E assets to a separate category within tangible assets referred to as oil and natural gas properties.

Longreach Oil and Gas Limited
Notes to Consolidated Financial Statements
In United States Dollars

As at and for the years ended December 31, 2013 and 2012

2. Basis of Presentation - continued

- iii. Amounts recorded for decommissioning obligations and the related accretion expense requires the use of estimates with respect to the amount and timing of decommissioning expenditures. Other provisions are recognised in the period when it becomes probable that there will be a future cash outflow. In 2013, the Company recorded a decommissioning obligation on its Koba-1 well at Sidi Moktar.
 - iv. Compensation costs recognised 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.
 - v. The Company's non-compensation based warrants are treated as derivative financial liabilities. The estimated fair value of each is adjusted on a quarterly basis with gains or losses recognised in the statement of operations and comprehensive income. The Black-Scholes model is based on significant assumptions such as volatility, dividend yield and expected term.
 - vi. Tax interpretations, regulations and legislation in the various jurisdictions in which the Company operates are subject to change. Therefore, 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 realised from future taxable earnings. The Company has yet to record any deferred tax assets or liabilities.
 - vii. The recoverability of the Company's investment is dependent on the liquidity of a private Company's shares, which is based in part on its performance. The Company will assess at each reporting period whether there is any objective evidence that a financial asset has been impaired. When the fair value of the investment cannot be derived from active markets, they are determined using recent transactions or a variety of valuation techniques that may include the use of mathematical models. The inputs to these models are taken from observable markets where possible, but where this is not feasible, a degree of judgment is required in establishing fair values. The judgments include considerations of liquidity and model inputs such as volatility. Changes in assumptions about these factors could affect the reported fair value of financial instruments.
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3. Summary of Significant Accounting Policies

The significant accounting policies used in the preparation of these consolidated financial statements are described below.

Basis of consolidation:

(i) Subsidiaries:

Subsidiaries are entities controlled by the Company. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases or the subsidiaries become dormant.

The purchase 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 acquisition over the fair value of the identifiable assets, liabilities and contingent liabilities acquired is recorded as goodwill. If the cost of the acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised immediately in the statement of operations and comprehensive income (loss).

(ii) Jointly controlled operations and jointly controlled assets:

Most 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 any relevant revenue and related costs.

Longreach Oil and Gas Limited
Notes to Consolidated Financial Statements
In United States Dollars

As at and for the years ended December 31, 2013 and 2012

3. Summary of Significant Accounting Policies – continued

- (iii) Transactions eliminated on consolidation:
Intercompany balances and transactions, and any unrealised income and expenses arising from intercompany transactions, are eliminated in preparing these consolidated financial statements.

Financial instruments:

- (i) Non-derivative financial instruments:
Non-derivative financial instruments comprise cash and cash equivalents, accounts receivables, restricted cash, investment and advances, accounts payable and accrued liabilities and related party loan and other liabilities. Non-derivative financial instruments are recognised initially at fair value net of any directly attributable transaction costs except for non-derivative instrument classified as fair value through profit and loss ("FVPL"). Subsequent to initial recognition, non-derivative 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 profit and loss 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, directly attributable transaction costs are recognised in earnings when incurred. Financial instruments at fair value through earnings are measured at fair value, and changes therein are recognised in earnings.

Other:

Other non-derivative financial instruments, such as accounts receivable, accounts payable and accrued liabilities, and related party loan and other liabilities are measured at amortised cost using the effective interest method. The Company's investments are classified as available for sale.

- (ii) Derivative financial instruments:
The Company may enter into certain financial derivative contracts in order to manage the exposure to market risks from fluctuations in commodity or currency prices. These instruments are not used for trading or speculative purposes. The Company has not designated its financial derivative contracts as effective accounting hedges, and thus not applied hedge accounting, even though the Company considers all commodity contracts to be economic hedges. All financial derivative contracts when entered into will be classified as fair value through earnings and are recorded on the statement of financial position at fair value. Transaction costs are recognised in earnings when incurred.

Embedded derivatives are 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 recognised immediately in earnings. Certain warrants issued by the Company are considered as further discussed below.

- (iii) Share capital
Common shares are classified as equity. Incremental costs directly attributable to the issue of common shares and share options are recognised as a deduction from share capital, net of any tax effects.

