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PACIFIC RUBIALES ENERGY CORP.

MANAGEMENT DISCUSSION AND ANALYSIS

March 13, 2013

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For the year ended December 31, 2012

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1. Preface

This Management Discussion and Analysis ("**MD&A**") contains forward-looking information and is based on the current expectations, estimates, projections and assumptions of Pacific Rubiales Energy Corp. This information is subject to a number of risks and uncertainties, many of which are beyond the Company's control. Users of this information are cautioned that actual results may differ materially. For information on material risk factors and assumptions underlying our forward-looking information, see page 36.

This MD&A is management's assessment and analysis of the results and financial condition of the Company, and should be read in conjunction with the accompanying audited annual consolidated financial statements for the years ended December 31, 2012, and December 31, 2011 and related notes. The preparation of financial information is reported in United States dollars and is in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board ("**IASB**") unless otherwise noted. All comparative percentages are between the years and quarters ended December 31, 2012 and December 31, 2011, unless otherwise stated. The following financial measures: (i) EBITDA; (ii) funds flow from operations; and (iii) adjusted net earnings from operations, as referred to in this MD&A, are not prescribed by International Financial Reporting Standards ("**IFRS**") and are outlined under "Additional Financial Measures" on page 34. All references to net barrels or net production reflect only the Company's share of production and after deducting royalties. A list of abbreviations for oil and gas terms is provided on page 39.

In order to provide shareholders of the Company with full disclosure relating to potential future capital expenditures, we have provided cost estimates for projects that, in some cases, are still in the early stages of development. These costs are preliminary estimates only. The actual amounts are expected to differ and these differences may be material. For further discussion of the significant capital expenditures, see "Capital Expenditures" on page 20.

References to "**we**", "**our**", "**us**", "**Pacific Rubiales**", "**PRE**", or the "**Company**" mean Pacific Rubiales Energy Corp., its subsidiaries, partnerships and joint venture investments, unless the context otherwise requires. The table and charts in this document form an integral part of this MD&A.

Additional information relating to the Company filed with Canadian securities regulatory authorities, including the Company's quarterly and annual reports and the Annual Information Form, are available on SEDAR at www.sedar.com, SIMEV at www.superfinanciera.gov.co/web_valores/Simev, BOVESPA at www.bmfbovespa.com.br and on the Company's website at www.pacificrubiales.com. Information contained in or otherwise accessible through our website does not form a part of this MD&A and is not incorporated by reference into this MD&A.

This MD&A was prepared originally in the English language and subsequently translated into Spanish and Portuguese. In the case of any differences between the English version and its translated versions, the English document shall prevail and be treated as the governing version.

2. 2012 Year-End Highlights

During the year ended December 31, 2012, the Company continued its trend of production growth and exploratory success, leveraging its technical know-how and operational expertise. The results for this year underline the strength of the Company's assets, operational activity, capacity to increase production and delivery of robust financial results. Management is focused on meeting challenging operational goals, pursuing an ambitious exploration and production ("E&P") program, while delivering on its paramount strategic focus: Growth.

As part of this strategy, a new and more robust Company has emerged, not only from assuming the challenges of growing production from its existing fields in Colombia and building on the success of its exploratory program, but also as a result of the strategic acquisition of new and promising assets in other countries. During 2012, the Company completed the acquisition of PetroMagdalena Energy Corp. ("PetroMagdalena") and C&C Energia Ltd. ("C&C") in Colombia, and also acquired interests in offshore Brazilian assets from Karoon Gas Australia Ltd. ("Karoon"), Peruvian assets from BPZ Resources, Inc. ("BPZ"), Guyana assets through CGX Energy Inc. ("CGX") an equity investment and Papua New Guinea assets from InterOil Corporation ("InterOil").

Highlights of the Company's activities during the year-ended December 31, 2012 include:

- **Production continues to grow in 2012.** During 2012, the average net production after royalties and internal consumption in Colombia and Peru totaled 97,657 boe/d (246,575 boe/d total field production), representing an increase of 13% year-over-year. In Colombia, average net production reached 96,084 boe/d (243,264 boe/d total field production), driven by more than 246 development wells drilled mainly in the Rubiales and Quifa SW fields, and the production from the new acquisitions. In Peru, average net production for 2012 reached 1,573 bbl/d (3,311 bbl/d total field production) coming from the acquisition of a 49% participating interest in Block Z-1, which closed on December 12, 2012.

Production in Colombia and Peru continue to grow as average net production for the fourth quarter 2012 reached 108,149 boe/d (271,342 boe/d total field production) and as of March 11, 2013, production net after royalties stands at 128,051 boe/d (307,456 boe/d total field production), a 18% increase from the average net production reported for the fourth quarter 2012.

- **Significant growth in net after royalty Proved plus Probable reserves ("2P").** Total 2P net reserves grew to 513.7 MMboe at December 31, 2012, up 26% from 407.3 MMboe at December 31, 2011. The Company achieved a 2P reserves replacement of 398% and 2P Reserves Life Index ("RLI") increased to 14 from 13. Total net proved reserves ("1P") grew by 5% in the same period to 335.5 MMboe. Approximately 77% of net 2P and 74% of 1P reserves are oil and liquids with the majority of these being heavy oil. Significant reserves additions resulted from acquisitions (totaling 92 MMboe), including first reserves bookings and production in Peru in Block Z-1, and onshore Colombia additional reserves and production from the PetroMagdalena and C&C acquisitions. At year-end 2012, the Company continued its successful reserves base diversification, with the Rubiales field now representing less than 19% of total 2P reserves. See the heading entitled "Advisories" for further information regarding boe conversion.
- **Resource evaluation of 35 exploration Blocks.** The Company received independent resource assessment reports for some of the Company's exploration Blocks in Colombia (23), Peru (4), Brazil (4), Papua New Guinea (2) and Guatemala (2), resulting in a Best Estimate (P50) for contingent and prospective resources of 3,793 MMboe as of September 30, 2012 for those exploration Blocks.
- **Strong revenue generation.** The Company increased revenues to \$3,885 million compared to \$3,381 million in the same period of 2011, driven by a significant increase in production and in realized prices. Consolidated net earnings for the year 2012 were \$528 million or \$1.79 per common share, compared to \$554 million, or \$2.04 per common share in 2011. Adjusted net earnings from operations before non-cash items for the year 2012 were \$653 million compared to \$742 million in 2011.
- **EBITDA and Cash Flow Continue to Grow.** EBITDA for the year 2012 totaled \$2,018 million, compared to \$1,959 million during 2011. EBITDA for the year 2012 represented a 52% margin on total revenues for the period. Funds flow and cash flow from operations increased to \$1,388 million and \$1,803 million compared to \$1,369 million and \$1,219 million in 2011, respectively. See the heading entitled "Additional Financial Measures" for further information.
- **Operating Netbacks Remained Strong.** Combined oil and gas netback was \$60.20/boe, remained stable in comparison to 2011 (\$60.19/boe). Crude oil operating netback during the year 2012 remained strong at \$63.14/bbl, 1% lower than in 2011 (\$63.70/bbl).

- **Acquisitions:** In furtherance of the Company's long term growth strategy, a number of important acquisitions were made during 2012. These included oil production assets in Peru (offshore Block Z-1) and light oil and gas producing assets in Colombia (PetroMagdalena and C&C). In addition, the Company increased its participation in CGX, acquired significant participation interests in new exploration Blocks in offshore Brazil, and onshore Colombia, Peru and Papua New Guinea, this latter approved on January 24, 2013. These investments are well aligned with the Company's strategy of early stage large resource capture and the objective of being the leading Latin American independent explorer and producer of hydrocarbons.

The Company invested a total amount of \$122 million in Pacific Infrastructure Inc. ("**Pacific Infrastructure**"), increasing our equity interest to approximately 53.4% as of March 2013; this investment will ensure the timely completion of the project, which will allow access to additional storage and export crude oil capacity in Cartagena on the Colombia Caribbean coast, as well as to a new oil pipeline that will link the existing Coveñas crude oil terminal with Cartagena.

- **Continuing drilling activity in the Colombian exploration Blocks with a success rate of 80% in 2012.** During 2012, total net exploration capital expenditure of \$355 million consisted of the following exploration activity: drilling a total of 55 exploratory wells (including 6 exploration, 36 appraisal and 13 stratigraphic wells), the acquisition of 778 km of 2D and 857 km² of 3D seismic surveys; and initiation of exploration activity in Brazil and in the CPE-6 E&P Block. As a consequence of the drilling campaign, the Company announced three new discoveries in 2012: the Cotorra-1X (Guama Block), Chaman-1 (Sabanero Block) and Petirrojo Sur-1 (Cubiro Block), and obtained the approval for the commerciality of the Cajuá field in Quifa Block.
- **New discovery in Brazil.** On January 24, 2013, the Company announced that the Kangaroo-1 well in the Kangaroo prospect, offshore Brazil, found 25 meters (~82 feet) of gross reservoir column in Eocene age sands. Karoon Petroleo & Gas Ltda., a subsidiary of Karoon and the operator for the Block, considers that the reservoir can flow at commercial rates and is thus planning an appraisal well for the near future. The operator is currently drilling the Emu/Cassowary prospect, northeast of the Kangaroo discovery.
- **New discovery on the Guama exploration Block.** On February 20, 2013, the Company announced the discovery of natural gas and condensate in the Manamo-1X exploration well drilled on the Guama Block in the Lower Magdalena basin, onshore Colombia. Manamo-1X was drilled to a total depth of 7,600 feet. The petrophysical evaluation indicates a total of 251 feet of net pay. The well was tested across a 91 foot perforated zone, reaching gas flow rate of 4.9 MMcf/d and 296 bbl/d 54° API condensate through a 16/64" choke.
- **Total capital expenditures.** Capital expenditures excluding acquisitions during the year 2012 totaled \$1,548 million (\$1,096 million in 2011). Of this amount, \$595 million were invested in the expansion and construction of production infrastructure; \$355 million went into exploration activities (including drilling, seismic, other geophysical activities) in Colombia, Peru and Guatemala; \$135 million on surface facilities; \$347 million for development drilling; and \$116 million in other projects, which included the Company's Synchronized Thermal Additional Recovery ("**STAR**") pilot project at Quifa SW.
- **Credit Agency Upgrade.** On October 31, 2012, Fitch Ratings raised its corporate credit rating to "BB+" from "BB". They also raised their rating on the Company's senior unsecured notes to "BB+". Fitch also indicated that the Company's outlook is stable, citing the Company's continued production and reserves diversification, proven track record of increasing production, maintaining adequate reserve replacement ratios, and the lower business risk as a result of the completion of key infrastructure projects.
- **Cash dividend.** A fourth quarter cash dividend in the aggregate amount of approximately \$33 million or \$0.11 per common share was paid on December 20, 2012 to shareholders of record as of December 12, 2012. The Company paid a total of \$130 million or \$0.44 per common share during 2012.
- **Revolving Credit Agreements.** On September 2012, the Company entered into a \$400 million revolving credit facility agreement and guaranty agreement with a syndicate of international lenders with Bank of America, N.A. as administrative agent; and a Colombian peso equivalent revolving credit agreement equivalent to \$300 million, with a syndicate of Colombian lenders and Sociedad Fiduciaria Bogotá, S.A., as administrative agent. In addition, on February 2013, the Company entered into a \$100 million credit facility agreement with Banco ITAÚ BBA S.A. – Nassau Branch. These facilities provide the Company with significant advantages over the replaced former credit line, increasing operating flexibility and improving liquidity, and will be used to finance ongoing working capital needs, capital expenditures and other general corporate purposes of the Company and its subsidiaries.

3. Farm-in Agreements and Business Acquisitions

Acquisitions

During the fourth quarter, the Company entered into and/or completed acquisitions of interests or farm-in agreements including producing and exploratory assets in Colombia, Peru and Guyana. In addition, on January 24, 2013, the Papua New Guinea authorities approved the acquisition of a participating interest announced on April, 2012.

The acquisitions in Colombia had a positive impact for the Company, adding net production volumes of 9,976 boe/d in 2012 as well as 86.1 MMboe of net 2P reserves and prospective resources of 642.4 MMboe (in the year-end 2012 certified reserves and resource evaluations).

Acquisition of C&C Energia Ltd.

On December 31, 2012, Pacific Rubiales acquired all of the issued and outstanding shares of C&C by way of a plan of arrangement (the "**C&C Acquisition**").

With the C&C Acquisition, the Company increased its production portfolio by acquiring three development Blocks (Cravoviejo, Cachicamo, and Llanos-19 Blocks), all located in the Central Southern Llanos Basin in Colombia. These Blocks produce light oil in close proximity to our existing pipeline infrastructure, and which can be used as diluent to mix with the Company's heavy oil production, capturing added components of the value chain.

As part of the C&C Acquisition, Pacific Rubiales retained a 5% equity interest in Platino Energy Corp. ("**Platino**"), which permits the Company to retain upside potential on the exploratory assets Coati, Andaquies and Putumayo-8 Blocks located in the Putumayo Basin in Colombia, and in Morpho Block located in the Middle Magdalena Valley in Colombia (collectively, the "**Spin-Off Properties**").

Pursuant to the terms of the applicable E&P contracts for each of the Spin-Off Properties, C&C provided notification of the Platino reorganization to the Agencia de Hidrocarburos ("**ANH**") on December 27, 2012. The ANH has the right to evaluate the legal, financial and technical capacity of Platino or its subsidiaries to operate the Spin-Off Properties. As a result of such evaluation, the ANH can require additional guarantees from other entities. The parties are awaiting ANH's confirmation of the transaction.

Completion of a 49% participating interest in Block Z-1, Peru with BPZ

During the second quarter of 2012, the Company reached an agreement to acquire a 49% participating interest in the Peru offshore Block Z-1 from BPZ. Under the terms of the agreement, Pacific Rubiales paid \$150 million, and agreed to fund \$185 million of BPZ's share of capital and exploratory expenditures from an effective date of January 1, 2012.

Net oil production during the fourth quarter of 2012 attributed to its 49% interest in Block Z-1 was 1,457 bbl/d from the Corvina and Albacora fields. Certified 100% net 2P reserves at December 31, 2012 on both fields was 88.2 MMbbl (39.9 MMbbl attributed to the Company's 49% interest).

On January 2, 2013 the Company announced that the President of Peru signed the Supreme Decree authorizing the amendment recognizing Company's acquisition of a 49% participating interest in the offshore Block Z-1 in Peru from an effective date of January 1, 2012. The completion date of this transaction was December 12, 2012.

Approval of the Acquisition on a Participating Interest in an Onshore License in Papua New Guinea

On April 30, 2012, the Company entered into an agreement with InterOil Corporation to acquire a 10% net participating interest in the PPL237 Petroleum Prospecting License and the Triceratops structure located within PPL237 in Papua New Guinea for an estimated total investment of \$345 million. The investment is comprised of an upfront payment of \$116 million, funding of an agreed exploration work program and cash payments based on the independently certified resources of the Triceratops structure. The Papua New Guinea authorities approved the transaction on January 24, 2013.

Farm-in Agreement in Peru with Maurel et Prom

On December 4, 2012, Maurel et Prom Peru S.A.C. and the Company executed a farm-in agreement pursuant to which the Company acquired, subject to governmental approval, a 50% working interest and operatorship in the exploration contract for Block 116 located in northeastern Peru. This agreement completed the transaction originally announced by the Company on October 12, 2011.

This Block has an area of 6,600 km² covering most of what is known as the Santiago sub-basin, in the western-most area of the Marañon basin. Geologically, Block 116 is located in the Peruvian Andean Foothills, a structurally complex and minimally explored area that has important hydrocarbon potential in Paleozoic, Cretaceous and Tertiary rocks. The main Peruvian pipeline, the “Oleoducto Norperuano”, passes through the central part of the Block.

Agreement to invest C\$35 million to acquire control of CGX

On February 27, 2013, the Company announced that it has entered into a binding term sheet with CGX, pursuant to which Pacific Rubiales agreed to invest C\$35 million in CGX at a price of C\$0.14 per unit for an aggregate of 250 million units. Each unit will consist of one common share and one common share purchase warrant of CGX, with each warrant being exercisable to acquire one CGX common share at an exercise price of C\$0.20 per share for a period of five years following the date of issuance of the units.

This investment will allow the Company to expand and deepen its position in the highly prospective offshore Guyana oil play. We consider CGX's large acreage position in Guyana to be a premier, world-class exploration asset in an offshore basin with analogous geology to West Africa, Brazil and Venezuela. This investment is well-aligned with the Company's technical strengths, strategy of early stage large resource capture and objective of being the leading Latin American independent explorer and producer of hydrocarbons. Pursuant to the terms of a subscription agreement, Pacific Rubiales will nominate a majority of the board of directors of CGX.

4. Financial and Operating Summary

Financial Summary

A summary of the financial results for the three and twelve months ended December 31, 2012 and 2011 are as follows:

<i>(in thousands of US\$ except per share amounts or as noted)</i>	Year Ended		Three Months Ended	
	December		December	
	2012	2011	2012	2011
Oil and gas sales	\$ 3,884,762	\$ 3,380,819	\$ 1,046,689	\$ 1,011,476
EBITDA ⁽¹⁾	2,018,395	1,959,092	429,041	566,671
EBITDA Margin (EBITDA/Revenues)	52%	58%	41%	56%
Per share - basic (\$) ⁽²⁾	6.85	7.20	1.45	2.02
- diluted (\$)	6.67	6.57	1.41	1.97
Net earnings	527,729	554,336	(23,777)	80,834
Per share - basic (\$) ⁽²⁾	1.79	2.04	(0.08)	0.29
- diluted (\$)	1.74	1.97	(0.08)	0.28
Cash Flow from Operations	1,802,735	1,219,057	676,938	477,530
Per share - basic (\$) ⁽²⁾	6.12	4.48	2.28	1.70
- diluted (\$)	5.95	4.09	2.23	1.66
Adjusted Net earnings from operations	652,857	742,288	38,169	167,091
Per share - basic (\$) ⁽²⁾	2.22	2.73	0.13	0.60
- diluted (\$)	2.16	2.49	0.13	0.58
Non-operating items	125,128	187,952	61,946	86,257
Funds Flow from Operations ⁽¹⁾	1,387,544	1,368,599	231,532	351,760
Per share - basic (\$) ⁽²⁾	4.71	5.03	0.78	1.26
- diluted (\$)	4.58	4.59	0.76	1.22

(1) See “Additional Financial Measures” on page 34.

(2) The basic weighted average number of common shares outstanding for the year ended December 31, 2012 and 2011 was 294,576,424 (fully diluted – 302,823,229) and 271,985,534 (fully diluted – 298,271,197), respectively.

Adjusted earnings from operations is a non-IFRS financial measure that represents net earnings adjusted for certain items of a non-operational nature, including non-cash items. The Company evaluates its performance based on adjusted net earnings from operations. The reconciliation "Adjusted Net Earnings from Operations" lists the effects of certain non-operational items that are included in the Company's financial results and may not be comparable to similar measures presented by other companies.

Net earnings for the year 2012 totaled \$527.7 million and include a number of non-operating and non-cash items totaling \$125 million, mainly related to mark-to-market gain/losses on derivatives, loss from equity investments, foreign exchange gain/losses, share-based compensation and equity tax. These items may or may not materialize or reoccur in future periods. Also included in net earnings were one-off expenses of \$15 million related to the acquisitions of PetroMagdalena and C&C.

Consolidated loss for the fourth quarter of 2012 was \$24 million, compared to a net earnings of \$80.8 million during the same period of 2011. Results for the fourth quarter of 2012 were impacted by impairment of exploratory assets and equity investments of \$121 million, required by IFRS accounting rules and provision for overlift of \$92 million related with the high-price clause on the production of Quifa SW field. Adjusted net earnings from operations before non-cash items for the fourth quarter of 2012 were \$38 million compared to \$167.1 million in the year 2011. The reconciliation of adjusted net earnings from operations to net earnings is as follows:

<i>(in thousands of US\$)</i>	Year Ended December		Three Months Ended December	
	2012	2011	2012	2011
Adjusted earning from operations ⁽¹⁾	\$ 652,857	\$ 742,288	\$ 38,169	\$ 167,091
Non-operating items				
(Loss) gain on risk management contracts	10,130	8,831	(13,663)	(46,458)
Share-based compensation	(32,902)	(48,783)	(853)	(316)
Equity tax	-	(68,446)	-	-
Gain (loss) from foreign exchange	577	(39,894)	13,421	1,947
Incentive for early conversion of debentures	-	(46,489)	-	(46,489)
(Loss) gain from equity investments	(102,933)	6,829	(60,851)	5,059
Total non-operating items	(125,128)	(187,952)	(61,946)	(86,257)
Net earnings as reported	527,729	554,336	(23,777)	80,834

(1) See "Additional Financial Measures" on page 34.

Operating Summary

The Company produces and sells crude oil and natural gas. It also purchases crude oil from third parties to be used as diluents and for trading purposes. The combined crude oil and gas operating netback during the year 2012 was \$60.20/boe, higher as compared to 2011 (\$60.19/boe). Crude oil operating netback during the year 2012 was \$63.14/bbl, 1% lower in comparison to 2011 (\$63.70/bbl) and crude oil trading operating netback was \$3.38/bbl, 6% lower in comparison to 2011 (\$3.58/bbl). Natural gas operating netback was \$35.01/boe, 13% higher in comparison to 2011 (\$31.09/boe).

The combined crude oil and gas operating netback during the fourth quarter 2012 was \$46.44/boe, or 34% lower than the same period of 2011 (\$69.62/boe). The main reasons for the lower operating netback were:

- A 6% reduction in the combined realized oil and gas price from \$100.52/boe in fourth quarter 2011 to \$94.61/boe in the fourth quarter of 2012, in line with the WTI international price trend.
- Increase in the overlift cost by \$8.87/bbl due to the booking of a provision of \$92 million to settle the additional volume to Ecopetrol S.A. ("Ecopetrol") under the high-prices clause (the "PAP") in Quifa SW field, as indicated under the heading entitled "Royalties".
- Increase in operating costs of \$3.89/bbl during the fourth quarter of 2012 mainly due to increased water disposal at the Rubiales, Quifa and Cajua fields.
- Additional workover and maintenance activities in fourth quarter 2012 of \$1.79/bbl.
- Increased land transportation cost at Cajua field of \$1.52/bbl as the fluid is currently transported by tank truck to the water treatment facilities. Nevertheless, loading facilities were constructed by the end of the year, which has already lowered this cost. In addition, flow lines are planned to be constructed as soon as the license is obtained, which will further reduce the transportation costs for the Cajua field.
- The reduction in the fourth quarter netback was offset by a significant volume of production and sales as indicated under the heading entitled "Discussion of 2012 Financial Results - Revenues".