- (iv) Warrants
The non-compensation based warrants entitle the holder to acquire a fixed number of common shares for a fixed Canadian Dollar price per share. An obligation to issue shares for a price that is not fixed in the Company's functional currency of United States Dollars, and that does not qualify as a share based payment, must be classified as a derivative liability and measured at fair value with changes recognised in the statements of operations and comprehensive income (loss) as they arise. The Company has recorded these changes as financing income and expenses. The transaction costs associated with the issuance of the warrants are expensed when incurred.
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Longreach Oil and Gas Limited
Notes to Consolidated Financial Statements
In United States Dollars

As at and for the years ended December 31, 2013 and 2012

3. Summary of Significant Accounting Policies – continued

Foreign Currency Translation:

The consolidated financial statements are presented in United States dollars which is the reporting and functional currency. Transactions denominated in a currency other than the functional currency are translated at the prevailing rates on the date of the transaction. Any monetary items held in a currency which is not the functional currency are translated to the functional currency at the prevailing rate as at the date of the statement of financial position. All exchange differences arising as a result of the translation to the functional currency are recorded in net income (loss) from operations.

Property, plant and equipment and exploration and evaluation assets:

Exploration and evaluation expenditures:

Pre-licence costs are recognised in the statement of operations when incurred. Exploration and evaluation costs, including the costs of acquiring undeveloped land and drilling costs are initially capitalised until the drilling of the well is complete and the results have been evaluated. The costs are accumulated in cost centres 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 reserves are determined to exist. If proved reserves are found, the drilling costs and associated undeveloped land are assessed for impairment when transferred to property, plant and equipment. The cost of licenses on undeveloped land that expire or any impairment recognised during a period, is charged as an impairment expense and if not material charged to depletion and depreciation expense.

Exploration and evaluation assets are also 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"). The Company has grouped its exploration and evaluation assets into the following five CGU's: Sidi Moktar onshore, Sidi Moussa offshore, Foum Draa offshore and Zag Basin onshore.

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

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 amortised 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 recognised in the statement of operations and comprehensive income (loss).

An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognised. For financial assets measured at amortised cost the reversal is recognised in the statements of operations and comprehensive income (loss).

(ii) Non-financial assets:

The carrying amounts of the Company's non-financial assets, other than exploration and evaluation 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. Exploration and evaluation assets are assessed for impairment when they are transferred to property, plant and equipment, and also if facts and circumstances suggest that the carrying amount exceeds the recoverable amount.

Longreach Oil and Gas Limited
Notes to Consolidated Financial Statements
In United States Dollars

As at and for the years ended December 31, 2013 and 2012

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 may be 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 may be 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 utilising geological, production, recovery and economic projections.

Any 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. Exploration and evaluation assets are allocated to related CGUs 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, plant and equipment).

An impairment loss in respect of goodwill is not reversed. In respect of other assets, impairment losses recognised 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 recognised.

Share based payment:

The Company has established a share based payment plan (the "Plan") comprised of a Stock Option Plan (refer to note 11 for further details of the Plan). The Company uses the fair value method for valuing share based payment. 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 share based payment reserve. 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 recognised value in share based payment reserve is recorded as an increase to shareholders' equity.

Provisions:

A provision is recognised 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 recognised for future operating losses.

Longreach Oil and Gas Limited
Notes to Consolidated Financial Statements
In United States Dollars

As at and for the years ended December 31, 2013 and 2012

3. Summary of Significant Accounting Policies – continued

Decommissioning obligations:

The Company's activities may give rise to dismantling, decommissioning and site disturbance remediation activities. Provision is made for the estimated cost of abandonment and site restoration and capitalised 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. 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 recognised as accretion expense whereas increases/decreases due to changes in the estimated future cash flows or changes in the discount rate are capitalised. Actual costs incurred upon settlement of the decommissioning obligations are charged against the provision to the extent the provision was established.

Revenue:

Revenue from the sale of oil and natural gas is recorded when the significant risks and rewards of ownership of the product is transferred to the buyer which is usually when legal title passes to the external party.

Royalty income is recognised as it accrues in accordance with the terms of any overriding royalty agreements.