Set out below is the operating netback for crude oil, gas and trading volumes the three and twelve months ended December 31, 2012:

Full year 2012

	Year ended December			2011 Combined
	2012 Oil	2012 Gas	2012 Combined	
Average daily volume sold (boe/day)⁽¹⁾	93,141	10,902	104,043	96,997
Operating netback (\$/boe)				
Crude oil and natural gas sales price	102.94	42.19	96.58	91.58
Production cost of barrels sold ⁽²⁾	11.71	4.60	10.96	5.48
Transportation (trucking and pipeline) ⁽³⁾	13.95	0.20	12.51	10.93
Diluent cost ⁽⁴⁾	11.08	-	9.92	14.23
Other costs ⁽⁵⁾	1.12	2.65	1.28	0.57
Total production cost	37.86	7.45	34.67	31.21
Overlift/Underlift ⁽⁶⁾	1.94	(0.27)	1.71	0.18
Operating netback crude oil and gas (\$/boe)	63.14	35.01	60.20	60.19

Netback Crude Oil Trading	Year ended December	
	2012	2011
Average daily volume sold (boe/day)	4,937	3,449
Operating netback (\$/boe)		
Crude oil traded	114.62	110.10
Cost of purchases of crude oil traded	111.24	106.52
Operating netback crude oil trading (\$/boe)	3.38	3.58

Fourth Quarter 2012

	Three months ended December			2011 Combined
	2012 Oil	2012 Gas	2012 Combined	
Average daily volume sold (boe/day)⁽¹⁾	107,392	11,031	118,423	99,139
Operating netback (\$/boe)				
Crude oil and natural gas sales price	99.83	43.80	94.61	100.52
Production cost of barrels sold ⁽²⁾	14.78	6.61	14.02	5.73
Transportation (trucking and pipeline) ⁽³⁾	14.57	0.01	13.22	10.59
Diluent cost ⁽⁴⁾	8.52	-	7.72	13.74
Other costs ⁽⁵⁾	5.14	2.99	4.94	1.54
Total production cost	43.01	9.61	39.90	31.60
Overlift/Underlift ⁽⁶⁾	9.21	(0.89)	8.27	(0.70)
Operating netback crude oil and gas (\$/boe)	47.61	35.08	46.44	69.62

Crude oil trading	Three months ended December	
	2012	2011
Average daily volume sold (boe/day)	1,718	9,067
Operating netback (\$/boe)		
Crude oil traded	100.66	113.51
Cost of purchases of crude oil traded	96.99	109.79
Operating netback crude oil trading (\$/boe)	3.67	3.72

(1) Combined operating netback data based on weighted average daily volume sold which includes diluents necessary for the upgrading of the Rubiales blend.

(2) Cost of production mainly includes lifting cost and other direct production cost such as fuel consumption, outsourced energy, fluid transport (oil and water), personnel expenses and workovers, among others. Increases in the oil production cost are driven by higher fluid (mainly water) production which affects fuel consumption, outsourced energy and fluid transport costs; as compared to prior period of 2011.

- (3) Includes the transport costs of crude oil and gas through pipelines and tank trucks incurred by the Company to take the products to the delivery points to customers.
- (4) During 2012 oil diluent cost decreased 30% (\$4.31/bbl), due to the use of lower volume of diluents (4,447 bbl/d, around 33%) with higher blending ratios, mainly natural gasoline (81.9° API), while we increased our oil sales 3.5% (3,128 bbl/d), even though 2012 diluent prices, storage and trucking fees were higher than 2011 by \$14.32/bbl (\$117.45/bbl vs. \$103.13/bbl). Adjusted Net blending cost of Rubiales crude increased to \$3.65 bbl in the year 2012 from \$3.14/bbl in 2011 (16%). This increase was mainly due to higher net diluent costs (\$25.10/bbl vs. \$13.66/bbl) because higher diluent prices, storage and pipeline fees, compensated by an improved blending average ratio of 14.55%, as indicated in the below table:

Adjusted Net Cost of Diluent	Year Ended		Three Months Ended	
	December		December	
	2012 (US\$/bbl)	2011 (US\$/bbl)	2012 (US\$/bbl)	2011 (US\$/bbl)
Average diluent purchase price	117.45	103.13	113.44	106.95
Pipeline fees	11.25	7.76	11.25	7.76
Average Rubiales blend sales price	(103.60)	(97.23)	(100.54)	(106.69)
Net diluent cost per barrel	25.10	13.66	24.15	8.02
Average blending ratio	14.55%	23.00%	14.67%	22.50%
Net Blend cost per barrel	3.65	3.14	3.54	1.80

For the purpose of securing diluents for blending Rubiales crude oil, the Company purchased 8,436 bbl/d during the year 2012 vs. 10,647 bbl/d in the same period of 2011. In 2012 the Company increased purchases of natural gasoline (81.9° API) to 7,444 bbl/d vs. 2,938 bbl/d in 2011 and continued local purchases (992 bbl/d in 2012 vs. 7,709 bbl/d in 2011) of light crude oils (40° API average).

- (5) Other costs mainly correspond to royalties on gas production, external road maintenance at the Rubiales field, inventory fluctuation, storage cost and the net effect of the currency hedges of operating expenses incurred in Colombian pesos during the period. The increase in other cost during the fourth quarter 2012, were driven by inventory fluctuation cost (\$4/bbl) due to increased sales during this period. This increase is offset with the prior quarter inventory fluctuation.
- (6) Corresponds to the net effect of the overlift position for the period amounting to \$65.0 million, which generated an increase in the combined costs to \$1.71/boe as explained in "Discussion of 2012 Financial Results– Financial Position – Operating Costs" on page 22.

Reconciliation of volumes produced vs. volumes sold

The following is a reconciliation of volumes produced or purchased in Colombia vs. volumes sold during the year and three months ended December 31, 2012; including a breakdown of crude oil production and diluent and crude oil trading purchases:

Full year 2012

Production and sales volumes (boe/day) ⁽¹⁾	Year ended December			
	Oil	Gas	Combined	2011 Combined
Average total field production	234,826	11,749	246,575	218,450
Share before royalties	107,700	10,963	118,663	102,190
Average net production (after royalties and field consumption) Colombia	85,123	10,961	96,084	86,497
Average net production (after royalties) Peru ⁽³⁾	1,573	-	1,573	-
Beginning inventory (ending inventory December 31)	6,664	-	6,664	3,299
Average net production Colombia (after royalties and field consumption)	85,123	10,961	96,084	86,497
Average net production Peru since acquisition date ⁽³⁾	95	-	95	-
New acquisition (beginning inventory in the closing date of transaction) ⁽²⁾	102	-	102	-
Purchases of diluents and oil for trading ⁽¹⁾	12,863	-	12,863	19,480
Other inventory movements ⁽¹⁾	(2,433)	(59)	(2,492)	(2,148)
Ending inventory December 31.	(4,336)	-	(4,336)	(6,682)
Average daily volume sold (boe/day)	98,078	10,902	108,980	100,446
Breakdown average daily volume sold (boe/day)				
Oil and Gas sold	93,141	10,902	104,043	96,997
Crude Oil Trading Sold	4,937	-	4,937	3,449
Total average daily volume sold	98,078	10,902	108,980	100,446

Fourth Quarter 2012

Production and sales volumes (boe/day) ⁽¹⁾	Three months ended December			2011 Combined
	Oil	Gas	Combined	
Average total field production	259,295	12,047	271,342	236,048
Share before royalties	120,247	11,166	131,413	107,760
Average net production (after royalties and field consumption) Colombia	95,526	11,166	106,692	90,959
Average net production (after royalties) Peru ⁽³⁾	1,457	-	1,457	-
Beginning inventory (ending inventory September 30)	23,419	-	23,419	28,847
Average net production Colombia (after royalties and field consumption)	95,526	11,166	106,692	90,959
Average net production Peru since acquisition date ⁽³⁾	379	-	379	-
New acquisition (beginning inventory in the closing date of transaction) ⁽²⁾	103	-	103	-
Purchases of diluents and oil for trading ⁽¹⁾	10,317	-	10,317	19,192
Other inventory movements ⁽¹⁾	(3,383)	(135)	(3,518)	(4,280)
Ending inventory December 31.	(17,251)	-	(17,251)	(26,512)
Average daily volume sold (boe/day)	109,110	11,031	120,141	108,206
Breakdown average daily volume sold (boe/day)				
Oil and Gas sold	107,392	11,031	118,423	99,139
Crude Oil Trading Sold	1,718	-	1,718	9,067
Total average daily volume sold	109,110	11,031	120,141	108,206

The following table provides a breakdown of sales volumes by crude oil produced, diluents and crude oil trading in Colombia during the year and three months ended December 31, 2012:

Production and sales volumes (boe/day) ⁽¹⁾	Year ended December 2012		
	Oil Production	Diluent and Trading	Total
Beginning inventory (ending inventory December 31)	3,431	3,233	6,664
Average net production Colombia (after royalties and field consumption)	85,123	-	85,123
Average net production Peru since acquisition date ⁽³⁾	95	-	95
New acquisition (beginning inventory in the closing date of transaction) ⁽²⁾	102	-	102
Purchases of diluents and oil for trading ⁽¹⁾	-	12,863	12,863
Other inventory movements ⁽¹⁾	(2,291)	(142)	(2,433)
Ending inventory December 31.	(2,928)	(1,408)	(4,336)
Average daily volume sold (boe/day)	83,532	14,546	98,078

Production and sales volumes (boe/day) ⁽¹⁾	Three months ended December 2012		
	Oil Production	Diluent and Trading	Total
Beginning inventory (ending inventory September 30)	16,949	6,470	23,419
Average net production Colombia (after royalties and field consumption)	95,526	-	95,526
Average net production Peru since acquisition date ⁽³⁾	379	-	379
New acquisition (beginning inventory in the closing date of transaction) ⁽²⁾	103	-	103
Purchases of diluents and oil for trading ⁽¹⁾	-	10,317	10,317
Other inventory movements ⁽¹⁾	(3,588)	205	(3,383)
Ending inventory December 31.	(11,648)	(5,603)	(17,251)
Average daily volume sold (boe/day)	97,721	11,389	109,110

(1) See additional detail in "Inventory Movements" on page 15.

(2) During 2012, the Company acquired producing assets from C&C, Block Z-1 and PetroMagdalena.

(3) Net income associated to the volume of production and sales from January 1, 2012 through the completion date of the BPZ acquisition on December 12, 2012 was accounted as lower amount of the future carry investment in Peru. Production and sales of 34,868 bbl from December 13, through December 31, 2012 were reflected in the Company's results, as the Company had legal entitlement of the 49% over the assets, reserves and production.

Royalties and Volume Allocation

Royalties

The current royalty rates for volumes of hydrocarbons produced from the Company's Colombian assets range from 5% to 20%, and 5% for Peru. Royalties on production represent the entitlement of the respective states to a portion of the Company's share of production and are recorded using rates in effect under the terms of contract and applicable laws at the time of hydrocarbon discovery. In Colombia, royalties for oil may be payable in kind while for gas they are payable in cash. In Peru, royalties calculations for oil resulted in a 5.3% levy on total gross revenues and the government allows the companies to pay either in kind or cash; however the current practice is to pay the royalties in cash.

Additional Production Share in the Quifa SW

The Company's share of production before royalties in the Quifa SW field is 60%; however, this participation may decrease from time to time when the high-prices clause, stipulated in the Quifa Association Contract, is triggered.

On September 27, 2011, Ecopetrol and the Company agreed on an arbitration process to settle differences in the interpretation of this PAP clause in the Quifa Association Contract and its effect on the production division. On April 12, 2012, the Company initiated the arbitration process before the Bogotá Chamber of Commerce. In addition, both parties agreed to apply the formula that the ANH uses in its contracts to assign the presumptive additional share to Ecopetrol, as from the activation of the additional production clause in April 2011, until the arbitration is concluded. At the end of 2012, the volumes corresponding to Ecopetrol as per the ANH formula from April 1, 2011 to December 31, 2012 have been completely delivered to Ecopetrol via reduced net production share.

On March 13, 2013, the arbitration panel delivered its decision interpreting that the PAP clause should be calculated on 100% of the production of the Quifa SW field, instead of simply the Company's 60%. However, the arbitration panel expressly denied Ecopetrol's demand for an order for Pacific Rubiales to deliver the associated volumes of hydrocarbons as a result of its interpretation of the PAP clause. The arbitration decision is not yet firm nor does it provide enforceable remedies against the Company. The Company is evaluating the decision as it leaves open several unresolved issues and also evaluating all of its alternative remedies under Colombian laws and applicable international treaties.

In the event that the interpretation of the PAP clause by the arbitration panel becomes enforceable, the Company would be required to deliver an additional 1,393,252 bbl of oil to Ecopetrol, representing Ecopetrol's additional share in Quifa SW production from April 3, 2011 to December 31, 2012, which in any case would be delivered in kind from future production out of 10% of its daily net share of production of the Quifa SW field (as of today, approximately 2,270 bbl/d over a 20 month period). This additional volume has been recorded as an over-lift on the consolidated financial statements as at December 31, 2012.

As a result of the above and under prudent accounting practice, a provision has been made in the Company's 2012 year-end financials to account for cumulative amounts accrued as follows:

- \$92 million negative impact on 2012 EBITDA, from \$2,110 million to \$2,018 million, representing approximately a 4% reduction.
- \$61 million negative impact on 2012 Net Income, from \$589 million to \$528 million, which is around a 10% reduction.

The Company is evaluating all available courses of action and will vigorously defend its rights under the Quifa Association contract.

5. Operating Results

Update on Environmental Permits

Colombia

During 2012, the Company submitted for evaluation to the Environmental Authority in Colombia ("ANLA") nineteen licensing processes, all of them are in full compliance with the regulations and processes governing environmental licenses in Colombia.

As of December 31, 2012, the following six licenses were granted: (i) exploration license for CPO-12 and Guasimo Blocks; (ii) license to expand the water injection capacity in the Rubiales field by 400 Mbbl/d; (iii) La Creciente field

obtained the permits to install more facilities for treatment; (iv) license for the gas pipeline San Pedro – Bremen, a pipeline 32 km long with 24” diameter to transport gas produced in La Creciente field; and (v) Petroeléctrica de los Llanos (“**PEL**”) received the license for the electrical interconnection line from the Chivor central plant to the Rubiales field.

Thirteen environmental licenses are in progress for 2013, the most important of which are: (i) additional water injection for the Rubiales field; (ii) blanket exploration and development license for the CPE-6 Block; and (iii) license to increase the oil production in the Copa field. The Company expects to receive these licenses during the first half of 2013.

Peru

During 2012, the Peruvian government approved the environmental permits for two exploratory wells in Block 116 and one exploratory well in Block 138. In addition, the Company received the environmental permit for the activities of the CX15 platform in the Block Z-1 and the approval for 789 km 2D seismic survey for Block 135.

Exploration

During the fourth quarter of 2012, the Company focused its exploration activity in the eastern Llanos and Lower Magdalena basins in Colombia, and in the Santos basin, offshore Brazil. Six exploration wells were drilled during the period: one exploration well each in the Sabanero and, SSJN-9 Blocks and two wells in each the CPO-12 and Cubiro Blocks. Also, during December 2012, the Company started drilling four exploration wells: one each on the CPO-1, CPO-12 and Guama Blocks in Colombia and one on the exploration Blocks offshore in the Santos Basin, Brazil: S-M-1101, S-M-1102, S-M-1037 and S-M-1165 (the “**Karooon Blocks**”). All these wells reached final depth during January 2013. The Company also finished 385 km of 2D seismic and 176 km² of 3D seismic surveys. The following is a summary of the exploration campaign during the fourth quarter 2012.

Colombia

In the Sabanero Block, Maurel and Prom Colombia B.V. (“**Maurel et Prom**”), the operator of the contract, drilled the Chaman-1 exploration well, located in northeastern part of the Block, approximately 10 km north of the producing Sabanero oil field. The well showed 16 feet of net pay in the C-7 Unit and resulted in a new oil discovery. The well is currently under extended production test, producing an average of 113 bbl/d of 13.4° API oil. Also, during the period, Maurel et Prom finished the acquisition and processing of 247 km of 2D seismic in the northern part of the Block.

In the CPO-12 Block, two exploration wells were drilled as part of the exploration commitments with the ANH: The Espiguero-1X well was drilled in the southeastern border of the Block, and encountered only two feet of net pay, so the well was plugged and abandoned. The Escarabajo-1X well was drilled in the northwestern border of the Block. The well showed hydrocarbon traces in the interval of interest but the petro-physical evaluation did not show any net pay, and the well was plugged and abandoned.

In the CPE-6 Block, the Company continued with the acquisition of 366 km² of 3D seismic survey in the northern part of the Block. The survey results are expected to be ready by June 2013.

In the Cubiro Block, the Company drilled and logged the Petirrojo Sur 1 exploration well and the Petirrojo Sur 2 appraisal well. Both wells were completed in the Carbonera C7 sand, where 13 feet of net pay were found with no indication of an oil-water contact. These wells are currently under extended production tests, producing an average of 120 and 580 bbl/day of 38 °API oil respectively.

In the Muisca Block, Maurel et Prom, operator of the Block, continued with the acquisition of 250 km² of 3D seismic survey.

In the COR-15 Block, operated by Maurel et Prom, the Company continued the interpretation of 176 km² of 3D seismic survey. In the COR-15 and COR-24 Blocks it has, started an aeromagnetic and aerogravity survey. The results of these surveys are expected by the first quarter of 2013.

In the SSJN-9 Block, located in the Lower Magdalena Valley basin, Maurel et Prom, the operator of the Block, drilled the Santa Fe-1 exploration well. The main exploration target Ciénaga de Oro Inferior was reached at 7350’ MD (7110’ TVDSS). The petro-physical evaluation of well logs showed no net pay, and the well was plugged and abandoned.

In the Portofino Block, Canacol Energy Ltd. the operator of the Block, finished the acquisition of 78 km of 2D seismic data in the northern and southern regions of the Block and 45 km² of 3D seismic in the southern region of the Block, which will be used to locate planned wells.

In the CPE-1 Block, the Company started the acquisition of 438 km 2D seismic program to comply with the exploration commitments for the Block. By December 31, 2012, the Company had acquired 138 km of 2D seismic.

During December 2012, the Company started drilling three additional exploration wells: the Hayuelo-1X well in the CPO-12 Block, the Altillo Oeste-1 in the CPO-1 Block and the Manamo-1X well in the Guama Block. The first two were plugged and abandoned during the first quarter 2013. In the Manamo-1X exploration well a preliminary petro-physical evaluation shows a total of 251 feet of net pay averaging 18% porosity in the Porquero formation and a short production test resulted in 4.9 MMcf/d of natural gas and 296 bbl/d of 54° API condensate through a 16/64" choke, across a 91 foot perforated zone.

Guatemala

In the Guatemala Blocks (N-10-96 and O-10-96), the Company, through the operator (Compañía Petrolera del Atlántico S.A. ("CPA")), completed 324 km of 2D seismic survey, continued the acquisition of 275 km² of a hyperspectral survey (85%) and also started the design and contracting for an exploration well, which is expected to be drilled during the second quarter of 2013.

Peru

On Block 138, the Company received the approval of the Environmental Management Plan required to drill the Yahuish 1X exploratory well. Civil works for the logistic base were ready by the end of December and drilling will begin in March 2013.

On Block 135, the Company started the acquisition of a 789 km 2D seismic survey in December 2012. The seismic interpretation is planned to commence in June 2013.

On Block Z-1, the Company is processing and interpreting approximately 1,142 km² of 3D seismic data acquired recently by BPZ (the operator). An additional 462 km² of 3D seismic data is expected to be completed during the first quarter 2013.

Brazil

Within the S-M-1101 and S-M-1165 offshore Block in Brazil, Karoon, the operator of the Block, started drilling the Kangaroo 1 well, the first exploration well drilled by the Company in the Santos Basin. The Kangaroo well had multiple targets in the late Cretaceous, Eocene and Miocene rocks, and its drilling operations were completed in February 2013.

The Kangaroo 1 well satisfied the minimum work commitments for the Karoon Blocks. The well was drilled to a total depth of 3,049 m (10,000 ft.), encountering a gross reservoir section of 25 m (82 ft.) in Eocene rocks. A complete set of wire line logs and rock and fluid samples was collected for reservoir analysis.

The drilling results for the year and three months ended December 31, 2012, are as follows:

	Year Ended December		Three Months Ended December	
	2012	2011	2012	2011
Successful exploratory wells	3	9	2	3
Successful appraisal wells ⁽¹⁾	34	36	1	6
Successful stratigraphic wells	7	13	-	8
Dry wells	11	11	3	2
Total	55	69	6	19
Success rate	80%	84%	50%	89%

(1) Includes horizontal appraisal wells.

Detail of Exploratory/Appraisal Wells Drilled During the Fourth Quarter of 2012

No. of wells	Block	Area / Field / Prospect	Well Name	Type	Total Depth TVDS (feet)	Net Pay (feet) ⁽²⁾
1	Sabanero ⁽¹⁾	Chaman	Chaman-1	Exploratory	2,948	16
2	Cubiro	Petirrojo	Petirrojo-1	Exploratory	5,840	13
3	Cubiro	Petirrojo	Petirrojo-2	Appraisal	5,278	13
4	CPO-12	Espiguero	Espiguero-1X	Exploratory	2,744	2
5	CPO-12	Escarabajo	Escarabajo-1X	Exploratory	3,912	-
6	SSJN-9	Santa Fe	Santa Fe-1	Exploratory	8,030	-

(1) The Company holds a 49.999% participation in Maurel and Prom Colombia B.V., which indirectly owns a 49.999% working interest in the Sabanero Block.