Income tax:

Income tax expense is comprised of current and deferred tax. Income tax expense is recognised in the statements of operations and comprehensive income (loss) except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity. Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted substantively at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised 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 recognised on the initial recognition of assets or liabilities in a transaction that is not a business combination. 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 realised simultaneously.

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilised. 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 realised.

Income (loss) per share:

Basic income (loss) per share is calculated by dividing the net income or loss attributable to common shareholders of the Company by the weighted average number of common shares outstanding during the period. Diluted per share amounts are calculated based on the treasury stock method, which assumes that any proceeds obtained on the exercise of the in the money stock options and warrants would be used to purchase common shares at the average market price for the period.

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3. Summary of Significant Accounting Policies – continued

New standards and interpretations:

Effective January 1, 2013 the Company has adopted the following standards, IFRS 7 – “Financial Instruments – Disclosures”, IFRS 10 – “Consolidated Financial Statements”, IFRS 11 – “Joint Arrangements”, IFRS 12 – “Disclosure of Interests in Other Entities”, and IFRS 13 – “Fair Value Measurements”. The adoption of these standards has not had any impact on the Company’s consolidated financial statements and related disclosures.

The Company will be required to adopt the following applicable new standards and amendments issued by the IASB, and is currently evaluating the impact on the consolidated financial statements as discussed below.

i) IFRIC 21, “Levies” provides guidance on accounting for levies in accordance with the requirements of IAS 37, Provisions, Contingent Liabilities and Contingent Assets. The interpretation defines a levy as an outflow from an entity imposed by a government in accordance with legislation and states that levies do not arise from executory contracts or other contractual arrangements. The interpretation also confirms that an entity recognizes a liability for a levy only when the triggering event specified in the legislation occurs. This IFRIC is effective for annual periods commencing on or after January 1, 2014 and is to be applied retrospectively. The Company will adopt IFRIC 21 in its financial statements for the annual period beginning January 1, 2014.

ii) IFRS 9, as issued, reflects part of the IASB’s work on the replacement of IAS 39 “Financial Instruments: Recognition and Measurement” and applies to classification and measurement of financial assets and financial liabilities as defined in IAS 39 and hedging transactions. The standard has no effective date. In subsequent phases, the IASB will address impairment of financial assets. The adoption of IFRS 9 may have an effect on the classification and measurement of the Company’s financial assets and financial liabilities. The Company will quantify the effect in conjunction with the other phases, when the final standard including all phases is issued with an effective date.

Longreach has not applied any of these new standards as of December 31, 2013, and continues to evaluate the extent of the impact that adoption will have on the consolidated financial statements.

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4. APIC Transaction

On December 21, 2012, a statutory scheme arrangement (the "Transaction") under Jersey law whereby Longreach acquired APIC Petroleum Corporation ("APIC") via the issuance of one Longreach share for every 5.3846 APIC shares. The acquisition of APIC has been accounted for as an asset transaction, as the acquisition of APIC does not constitute a business combination for accounting purposes resulting in Longreach being the continuing entity for accounting purposes. The fair value of the net assets of APIC acquired have been recorded at their estimated fair value:

Net assets acquired:	
Cash	\$ 30,371,841
Other current assets	133,224
Investments and advances (Note 6)	180,000
Accounts payable and accrued liabilities	(54,834)
Non-compensatory replacement warrants (i)	(39,793)
Fair value of the net assets acquired	<u>\$ 30,590,438</u>
Consideration:	
57,363,747 ordinary shares (ii)	\$ 40,613,962
1,433,707 Replacement options (iii)	373,725
	<u>\$ 40,987,687</u>
Excess of consideration over net assets acquired included in statement of operations (iv)	<u>\$ 10,397,249</u>