(2) "Net Pay" represents the total estimated net pay encountered in the horizontal (HZ) or vertical drilled sections.

Production

Average Daily Oil and Gas Production– Net Volumes Before and After Royalties

Colombia

Average net production after royalties for 2012 reached 96,084 boe/d (243,264 boe/d total field production) representing approximately 11% growth year-over-year mainly due to:

- Drilling of 174 producing wells at the Rubiales field, 56 producing wells at the Quifa SW field and 16 wells at the Cajúa field during the same period, as well as an increase in the capacity of production facilities at Rubiales and Quifa. Net production at Rubiales and Quifa increased 10% while the La Creciente natural gas field increased by 1% as compared to 2011.
- License modification for the water disposal in Rubiales field, allowing for the injection of an additional 400 thousand barrels of water per day. The Company has submitted a license modification for an additional 1 million barrels of water per day, which is expected to be granted by the first half of 2013.
- Average net production after royalties contributed by the PetroMagdalena acquisition during 2012 totaled 1,847 boe/d (total field production of 3,563 boe/d), representing 2% of the total net production after royalties reported by the Company during the year. At the completion date of the acquisition, the net production of PetroMagdalena was 3,700 boe/d (total field production of 6,432 boe/d) and at December 31, 2012 the net production was 6,613 boe/d (total field production of 10,923 boe/d), representing an increase of 79%.

During the fourth quarter of 2012, net production after royalties and field consumption averaged 106,692 boe/d (total gross field 268,369 boe/d); this volume is 15,733 boe/d (total gross field 32,321 boe/d) higher (17%) as compared to the same period of 2011.

During 2012, average net production after royalties of C&C totaled 9,976 bbl/d (total field production of 10,855 bbl/d). This volume was not included in the average net production reported by the Company during the year 2012 as the completion date of the C&C Acquisition was December 31, 2012. Production volumes will be reported from the first quarter of 2013 onwards.

Peru

The production shown in the following table corresponds to the 49% deemed participating share of production attributable to the Company from Block Z-1 for the period pursuant to a Stock Purchase Agreement (“SPA”) signed on April 27, 2012 between the Company and BPZ. Under the terms of the SPA: (i) at closing, operating revenues and expenses will be allocated to each partner’s respective participating interest; and (ii) once approvals by the relevant Peruvian authorities are granted, the Company shall receive a 49% interest in the production of hydrocarbons from the Block Z-1 effective as of January 1, 2012. Revenues and costs have been recognized in the Company’s financial results with respect to the production from Block Z-1 since December 12, 2012 as its full entitlement from that date as a result of the approval of the applicable Peruvian authorities.

Net production for the fourth quarter of 2012 attributed from Block Z-1 averaged 1,457 bbl/d (total gross field 2,973 bbl/d). Production is expected to increase during the first semester of 2013 through the development drilling program from the new platform CX15 in the Corvina field which will start during the first quarter of 2013.

The following table sets out the average production for the three and twelve months ended December 31, 2012 at all of the Company’s producing fields located in Colombia and Peru:

Full year 2012

	Average Year Production (in boe/d)					
	Total field production		Share before royalties ⁽¹⁾		Net share after royalties	
	2012	2011	2012	2011	2012	2011
Producing Fields - Colombia						
Rubiales / Piriri	177,015	165,446	74,113	68,503	59,285	54,802
Quifa ⁽²⁾	46,701	36,496	27,851	20,928	22,070	19,181
La Creciente ⁽³⁾	10,864	10,801	10,662	10,586	10,660	10,584
Cubiro	2,196	-	1,408	-	1,295	-
Abanico	1,584	2,183	454	643	436	617
Sabanero ⁽⁴⁾	1,244	-	613	-	576	-
Dindal / Rio Seco	1,130	1,220	672	725	553	609
Cajua	926	-	556	-	522	-
Arrendajo	901	-	478	-	440	-
Rio Ceibas	-	1,754	-	475	-	380
Other producing fields ⁽⁵⁾	703	550	260	330	247	324
Total Production - Colombia	243,264	218,450	117,067	102,190	96,084	86,497
Producing Fields - Peru (See note below)						
Block Z-1 ⁽⁶⁾	3,311	-	1,596	-	1,573	-
Total Production - Peru	3,311	-	1,596	-	1,573	-
Total Production Colombia and Peru	246,575	218,450	118,663	102,190	97,657	86,497

Fourth Quarter 2012

	Average Q4 Production (in boe/d)					
	Total field production		Share before royalties ⁽¹⁾		Net share after royalties	
	Q4 2012	Q4 2011	Q4 2012	Q4 2011	Q4 2012	Q4 2011
Producing Fields - Colombia						
Rubiales / Piriri	192,395	178,826	80,975	74,015	64,756	59,212
Quifa ⁽²⁾	49,271	40,995	29,373	21,119	23,040	19,313
La Creciente ⁽³⁾	11,072	10,898	10,833	10,623	10,831	10,621
Cubiro	5,877	-	3,783	-	3,480	-
Cajua	2,875	-	1,725	-	1,622	-
Arrendajo	1,583	-	1,069	-	983	-
Abanico	1,479	1,908	408	561	390	539
Dindal / Rio Seco	1,379	1,198	803	696	655	600
Sabanero ⁽⁴⁾	1,247	76	615	36	578	68
Rio Ceibas	-	1,733	-	472	-	378
Other producing fields ⁽⁵⁾	1,191	414	372	238	357	228
Total Production - Colombia	268,369	236,048	129,956	107,760	106,692	90,959
Producing Fields - Peru (See note below)						
Block Z-1 ⁽⁶⁾	2,973	-	1,457	-	1,457	-
Total Production - Peru	2,973	-	1,457	-	1,457	-
Total Production Colombia and Peru	271,342	236,048	131,413	107,760	108,149	90,959

(1) Share before royalties is net of internal consumption at the field and before PAP at the Quifa SW field.

(2) Includes Quifa SW field and early production from Quifa North prospects. The Company's share before royalties in the Quifa SW field is 60% and decreases according to a high-prices clause that assigns additional production to Ecopetrol.

(3) Royalties on the gas production from La Creciente field are payable in cash and accounted as part of the production cost. Royalties on the condensates are paid in kind, representing a small impact in the net share after royalties. The Company has completed 80% of the project to increase the process capacity to 100 MMcf/d at La Creciente Station.

(4) The Company holds a 49.999% participation in Maurel and Prom Colombia B.V., which indirectly owns a 49.999% working interest in the Sabanero Block.

(5) Other producing fields corresponds to producing assets located in Cerrito, Moriche, Las Quinchas, Guasimo and Bugarvilles Blocks. Also includes the acquired Blocks from PetroMagdalena such as Carbonera, Carbonera La Silla and Yamu Blocks (Yamu is not an operated Block). Subject to Ecopetrol's and ANH's approval, the Company has divested its participation in the Moriche, Las Quinchas, Guasimo, and Chipalo Blocks.

(6) Block Z-1 includes the Corvina and Albacora fields which are operated by BPZ in which the Company acquired a 49% undivided participating interest on April 27, 2012. The transaction was completed upon receiving governmental approval on December 12, 2012; the Company or any of its subsidiaries will be the technical operations manager under an Operating Services Agreement. The applicable royalties in Peru are paid in cash and are accounted as part of the production cost.

Supply and Sales Balance

The following is the Company's reconciliation of inventory volumes (boe produced vs. boe sold) for the year and three months ended December 31, 2012:

<u>Inventory Movements</u>	<u>Year Ended</u>		<u>Three Months Ended</u>	
	<u>December</u>		<u>December</u>	
	<u>Total boe</u>	<u>Aver. day</u>	<u>Total boe</u>	<u>Aver. day</u>
	<u>Net</u>	<u>Net</u>	<u>Net</u>	<u>Net</u>
Beginning inventory	2,439,084		2,154,535	
Transactions during the period				
Net oil and gas production	35,166,807	96,084	9,815,622	106,692
Net oil and gas production Peru	34,879	95	34,879	379
Settlement of overlift position ⁽¹⁾	(286)	(3)	(77,179)	(839)
New acquisition (beginning inventory in the closing date of transaction) ⁽²⁾	37,481	102	9,484	103
Purchases of diluents	3,087,617	8,436	778,165	8,459
Purchases of oil for trading	1,620,294	4,427	170,970	1,858
Total sales production assets ⁽³⁾	(39,887,306)	(108,980)	(11,052,878)	(120,141)
Total sales exploration assets ⁽⁴⁾	(329,030)	(899)	(279,566)	(3,039)
Overlift position ⁽⁵⁾	104,739	287	104,739	1,138
Settlement PAP	(548,675)	(1,499)	(124,511)	(1,353)
Volumetric compensation and operational (losses) gains	(138,514)	(378)	52,830	575
Ending inventory ⁽⁶⁾	1,587,090		1,587,090	

(1) This volume corresponds to the settlement of the overlift position for crude oil as of December 31, 2011 and September 30, 2012, respectively, which resulted in a lower volume of sales during the period it was settled.

(2) During the fourth quarter of 2012, the Company acquired C&C and the production from Block Z-1 was recognized and adjusted as of the effective date, upon completion date of the transaction, which was December 12, 2012. In addition, during the third quarter of 2012 the Company completed the acquisition of PetroMagdalena.

(3) Includes the sales of crude oil and gas from producing fields plus diluents.

(4) Includes sales of crude oil produced from successful exploratory wells under extended testing. The sale of the extended testing volume is booked as a lower amount of the investment according to IFRS accounting rules.

(5) This volume corresponds to a net overlift position of 104,739 boe of crude oil and gas as of December 31, 2012, which will be settled during future periods.

(6) Corresponds to crude oil inventory in tanks as of the end of December 31, 2012 at the fields, pipelines and Coveñas Terminal.

Commercial Activity

Year 2012 Market Overview

In 2012, the world experienced a year of economic deceleration to 3.0% from 3.6% GDP growth in 2011. Crude oil prices continued to suffer from volatility with opposite forces dominating at different times. As a consequence Latin American and USGC crude prices increased their values vs. WTI in 2012. For example, Maya crude oil, which is used as a heavy crude reference, was traded at an average of WTI + \$5.5/bbl vs. WTI + \$3.5/bbl in 2011 (+\$2/bbl).

The geopolitical tensions in the Middle East and the supply disruptions in the North Sea and countries in West and East Africa, affected crude oil production levels. These events, amplified by market speculation, drove prices up. On the other hand, concerns about global economic developments, especially in the Euro-zone, the U.S. "fiscal cliff" worries and Chinese economic deceleration of 7.6% vs. 9.4% GDP growth in 2011, generated crude oil demand worries. These issues had the effect of driving prices down. As a result of all of the above events, WTI Nymex prices declined to \$94.15/bbl in 2012 from \$95.11/bbl in 2011 (- \$0.96/bbl). Meanwhile, Brent prices increased to \$111.68/bbl in 2012 vs. \$110.91/bbl in 2011 (+ \$0.77/bbl).