- (i) Longreach also issued 580,358 non-compensatory replacement warrants exercisable at CAD\$0.646152. The fair market value of the warrants is \$39,793 and was estimated using the Black-Scholes option pricing model with the following assumptions: dividend yield – nil, expected volatility 50%, risk free rate – 1.1%, expected life – 0.06 years. The replacement warrants are non-compensatory in nature, they are treated as a derivative financial liability.
- (ii) The total consideration amount for the acquisition of APIC has been based on a share price of CAD \$0.70, which is the share price of Longreach on December 21, 2013, the closing date of the Transaction.
- (iii) Pursuant to the acquisition of APIC by Longreach, the Company issued 1,433,707 replacement options with 579,424 replacement options exercisable at CAD\$0.54 and 854,283 replacement options exercisable at CAD\$1.18. The weighted average fair market value per replacement option of CAD\$0.258 was estimated using the Black-Scholes option pricing model with the following assumptions: dividend yield – nil, expected volatility 70%, risk free rate – 1.5%, expected life from – 1.00 to 4.11 years and an estimated forfeiture rate 5%.
- (iv) The excess consideration over the fair value of the net assets acquired is recorded in the current period in the statement of operations and comprehensive loss.

The transaction between Longreach and APIC had the following related party features:

Longreach and APIC had a common Non-executive Director who declared his interest in respect to the Transaction as a result of serving on both Boards. The common Non-executive Director of APIC and Longreach abstained from voting in his capacity as a Director on the Transaction. Further, the Non-executive Director's employer received a transaction fee of \$100,000 (CAD) from APIC in connection with the completion of the APIC Transaction and \$484,840 of commissions related to the APIC private placement. The transaction fee and brokerage commission were considered to be at an arm's length rate.

In addition, a Longreach Non-executive Director participated in the APIC financing and was issued 142,857 Longreach shares.

The aforementioned payments are considered related party transactions and have been measured at the agreed to exchange amounts, which is the amount of consideration established and agreed to by the related parties.

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5. Restricted Cash

The Company has a restricted cash balance, which represents the following bank deposits securing licenses as follows:

	In favor of	December 31, 2013	December 31, 2012
Zag licence	San Leon	\$ -	\$ 150,000
Tarfaya licence (1)	San Leon	300,000	300,000
Zag exploration licence	San Leon	600,000	225,000
Sidi Moktar farm-in arrangement (Note 13(a))	MPE	2,500,000	2,500,000
Other (1)	Barclays	27,163	29,109
		<u>3,427,163</u>	<u>3,204,109</u>
Current portion of restricted cash		<u>(327,163)</u>	<u>(3,204,109)</u>
		<u>\$ 3,100,000</u>	<u>\$ -</u>

Additional details with respect to the work commitments of the licences are as disclosed in Note 13.

(1) Classified as current restricted cash in the 2013 financial year.

6. Investments and Advances

- (a) Longreach through the transaction with APIC (Note 4) acquired an 11.28% common equity interest in Aizan Technologies Inc. ("Aizan"), a private company, valued at approximately \$130,000 at December 31, 2013 and at the time of closing of the APIC transaction. Aizan is a private technology company providing cloud based voice solutions focused on intelligent call routing and intelligent call management.
- (b) The Company via the APIC transaction (Note 4) acquired a \$51,155 subordinated series D convertible debenture in Aizan bearing interest at 10% per annum which matures on March 31, 2014. Aizan has requested an extension with respect to the repayment of the debenture. The debenture is convertible into common shares on the following basis: (i) at a price of \$0.63 per share, at any time prior to the maturity date, upon the election of holders of not less than a specified majority percentage of all of the issued and outstanding series D debentures or (ii) upon the occurrence of a liquidity event at a price equal to the lessor of (a) \$0.63 per share and (b) 80% of the value attributable to each common share in such circumstance.

7. Exploration and Evaluation Assets

Balance, December 31, 2011	\$ 4,479,456
Additions	3,157,856
Balance, December 31, 2012	<u>7,637,312</u>
Additions	19,990,580
Impairment	(2,151,594)
Balance, December 31, 2013	<u>\$ 25,476,298</u>

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7. Exploration and Evaluation Assets - continued

The Company's exploration and evaluation assets consist entirely of costs pertaining to the Company's licences in Morocco. At December 31, 2013, the costs associated with the Tarfaya license were considered to be impaired as the required work commitments were not achieved and the license expired subsequent to year end. The evaluation of the technical feasibility or commercial viability of the other licences has not been established.

During the year, the Company capitalised \$501,200 (2012 - \$58,694) of administrative salaries and costs and \$202,570 (2012 - \$18,178) related to share based payments directly related to exploration and evaluation activities on the Sidi Moktar license.

8. Property and Equipment

Cost		
Balance, December 31, 2012	\$	35,037
Additions		<u>129,211</u>
Balance, December 31, 2013	\$	<u><u>164,248</u></u>
Accumulated depreciation		
Balance, December 31, 2012	\$	(12,880)
Depreciation charge		<u>(36,691)</u>
Balance, December 31, 2013	\$	<u><u>(49,571)</u></u>
Net book value		
Net book value, December 31, 2012	\$	<u>22,157</u>
Net book value, December 31, 2013	\$	<u><u>114,677</u></u>

All of the Company's property and equipment consists of office equipment and furniture and is located in Jersey, Morocco, Canada and in the United Kingdom.

9. Related party loan and other liabilities

As at December 31, 2012, the Company had loans payable of \$406,833 of which \$256,833 (£159,000) was due to a Director which was non-interest bearing, unsecured and due on demand. In 2013, the loan to the Director was re-paid in full and the \$150,000 that was held in trust for a joint venture partner was repaid.

10. Decommissioning Obligations

The following table presents the reconciliation of the beginning and ending aggregate carrying amount of the obligation associated with the decommissioning of oil and natural gas properties.

	December 31, 2013	December 31, 2012
Obligation, beginning of year	\$ -	\$ -
Liabilities incurred	750,000	-
Change in estimated cash flows	-	-
Accretion expenses	2,051	-
Obligation, end of year	<u>\$ 752,051</u>	<u>\$ -</u>

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10. Decommissioning Obligations - continued

The undiscounted amount of cash, required to settle the current obligation being only the Koba site restoration, adjusted for inflation, is estimated at \$796,000. The obligation was calculated using a risk free discount rate of 1.50 percent and an inflation rate of 2.0 percent. It is expected that the costs are expected to occur in 2017 but may be extended pending the final results of the Koba-1 well and extension of the Sidi Moktar license.

11. Share Capital

(a) Authorised

Unlimited number of Common Shares without nominal or par value

(b) Issued

	December 31, 2013		December 31, 2012	
	Issued	Amounts	Issued	Amounts
Common Shares				
Opening balance	80,829,145	\$ 50,502,432	23,465,398	\$ 9,888,470
APIC transaction (Note 4)	-	-	57,363,747	40,613,962
Exercise of warrants	290,179	206,760	-	-
Exercise of stock options	29,714	22,501	-	-
Balance, end of period	81,149,038	\$ 50,731,693	80,829,145	\$ 50,502,432
Warrants (Note 12)				
Opening balance	715,863	\$ 294,668	947,252	\$ 388,747
Agent warrants	-	-	-	-
Expired broker warrants	(715,863)	(294,668)	(231,389)	(94,080)
Balance, end of period	-	\$ -	715,863	\$ 294,667
		\$ 50,731,693		\$ 50,797,099

(c) Stock options

The Company has a stock option plan 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 vest at various rates as determined by the Board. The maximum term of the options is five years. The options are non-transferable if not exercised. A summary of the status of the Company's stock option plan as at December 31, 2013 and 2012 and changes during the respective years ended on those dates is presented below.

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11. Share Capital - continued

Stock Options	December 31, 2013		December 31, 2012	
	Number of options	Weighted average Exercise Price (CAD \$)	Number of options	Weighted average exercise price (CAD \$)
Beginning of year	3,133,707	\$0.94	1,700,000	\$1.10
Granted	4,145,000	\$0.70	500,000	\$0.60
APIC replacement grant	-	-	1,433,707	\$0.92
Exercised	(29,714)	\$0.54	-	-
Expired/Fortified	(895,568)	\$1.03	(500,000)	\$1.10
End of year	6,353,425	\$0.77	3,133,707	\$0.94
Exercisable, end of year	1,875,092	\$0.96	2,400,373	\$1.00

Date of Grant	Number Outstanding	Exercise Price (CAD \$)	Weighted Average Remaining Contractual Life	Date of Expiry	Number Exercisable December 31, 2013
August 16, 2011 (iii)	650,000	\$1.05	0.62 years	August 16, 2014	650,000
October 3, 2011	50,000	\$0.75	0.76 years	October 3, 2014	50,000
May 22, 2012 (iii)	500,000	\$0.60	3.39 years	May 22, 2017	166,667
December 21, 2012 (i)	181,999	\$0.54	0.71 years	September 17, 2014	181,999
December 21, 2012 (i)	139,284	\$0.54	1.29 years	April 15, 2015	139,284
December 21, 2012 (i)	687,142	\$1.18	3.16 years	February 28, 2017	687,142
January 15, 2013 (ii)	3,845,000	\$0.70	4.04 years	January 15, 2018	-
May 16, 2013 (iii)	300,000	\$0.70	4.38 years	May 16, 2018	-
	6,353,425		3.38 years		1,875,092

(i) Options issued pursuant to the APIC transaction (Note 4).