According to the U.S. Energy Information Administration (the "EIA"), in 2012 there was an incremental rise in world crude oil supply of +1.9 MMbbl/d to 89.0 MMbbl/d. EIA projects the total non-OPEC supply of crude oil grew by 0.5 MMbbl/d to an average 52.5 MMbbl/d in 2012. Although supply growth in the United States and Russia during 2012 outpaced their forecasts at the beginning of the year, overall non-OPEC liquid fuels production fell below the year-ago expectations due to unplanned outages in non-OPEC countries. Syria and the Sudan are currently the most significant sources of disruption to non-OPEC production and this situation is expected to continue in 2013. On the other hand, Mexico had a relatively small decrease in its output level in 2012 from 2.96 MMbbl/d to 2.94 MMbbl/d, despite output stabilization efforts. According to OPEC's secondary sources, Venezuela maintained its production levels around 2.38 MMbbl/d in 2012. The EIA estimates that world oil consumption grew by +0.9 MMbbl/d in 2012 to 89.2 MMbbl/d; meanwhile OECD consumption fell by 0.4 MMbbl/d, and non-OECD consumption grew 1.3 MMbbl/d in 2012. In 2013, Asia is expected to be the leading contributor for global consumption growth.

In 2012, OPEC crude oil production increased to 31.0 MMbbl/d from 29.8 MMbbl/d in 2011, led primarily by Saudi Arabia (production level around 10 MMbbl/d), UAE, Kuwait and Iraq. On the other hand Libya's production is estimated to average 1.5 MMbbl/d, below its pre-crisis level of 1.7 MMbbl/d. As Iran's crude oil sanctions continue, production is estimated to have decreased to 2.96 MMbbl/d from 3.66 MMbbl/d, according to EIA. This, in turn, caused OPEC production to increase, triggering a fall of OPEC's spare capacity to 2.0 MMbbl/d from a previously estimated 2.3 MMbbl/d in 2011. It is estimated that OPEC will continue to produce over 30 MMbbl/d of crude oil during the next two years to accommodate the projected increase in world oil consumption and to counterbalance supply disruptions.

In 2012, the WTI-Brent spread widened to a negative \$17.53/bbl differential in 2012 from a negative \$15.80/bbl in 2011 (-\$1.73/bbl), enabling market arbitrage opportunities into Asia and Europe. WTI and Brent continue to be the most actively traded spot crude oils in both the physical and paper markets. Bottlenecks (mainly due to limited transportation facilities to distribute the crude from Cushing to the refineries), has maintained WTI's disconnection to other physical markets. Nonetheless, these bottlenecks are expected to improve in the future due to entry of new pipeline capacity, such as the Seaway reaching 0.4 MMbbl/d in first quarter of 2013 (+0.25 MMbbl/d vs. 2012).

Prices and Sales Volume

- As indicated in the table below, the Company's combined realized international oil prices was \$103.28/bbl, higher by \$9.13/bbl as compared to the average WTI prices, due to a strong marketing activity coupled with a consistent close monitoring of WTI vs. Brent spread throughout the year.
- In the fourth quarter of 2012, natural gas sales averaged 62.89 MMcf/d, mainly from La Creciente field, at an average price of \$7.71/MMBtu (equivalent to \$7.68/MMcf), representing a premium of 28% over the weighted domestic regulated price of \$6.04/MMBtu for the quarter. This volume decreased slightly compared to the same period of 2011 when the sales volume was 63.95 MMcf/d. The reason was the lower volume available from the minor fields and the use of the natural gas to produce electricity in the Abanico field.
- In 2012, natural gas sales volumes were 62.14 MMscf/d on average, representing a 2.1% decrease from 63.5 MMscf/d for 2011. However, the revenue in 2012 was \$168,358,729 representing a 27% increase versus 2011 when the revenue for natural gas sales was \$132,186,545. These sales were mainly from La Creciente field, at an average price of \$7.43/MMBtu (equivalent to \$7.41/MMscf), representing a premium of 26% over the weighted domestic regulated price of \$5.90/MMBtu, and 163% over the Henry Hub natural gas prices in the United States during the same period.

Average benchmark crude oil and natural gas prices for the year 2012 and the fourth quarter were as follows:

Average Crude Oil and Gas Prices	Year Ended December		Three Months Ended December	
	2012 (\$/bbl)	2011 (\$/bbl)	2012 (\$/bbl)	° API
Domestic Market ⁽¹⁾	\$103.22	\$94.73	\$98.19	12.5
WTI NYMEX (Weighted Average of PRE Parcels)	\$94.04	\$94.57	\$88.10	38
Vasconia (Weighted Average of PRE Cargoes and Parcels) ⁽²⁾	\$106.02	\$107.95	\$100.94	24
Castilla (Weighted Average of Cargoes PRE) ⁽³⁾	\$103.56	\$97.23	\$100.45	19
Rubiales Blend Export. Barranquilla (Weighted Average Cargoes PRE) ⁽⁴⁾	\$94.32	\$97.19	\$94.49	12.5
Bunker (380 - 500) ⁽⁵⁾	\$100.77	-	\$104.15	
Combined Realized International Oil Sales Price	\$103.28	\$98.63	\$99.62	
PRE Natural Gas Sales (\$/MMBTU)	\$7.43	\$6.09	\$7.71	
Combined Realized Oil and Gas Sales Price	\$97.39	\$92.21	\$94.70	
WTI NYMEX (\$/bbl)	\$94.15	\$95.11	\$88.23	
BRENT ICE (\$/bbl)	\$111.68	\$110.91	\$110.13	
Regulated Gas Price (\$/MMBTU) ⁽⁶⁾	\$5.90	\$4.88	\$6.04	
Henry Hub average Natural Gas Price (\$/MMBtu)	\$2.83	\$4.03	\$3.54	

(1) Weighted average price of Rubiales and Cubiro sold domestic market.

(2) Weighted average price of 68 parcels and 6 cargoes of Vasconia crude oil in the year 2012. (4Q12= 24 parcels and 1 cargoes of Vasconia)

(3) Weighted average price of 27 Castilla crude oil cargoes in the year 2012. (4Q12 = 7 cargoes).

(4) Weighted average price of 30 Rubiales 12.5° API (Rubiales-Sabanero) small cargoes. (4Q12 = 10 small cargoes).

(5) Weighted average price of 77 Bunkers deliveries.

(6) The domestic natural gas sales price is referenced to MRP for gas produced in La Guajira field. The MRP is modified every six months based on the previous half-year variation of the US Gulf Coast Residual Fuel No. 6 1.0% sulphur, Platts.

Export Sales Volume

During the year of 2012 the Company sold 39.88 MMbbl (oil and gas) of which 35.71 MMbbl (89.54%) were exported. A breakdown of the export sales by destination follows:

Export destination

Destination	Year Ended December		Three Months Ended December	
	Volume (MMbbl)	%	Volume (MMbbl)	%
Asia	11.26	32%	5.88	58%
USA	10.07	28%	3.15	31%
Europe	8.77	24%	0.87	9%
LATAM/ Caribbean	4.61	13%	0.18	2%
Africa	1.00	3%	-	0%
Total Export	35.71	100%	10.08	100%

Export oil reference

Type Oil	Year Ended December		Three Months Ended December	
	Volume (MMbbl)	%	Volume (MMbbl)	%
Castilla Blend	25.45	71%	6.51	65%
Vasconia Blend	6.72	19%	1.87	18%
Rubiales	2.89	8%	1.43	14%
Bunkers	0.65	2%	0.27	3%
Total Export	35.71	100%	10.08	100%

Transport of Hydrocarbons

During the year 2012, the Company transported 117,284 bbl/d through the different pipelines and trucking systems as follows:

Means of transport	Year Ended December	Three Months Ended December
	Volume (Bbl/d)	Volume (Bbl/d)
ODL-OCENSA pipeline system	68,593	64,105
Crude oil transported through the ODC pipeline	16,473	19,467
Crude oil transported through the trucking system	32,218	44,690
Total Transport of Hydrocarbons	117,284	128,262

- The Guaduas Facility pumped 28,398 bbl/d of crude oil from the Company and third parties. This operation handled 11,879 bbl/d from third parties, generating an operational profit of \$2.3/bbl and a total profit of \$9.90 million, without any operational or environmental incidents during this quarter.
- Truck transportation costs were reduced by \$9.1 million during the fourth quarter of 2012, due to a renegotiation of transport rates. These savings were calculated by applying the average reduced transportation rates of \$2.22/bbl of the total volume of crude oil transported via trucks during this period.

6. Project Status

STAR Project in the Quifa Field

In March 2011, Pacific Rubiales and Ecopetrol agreed to advance with the STAR pilot project in the Quifa SW field as a preliminary step to expanding the technology. STAR is aimed at increasing the recovery in the Company's heavy oil fields in Colombia. The pilot test is being carried out in the Quifa SW field under the existing terms and conditions of the Association Contract.

All geological and reservoir studies have been completed and numerical simulations are in final steps. Production and air compression facilities have been completed in the Quifa pilot area and both are fully operational.

A cluster of nine wells has been constructed and a full primary production evaluation has been concluded, as well as two key tests undertaken in 2012. The steam injection test was performed in order to determine the response of the reservoir to increased temperature and a nitrogen test was performed in order to create a minimum gas saturation in the wellbore that will facilitate the upcoming air injection. Both tests indicated a positive response from the reservoir and the air injection started in February 2013. As of the date hereof, indirect measurements indicate that "in situ combustion" has taken place within the reservoir. All wells and production facilities are under continuous monitoring.

During September 2012, the Colombian Government (Colciencias) granted the Company a tax incentive for its investments in research and development in connection with the STAR technology. The incentive will provide an additional 75% deduction for the amounts invested and the possibility to fully depreciate the asset in the first year.

ODL Pipeline

The Company has a 35% interest in the ODL Pipeline with the balance of 65% owned by Ecopetrol. Since the ODL Pipeline began operations in 2009, a total of 211 MMbbl of diluted crude have been transported from the Rubiales field to the Monterrey and Cusiana Stations. The pipeline capacity was expanded in 2012 to 340,000 bbl/d.

For the twelve months ended December 31, 2012, the ODL Pipeline transported a total of 79 MMbbl and 35% of this volume corresponds to the Company's crude oil share. During the quarter the volume transported by ODL pipeline reached 20.4 MMbbl.

Carmentea – Araguaneý Pipeline Project

This new project involves an extension of the existing pipeline and comprises a new 85 km and 36 inch diameter pipeline with the capacity to transport up to 460,000 bbl/d between Cusiana and Araguaneý. This will allow additional volumes of oil transportation between the ODL Pipeline and the Bicentenario Pipeline ("**OBC Pipeline**").

As of December 2012, detailed engineering was ongoing. Purchase of pipe is expected to take place by third quarter 2013 once the environmental permits are approved.

Blending Project in Cusiana

This project will allow the blending of light oil trucked to a new diluent blending facility at the Cusiana station with heavy oil pumped through the ODL Pipeline. Consequently, API gravity in the ODL Pipeline will be reduced from 18 to 16 degrees with significant savings in diluent transportation costs. As of the date of this report, the project is under final stage of construction and commissioning, the project is expected to be operational in the second quarter 2013.