(ii) Subsequent to year end, 2,510,000 options were forfeited, of which 435,000 options were exercisable at \$0.60, 1,675,000 options were exercisable at \$0.70 and 400,000 options were exercisable at \$1.05.

The weighted average fair market value per option of approximately \$0.33 (CAD) was estimated using the Black-Scholes option pricing model with the following assumptions: dividend yield – nil, expected volatility 75% (2012 – 70%), risk free rate – 1.5% (2012 – 1.5%), expected life - 5 years (2012 – 5 years), an estimated forfeiture rate – 5% (2012 – 5%) and utilising the graded option method. The volatility was determined using the Company's trading volume.

(d) Escrowed securities

Pursuant to an Escrow Agreement, all of the 7,711,808 common shares and 390,104 share purchase warrants held by "principals" prior to the 2010 capital transaction, were deposited in trust and held in escrow. 10% of these shares were released on October 4, 2010 upon completion of the capital transaction and 15% will be released on each six month anniversary of that date. The Company has no common shares (2012 - 2,814,811) and no share purchase warrants (2012 - 175,547) remaining in escrow on December 31, 2013.

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12. Warrants Value Attributed in Equity Financing

(a) Warrants issued and outstanding

	December 31, 2013		December 31, 2012	
	Warrants	Amounts	Warrants	Amounts
Warrants (i)				
Opening balance	10,946,663	\$ 33,779	12,478,499	\$ 304,680
APIC replacement warrants (Note 4)	-	-	580,358	39,793
Exercised - non-compensatory	(290,179)	(16,889)	-	-
Expired – non-compensatory	(9,940,621)	NA	(1,880,805)	NA
Expired – compensatory	(715,863)	NA	(231,389)	NA
Fair value adjustment	-	(16,890)	-	(310,694)
Balance, end of period	-	\$ -	10,946,663	\$ 33,779

(i) Only values related to the non-compensatory warrants have been included in this table and do not include the compensatory warrants included in equity (Note 11(b)).

(b) Each non-compensatory warrant is measured at fair value quarterly using the Black-Scholes options pricing model. The fair value of warrants at December 31, 2013 and 2012 was estimated using the Black-Scholes options pricing model with the following weighted average assumptions:

	December 31, 2012
Number outstanding re-valued warrants, end of year	10,230,800
Fair value of warrants outstanding	\$0.003
Risk free interest rate	1.00%
Expected life	0.04 to 0.08 years
Expected volatility	40%

There were no warrants outstanding at December 31, 2013.

13. Commitments and Contingencies

(a) Sidi Moktar Farm-in

On May 16, 2012, Longreach entered into a Farm-in Agreement with Maghreb Petroleum Exploration S.A. ("MPE"). Pursuant to the Farm-in Agreement, Longreach will acquire a 50% interest in the onshore Sidi Moktar exploration licences referred to as Sidi Moktar West, Sidi Moktar South and Sidi Moktar North located in the Essaouira Basin in Central Morocco. In consideration for the acquisition of that interest, Longreach will be responsible for carrying out a work programme of acquiring, processing and interpreting new seismic data and drilling two earning wells by August 28, 2017. The Company has posted a bank guarantee of \$2.5 million (Note 5) with respect to this commitment.

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13. Commitments and Contingencies - continued

(b) Zag licence

Included in restricted cash is \$600,000 related to certain work commitments that need to be completed by May 2015. The Company has committed to its percentage share of further geophysical studies and the drilling of one exploration well. In 2012, the Company entered into an agreement with the operator whereby if the license is sold, farmed-out or other triggering event occurs, Longreach may be liable for up to \$1.1 million to the operator. This liability has not been recorded at the balance sheet date to the uncertainty of the triggering event occurring.

(c) Tarfaya licence

Included in restricted cash is \$300,000 related to certain work commitments that need to be completed by April 2014. The Company committed to its percentage share of further geophysical studies and the drilling of one exploratory well however, the operator subsequently failed to complete these commitments within the required licence period and Longreach is likely to be subject to an estimated penalty of \$1.5 million which has been accrued in these financial statements. The \$300,000 of restricted cash will be available to offset this estimated liability.

(d) Sidi Moussa licence

The Company has been advised by the operator Genel that it plans to drill an offshore exploration well targeting the Mid-Jurassic / Lower Triassic reservoirs in 2014. Longreach's estimated participation cost is approximately \$1 million.

(e) Rig Commitment

The Company at December 31, 2013 had a minimum financial commitment of \$1.8 million to a drilling contractor with respect to 2014 Sidi Moktar drilling activities.

(f) Office Leases

The Company has the following office lease agreements with monthly costs exclusive of common costs as follows:

Office Location	Currency of Rental Commitment	Total Base Rent Commitment	2014	2015	2016
Jersey	£	1,800	1,800	-	-
Morocco	€	21,600	16,200	5,400	-
UK	£	8,000	8,000	-	-
Canada	\$	91,266	40,326	40,752	10,188

The Jersey and United Kingdom office lease arrangements can be terminated on one and two months' notice respectively. The Morocco lease expires on March 31, 2015. The Canadian office lease arrangement expires on March 31, 2016.

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14. Financial Instruments

The Company may hold 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 minimises 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 financial instrument exposed to commodity risk.

(b) Market Risk

Market risk is comprised of two components: currency risk and interest rate risk.

(c) Credit Risk

Credit risk is the risk that arises when a party to a financial instrument will be unable to discharge its obligations as they become due. The Company's financial assets exposed to credit risk are cash and cash equivalents, restricted cash, and accounts receivable. Cash and cash equivalents and restricted cash is placed with major financial institutions. The maximum credit risk is approximate to the carrying value of such financial instruments. Management assesses quarterly if there should be any impairment of the financial assets of the Company. At December 31, 2013, none of the Company's financial assets are considered to be impaired.

(d) 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 is not exposed to interest rate risk as it borrows funds at a non-interest bearing rate as disclosed in Note 9. The Company currently does not use interest rate hedges or fixed interest rate contracts to manage the Company's exposure to interest rate fluctuations.

(e) Fair Value of Financial Instruments

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 instrument.

- Level 1 – Quoted prices are available in active markets for identical assets or liabilities as of the reporting date. Active markets are those in which transactions occur in sufficient frequency and volume to provide pricing information on an ongoing basis.
- Level 2 – Pricing inputs are other than quoted prices in active markets included in Level 1. Prices in Level 2 are either directly or indirectly observable as of the reporting date. Level 2 valuations are based on inputs, including quoted forward prices for commodities, time value and volatility factors, which can be substantially observed or corroborated in the marketplace.
- Level 3 – Valuations in this level are those with inputs for the asset or liability that are not based on observable market data.

Cash and cash equivalents and restricted cash have been classified as level 1. The investment in the Aizan convertible debenture (Note 6) and non-compensatory warrants (Note 12) are classified as level 2. The investment in the common equity of Aizan has been classified as level 3.

All financial assets (except for cash and cash equivalents and restricted cash which are classified as FVPL), are classified as either loans or receivables and are accounted for on an amortised cost basis. All financial liabilities are classified as other liabilities other than the warrants attributed to equity financing which are classified as FVPL. The investment in Aizan has been designated as available-for-sale. There have been no changes to the aforementioned classifications during the financial year ended December 31, 2013.

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14. Financial Instruments - continued

(f) Foreign Currency Exchange Risk

The Company operates on an international basis and therefore foreign exchange risk exposures arise from transactions denominated in currencies other than USD. 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, Moroccan Dirhams and Canadian Dollars and is exposed to fluctuations in exchange rates in these currencies. There are no exchange rate contracts in place at December 31, 2013 or 2012.