OBC Pipeline

In December 2010, the Company acquired a 32.88% equity interest in the OBC Pipeline. Oleoducto Bicentenario de Colombia S.A.S ("**OBC**") is a special purpose Company promoted by Ecopetrol, which has a 55.97% interest in the Company and with the participation of other oil producers operating in Colombia who control the remaining 11.15% interest. OBC will be responsible for the financing, design, construction and operation of the OBC Pipeline, Colombia's newest oil pipeline transportation system, which will run from Araguaneý, in the Casanare Department of central Colombia, to the Coveñas Export Terminal in the Caribbean.

The new pipeline will eventually add 450,000 bbl/d to the capacity of the existing pipeline systems, connecting the Eastern Llanos Basin to the export markets. The project, which will be constructed in phases, includes a new pipeline from Araguaneý Station to Coveñas export terminal. Total extension of this new pipeline is estimated to be 976 km with different sections of 30, 36 and 42 inch diameter line.

As of December 2012, phase 1, which comprises a 230 km, 42 inch pipeline from Araguaneý to Banadía, is under construction; 195 km of the pipeline have already been welded, the pumping station in Araguaneý is currently under expansion and two tanks of 600,000 bbl capacity each are currently under construction in the Coveñas terminal. The construction progress for phase 1 is 60% as of December 2012. The OBC Pipeline is expected to start pumping during the second half of 2013.

PEL – Power Transmission Line Project

The Company incorporated PEL, a wholly-owned subsidiary, in 2010. PEL is responsible for constructing and operating a new power transmission line of 230 kilovolts to connect the Rubiales field with Colombia's electrical grid. The new transmission line originates at the Chivor Substation and will stretch 260 km to the Rubiales field. The project includes two substations to supply power to the booster stations of the ODL Pipeline, as well as substations for the Rubiales and Quifa fields. The new power line will be able to supply up to 192 MVA that will be used in oil production and transportation activities. Field construction started in May 2012 and is expected to be completed by the third quarter of 2013. As of December 2012, the civil works in the Chivor substation were completed, and 115 out of 534 towers have been erected.

Small Scale LNG project

The Company is actively looking for alternate ways to monetize its existing natural gas reserves in La Creciente field, as well as exploiting its other extensive gas exploration resources in nearby fields. The Company has initiated a small scale liquefied natural gas (“LNG”) project that will be developed jointly with Exmar NV (“**Exmar**”), an experienced LNG/LPG transportation Company based in Belgium. The project is targeting LNG supply for power generation in Central America and the Caribbean.

The project comprises an 88 km, 18 inch gas pipeline from La Creciente to the Colombian Atlantic Coast and a Floating, Liquefying, Regasification and Storage Unit (“**FLRSU**”). The FLRSU may be connected to a Floating Storage Unit (“**FSU**”) in order to allow FOB exports to standard carriers (145,000 CBM).

In March 2012, the Company signed a tolling agreement with Exmar. Under the terms of this agreement, the first natural gas liquefaction is targeted for late 2014. Environmental permitting for the onshore portion of the gas pipeline was granted. Construction of the FLRSU is underway in WISON's shipyard on mainland China. Environmental licenses for the offshore pipeline (3.5 km) and port concessions are in progress. Basic engineering for the gas pipeline and offshore jetty started in the third quarter of 2012.

Water treatment project for agricultural development

In order to handle the increasing volumes of formation water produced in the mature Rubiales and Quifa fields, the Company has initiated a project which will treat produced formation water from these fields and employ it in water irrigation for development of a palm oil agricultural project for biodiesel manufacturing in the region. The first phase of this development includes the construction of two water treatment plants using Reverse Osmosis (RO) technology with a capacity of 500,000 bbl/d each. This project will bring significant savings in terms of energy and water injection facilities for water disposal. In addition, the palm oil project will create sustainable jobs and social development for the area.

As of December 2012, the basic engineering is in its final phase. Engineering, Procurement and Construction (EPC) contracts for the construction of the RO plants were awarded and environmental permitting was ongoing.

Puerto Bahía Project

As of December 31, 2012, the Company had an approximately 49% interest in Pacific Infrastructure, a private Company which is developing Puerto Bahía, an oil export terminal located in the Cartagena Bay in Colombia. Puerto Bahía will be developed in three phases: i) the first includes 1.7 MMbbl of oil and petroleum products storage capacity, a berthing position for vessels of up to 80K DWT, a truck loading/unloading station with a capacity of up to 30 Mbbbl/d and a fixed bridge; ii) the second envisions additional storage capacity of up to 3.3 Mbbbl, an additional berthing position for vessels of up to 150K DWT and barge handling facilities with a capacity of up to 45 Mbbbl/d; and iii) the third a multi-purpose terminal handling bulk materials, containers and a berthing platform measuring 300 metres.

During 2012, the environmental license, the port concession and the free trade zone permits were granted. Designs and engineering were also completed and construction of phase 1 started under an EPC contract.

Recognizing the strategic importance of world-class operating capabilities, Pacific Infrastructure signed a binding Memorandum of Understanding with Oiltanking International in December 2012. Oiltanking is recognized globally as a world-class operator of large-scale liquids terminals.

OLECAR Pipeline

Pacific Infrastructure is also developing the Olecar pipeline. This pipeline will connect Puerto Bahía with the oil pipeline hub at the port of Coveñas, ensuring the uninterrupted supply of crude oil for export. The Olecar project includes: i) a pumping station at Coveñas with a capacity of 300 Mbb/d; ii) a 30" diameter and 130 km pipeline; and iii) bidirectional connections between the Cartagena Refinery and Puerto Bahía.

As of December 2012, initial environmental studies were completed and right of way negotiations were in progress. Environmental permitting is expected in the second half of 2013.

7. Capital Expenditures

Excluding acquisition costs, capital expenditures during the year 2012, totaled \$1,548.2 million (\$1,096 million in 2011), 29% above the budget approved for 2012. As indicated below, \$594.8 million were invested in the expansion and construction of production infrastructure in order to ensure and increase the production capacity in Quifa and Rubiales fields; \$355.5 million went into exploration activities (including drilling, seismic, other geophysical activities) in Colombia, Peru and Guatemala; \$134.5 million of capital expenditures was spent on surface facilities and others; \$347.3 million for development drilling; and \$116.1 million in other projects including the STAR project. Details on the capital expenditure program for 2012 and 2011 are as follows:

(in thousands of US\$)	Year Ended December		Three Months Ended December	
	2012	2011	2012	2011
Production facilities	\$ 594,819	\$ 469,744	\$ 238,606	\$ 174,454
Exploration drilling including seismic acquisition ^{(1) (2)}	355,446	330,512	139,250	107,274
Early facilities and others ⁽²⁾	134,473	-	31,160	-
Development drilling	347,308	206,666	139,221	47,749
Other projects (STAR, Gas export, PEL)	116,150	89,083	53,119	20,605
Total capital expenditures	1,548,196	1,096,005	601,356	350,082

(1) Includes the drilling, seismic and other geophysical in Colombia, Peru and Guatemala

(2) Includes exploration investment, seismic acquisition and surface facilities of \$87 million in Maurel and Prom Colombia B.V. in which the Company holds a 49.999% participation and indirectly owns a 49.999% working interest in the Sabanero Block.

The following table shows the capital expenditures on acquisitions executed during the year 2012. Acquisitions were funded primarily by internally generated cash flow from operations:

(in thousands of US\$)	Year Ended December		Three Months Ended December	
	2012	2011	2012	2011
Acquisition Costs of Petromagdalena	\$ 226,598	\$ -	\$ -	\$ -
Z1 Block (Peru) ⁽¹⁾	266,448	-	85,000	-
Portofino Block (Colombia)	21,395	-	-	-
PPL37 Block (Papua New Guinea)	40,077	-	-	-
Karoon (Brazil)	40,000	-	40,000	-
C&C Energy Ltd. (Colombia) ⁽²⁾	533,647	-	533,647	-
Total capital expenditures for new acquisitions	1,128,165	-	658,647	-

(1) Acquisition of a 49% participating interest in Block Z-1, effective January 1, 2012. Revenue and production from Peru will be recognized on closing of the Block Z-1 transaction. The governmental approval was received in December 2012. The closing of the transaction occurred, in December 12, 2012.

(2) Correspond to acquisition of C&C paid through issuance of 22.8 million of common shares of the Company and cash consideration of \$65 thousand. See additional information in Note 4 to the audited consolidated financial statements.

8. Proved and Probable Oil and Gas Reserves

For the year ended December 31, 2012, the Company received independent certified reserves evaluation reports for all its assets, establishing that total net 2P reserves have grown to 513.7 MMboe from 407.3 MMboe, representing a 26% year- on year growth. This growth represents a 398% reserve replacement with net 2P reserve additions of 3.98 boe per boe produced. 1P reserves of 335.5 MMboe now represent 65% of the total 2P reserves; a growth of 5% when compared to the same period of 2011. The 1P reserves represent 1.05 boe per outstanding share (compared to 1.09 per share at December 31, 2011). The Company's RLI increased to 14 from 13. Approximately 77% of net 2P reserves are liquid hydrocarbons with the majority of these being heavy oil.

92 MMboe reserve additions were from acquisitions. This includes 64.6 MMboe of first reserve bookings in Peru's offshore Block Z-1 and 33.5 MMboe of additional reserves from the PetroMagdalena and C&C acquisitions, onshore Colombia. At year-end 2012, the Rubiales field represents less than 19% of total 2P reserves, demonstrating successful diversification of the Company's reserve base.

The following tables summarize information contained in the independent reserves reports prepared by RPS Energy Canada Ltd. ("RPS") dated February 18, 2013, Petrotech Engineering Ltd. ("Petrotech") dated February 28, 2013 and Netherland, Sewell & Associates, Inc. ("NSAI") dated January 31, with an effective date of December 31, 2012. RPS evaluated the reserves of the Company in the developed Rubiales and Quifa SW heavy oil fields, Petrotech evaluated the reserves in the remaining oil and gas fields in Colombia and the natural gas reserves in the Block Z-1, Peru and NASI evaluated the oil reserves in the Block Z-1, Peru. These reports were prepared in accordance with the definitions, standards and procedures contained in the Canadian Oil and Gas Evaluation Handbook ("COGE Handbook") and the National Instrument 51-101 – *Standards of Disclosure for Oil and Gas Activities* ("NI 51-101").