Assuming all other variables remain constant, a 1% increase or decrease in foreign exchange rates on the foreign cash balances at December 31, 2013 would have impacted the cash flows of the Company during the 2013 fiscal year by approximately \$38,000 (2012 - \$57,000).

(g) 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 a transaction on the due date;
- 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.

The Company's operating cash requirements including amounts projected to complete the Company's existing capital expenditure program are continuously monitored and adjusted as input variables change. These variables include but are not limited to results from new wells drilled, commodity prices, cost overruns on capital projects and regulations relating to prices, taxes, royalties, land tenure, allowable production and availability of markets. When these variables change, liquidity risks may necessitate the Company to conduct equity issues or obtain project debt financing. The loans payable are due on demand and the accounts payable have general terms ranging from 30 to 90 days from receipt of the invoice or joint venture billing. Note 2 further discusses the ability of the Company to meet its obligations as they come due.

15. Compensation to key management personnel

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Company. The Company's key management personnel are its directors and executive officers. Key management personnel compensation is comprised of the following:

	December 31, 2013	December 31, 2012
Executives and Executive Directors	\$ 1,144,332	\$ 518,785
Severance costs	405,427	-
Non-Executive Directors	115,000	120,000
Benefits and other personnel costs	25,479	12,419
Share based compensation	202,725	124,186
Total remuneration	<u>\$ 1,892,963</u>	<u>\$ 775,390</u>

Personnel expenses are recorded in general and administrative expenses. In 2013, \$471,385 (2012 - \$58,694) of expenses directly attributed to capital activities have been capitalised and included in exploration and evaluation assets.

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16. Capital Risk Management

The Company defines capital as total debt and shareholders' equity. The Board's policy is to maintain a capital base so as to maintain investor, creditor, and market confidence and sustain future development of the business.

The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern in order to pursue the development of its mineral properties and to maintain a flexible capital structure which optimises the costs of capital at an acceptable level of risk.

The Company manages the capital structure and makes adjustments to it in light of the economic conditions and the risk characteristics of the underlying assets. To maintain or adjust the capital structure, the Company may attempt to issue new shares, issue debt, acquire, or dispose of assets. In order to facilitate the management of its capital requirements the Company prepares an annual expenditure budget that is updated as necessary, depending on various factors. The Company has not changed its approach to capital management during the current year. The Company is not subject to any external capital restrictions. Longreach will be required to complete debt or equity financing to fund its exploration and development plans.

17. Subsequent Events

Except as disclosed elsewhere in these consolidated financial statements, the Company had the following subsequent events:

- (a) On March 20, 2014, the Company spudded the Kamar-1 well. The planned total depth is 3,500 metres and operations are expected to take approximately 70 days. The Kamar prospect is targeting a lower Liassic reservoir and a Triassic clastic reservoir.
 - (b) On April 10, 2014, Longreach completed a debenture financing of CAD\$9.7 million in order to fund the near term exploration programme of the Kamar-1 well, and administrative expenses. The debentures mature two years from the date of closing and bear an interest rate of 10% per annum, payable quarterly in arrears. Following the first anniversary of the date of closing, holders of Debentures may convert from time to time, in whole or in part, outstanding principal under the Debentures into Common Shares of the Company at a conversion price equal to the greater of: (a) CAD\$0.30 (subject to typical adjustments in certain circumstances); and (b) the current market price of the Shares at the time of conversion (based on the volume weighted average trading price of the Shares for the 20 trading days ending on the fifth trading day preceding the date of conversion). The Debentures provide customary events of default including failure to pay interest when due within 30 days, failure to repay principal on redemption or maturity, and the occurrence of insolvency events or proceedings. In addition, the Company has made certain covenants in favour of holders of Debentures, including covenanting not to incur additional indebtedness, covenanting to use commercially reasonable efforts to complete an equity financing within one year for the purpose of repaying or refinancing the Debentures, and covenanting to use commercially reasonable efforts to seek shareholder approval in certain circumstances for the creation of a new control person, if requested by a holder of Debentures who would otherwise need such approval in order to permit the full conversion of Debentures. The Company also issue the Debenture holders 9,700,000 warrants with each warrant being exercisable for a term of two years following closing and may be exercised for one Share at an exercise price of CAD\$0.30 per share (subject to typical adjustments in certain circumstances).
-