Reserves at December 31, 2012 (MMboe ⁽¹⁾)											
Country	Field	Total Proved (1P)			Probable (P2)			Proved Plus Probable (2P)			Hydrocarbon Type
		100%	Gross	Net	100%	Gross	Net	100%	Gross	Net	
Colombia	Rubiales	277.1	117.0	93.6	6.2	2.8	2.2	283.3	119.8	95.8	Heavy Oil
	Quifa SW	115.4	69.2	58.0	29.7	17.8	15.1	145.1	87.0	73.1	Heavy Oil
	Cajua	64.8	38.9	32.9	51.3	30.8	24.4	116.0	69.6	57.3	Heavy Oil
	Quifa Norte	11.3	6.8	6.0	36.3	21.8	18.1	47.6	28.6	24.1	Heavy Oil
	CPE-6	-	-	-	114.2	57.1	44.5	114.2	57.1	44.5	Heavy Oil
	Sabanero ⁽²⁾	20.0	10.0	9.0	-	-	-	20.0	10.0	9.0	Heavy Oil
	La Creciente	79.1	79.1	73.6	-	-	-	79.1	79.1	73.6	Natural Gas
	Guama	16.2	16.2	15.2	20.3	20.3	19.0	36.5	36.5	34.2	Natural Gas & Condensate
	Other Minor Blocks	7.1	3.0	2.7	2.5	1.5	1.2	9.6	4.5	3.9	Oil & Associated Natural Gas
	PMD Blocks	19.3	10.9	10.1	12.2	7.1	6.6	31.5	18.1	16.6	Light & Medium Oil
	C&C Blocks	18.0	18.0	15.1	2.0	2.0	1.8	20.0	20.0	16.9	Light & Medium Oil
	Sub-total	628.4	369.2	316.2	274.5	161.1	132.9	902.9	530.2	449.1	Oil & Natural Gas
Peru	Block Z-1	42.0	20.6	19.3	99.6	48.8	45.3	141.4	69.3	64.6	Light & Medium Oil, Natural Gas
	Total at Dec. 31, 2012	670.4	389.8	335.5	374.1	209.9	178.2	1,044.3	599.5	513.7	Oil & Natural Gas
	Total at Dec. 31, 2011	686.6	383.9	318.8	206.5	110.1	88.5	893.2	493.9	407.3	
	Difference	(16.2)	5.9	16.7	167.6	99.8	89.7	151.1	105.6	106.4	
	2012 Production ⁽³⁾	90.2	43.4	35.7	Total Reserves Incorporated			241.3	149.0	142.1	

(1) The term "boe" is expressed herein using the Colombian conversion standard of 5.7 Mcf: 1 bbl required by the Colombian Ministry of Mines and Energy and 6 Mcf: 1bbl for the Company's Peru reserves.

(2) The Company indirectly owns 49.999% of Maurel and Prom Colombia B.V., which owns the Sabanero Block.

(3) Includes production attributed from the acquisition of the 49% interest in Block Z-1, Peru effective as of January 1, 2012.

In the table above, 100% refers to total 100% field interest; Gross refers to WI before royalties; Net refers to WI after royalties; Numbers in table may not add due to rounding differences

All additional reserves information as required under NI 51-101, including the revised Block Z-1 oil reserves, will be included in the Company's Annual Information Form dated March 13, 2013.

9. Discussion of 2012 Financial Results

Revenues

(in thousands of US\$)	Year Ended December		Three Months Ended December	
	2012	2011	2012	2011
Net crude oil and gas sales	\$ 3,677,652	\$ 3,242,207	\$ 1,030,781	\$ 916,793
Trading revenue	207,110	138,612	15,908	94,683
Total Revenue	\$ 3,884,762	\$ 3,380,819	\$ 1,046,689	\$ 1,011,476
\$ per boe oil and gas	96.58	91.58	94.61	100.52
\$ per boe Trading	114.62	110.10	100.66	113.51
\$ Total average Revenue per boe	97.39	92.21	94.70	101.61

Total crude oil and gas sales revenues in the year 2012 were \$3,884.8 million, \$503.9 million higher than the same period of 2011. Net sales increased by 15% due to an increase in the barrels sold and a higher realized combined price. For additional details related to oil and gas sales, please refer to section 5 – Commercial Activities.

Following is an analysis of the revenue drivers for the year 2012 as compared to the same period of 2011:

	Year Ended December			
	2012	2011	Differences	% Change
Total of boe sold (Mboe)	39,887	36,663	3,224	9%
Avg. Combined Price - oil & gas and trading (\$/bbl)	97.39	92.21	5.18	6%
Total Revenue (000\$)	3,884,762	3,380,819	503,943	15%

Revenue increase due to the change in volume and price for the year end of 2012 in comparison to the year end of 2011 is as follows:

Reasons for the difference (000\$):			
Increase due to Volume	297,284		59%
Increase due to Price	206,659		41%
	<u>503,943</u>		

	Three Months Ended December			
	2012	2011	Differences	% Change
Total of boe sold (Mboe)	11,053	9,955	1,098	11%
Avg. Combined Price - oil & gas and trading (\$/bbl)	94.70	101.61	6.91	-7%
Total Revenue (000\$)	1,046,689	1,011,476	35,213	4%

Revenue increase due to the change in volume and price for the fourth quarter of 2012 in comparison to the same period of 2011 is as follows:

Drivers for the revenue increase (000\$):			
Due to Volume	111,556		317%
Due to Price	(76,343)		-217%
	<u>35,213</u>		

Operating Costs

(in thousands of US\$)	Year Ended December		Three Months Ended December	
	2012	2011	2012	2011
Oil and Gas Operating Costs	\$ 1,320,396	\$ 1,104,994	\$ 434,665	\$ 288,152
Trading Operating Costs	201,004	134,110	15,328	91,581
(Underlift) Overlift	65,020	6,405	90,079	(6,365)
Total Cost	\$ 1,586,420	\$ 1,245,509	\$ 540,072	\$ 373,368
\$ per boe crude oil and gas	34.67	31.21	39.90	31.60
\$ per boe Trading Operating Costs	111.24	106.52	96.99	109.79
\$ per boe Under/Overlift	1.71	0.18	8.27	(0.70)
\$ Total average Cost per boe	39.77	33.97	48.86	37.51

Operating costs for the entire 2012 totaled \$1,586.4 million (\$39.77/boe), higher by 17% as compared to 2011 (\$33.97/boe). This increase was mainly due to:

- Increased water disposal of Rubiales, Quifa and Cajua fields due to higher production volumes in 2012.
- The significant increase of crude oil for trading volumes in 2012 also increased the operating costs by 5%, as compared to the year 2011. Trading volumes are locally purchased in Colombia to third party crude oil producers subject to WTI reference price.
- Increased land transportation cost at Cajua field as the fluid is currently transported by tank truck to the water treatment facilities. Nevertheless, loading facilities were constructed by the end of 2012 and additional flow lines are planned to be constructed as soon as the license is obtained, which will bring down the transportation costs for Cajua field in 2013.
- Workover and maintenance activities executed throughout the year.
- Increase in the overlift cost by \$8.87/bbl due to the booking of a provision of \$92 million to settle the additional volume to Ecopetrol under PAP in Quifa SW field, as indicated under the heading entitled "Royalties".

Depletion, Depreciation and Amortization

(in thousands of US\$)	Year Ended December		Three Months Ended December	
	2012	2011	2012	2011
Depletion, depreciation and amortization	\$ 851,444	\$ 656,912	\$ 231,588	\$ 174,086
\$ per boe	21.35	17.92	20.95	17.49

Depletion, depreciation and amortization (“DD&A”) costs for the year 2012 were \$851.4 million (\$656.9 million in the same period of 2011). The increase of 30% over 2011 was primarily due to the increase in production and higher costs subject to depreciation. The increase was primarily due to the higher depreciable cost base of oil and gas properties primarily resulting from the acquisition of PetroMagdalena.

Impairment of E&E Assets

(in thousands of US\$)	Year Ended December		Three Months Ended December	
	2012	2011	2012	2011
Impairment of E&E Assets	\$ 102,060	\$ 12,066	\$ 75,772	\$ 12,066
\$ per boe	2.56	0.33	6.86	1.21

In 2012 the Company recognized an impairment loss of \$102.1 million on the write-down of certain exploration and evaluation assets based on an evaluation of the net recoverable amount of the fields.

General and Administrative

(in thousands of US\$)	Year Ended December		Three Months Ended December	
	2012	2011	2012	2011
General and administrative costs	\$ 279,947	\$ 176,218	\$ 77,576	\$ 71,437
\$ per boe	7.02	4.81	7.02	7.18

General and administrative expenses for the year 2012 were \$279.9 million, representing a \$103.7 million increase from the same period in 2011. The increase in G&A costs were primarily due to:

- Approximately 50% of the G&A increase resulted from the higher number of direct and indirect employees in 2012 due to the significant increase in the exploratory and producing activities of the Company. Total employees as of December 31, 2012 were 2,273 compared to 1,713 in the same period in 2011, a 33% increase.
- The remaining increase was mainly due to additional costs related to expansions in Colombia, Brazil, Peru and Papua New Guinea, and increase in the cost of back office, office rental, field personnel and technical assistance to support the growth of production and exploration activities.

Share-Based Compensation

(in thousands of US\$)	Year Ended December		Three Months Ended December	
	2012	2011	2012	2011
Share-based compensation	\$ 32,902	\$ 48,783	\$ 853	\$ 316
\$ per boe	0.82	1.33	0.08	0.03

Share-based compensation decreased by \$15.88 million or 32.6% to \$32.90 million as compared to \$48.78 million for 2011.

The Company granted 6 million options during 2012 with an average fair value of C\$8.58 per option compared to 4.6 million options granted in 2011 at a fair value of C\$10.47 per option.

Finance Cost

(in thousands of US\$)	Year Ended December		Three Months Ended December	
	2012	2011	2012	2011
Finance costs	\$ 91,299	\$ 86,469	\$ 24,333	\$ 15,501
\$ per boe	2.29	2.36	2.20	1.56

Finance cost includes interest on the Company's bank loans, convertible debentures, senior notes, revolving credit commitment fees, finance leases and fees on letters of credit. For the year 2012, interest expense totaled \$91.3 million compared to \$86.5 million for the same period of 2011. The increase in finance costs is due to interest on the new senior notes and revolving credit facilities.

Equity Investments

(in thousands of US\$)	Year Ended December		Three Months Ended December	
	2012	2011	2012	2011
(Loss) gain from equity investment	\$ (57,668)	\$ 6,829	\$ (15,586)	\$ 5,059
Loss Impairment of equity investment	(45,265)	-	(45,265)	-
Total Equity Investments	\$ (102,933)	\$ 6,829	\$ (60,851)	\$ 5,059
\$ per boe	(2.58)	0.19	(1.41)	0.51

Included in loss from equity investments is an impairment of \$45.3 million. The impairment consists of \$29.4 million relating to Pacific Coal and \$15.9 million related to CGX. Both investments have been recorded at their fair values estimated at their quoted prices at December 31, 2012.

Equity Tax Expense

(in thousands of US\$)	Year Ended December		Three Months Ended December	
	2012	2011	2012	2011
Equity Tax	\$ -	\$ 68,446	\$ -	\$ -
\$ per boe	-	1.87	-	-

On December 29, 2010, the Colombian Congress passed a law that imposes a surcharge on the existing equity tax levied on Colombian companies. This surcharge increased the equity tax rate for the Company from 4.8% to 6% and is applied on the net taxable equity as of January 1, 2011. The Company's total equity tax payable for the years 2012 to 2014 is \$34 million, to be paid in four equal installments. Nevertheless, the Company has recognized the full equity tax payable on the consolidated statement of financial position with a corresponding expense in 2011. The amount recognized is calculated by discounting the eight future equity tax payments by the Company's weighted cost of capital at 10.8%.

Foreign Exchange

(in thousands of US\$)	Year Ended December		Three Months Ended December	
	2012	2011	2012	2011
Foreign exchange gain (loss)	\$ 577	\$ (39,894)	\$ 13,421	\$ 1,947
\$ per boe	0.01	(1.09)	1.21	0.20

Foreign exchange gains or losses primarily result from the movement of the Colombian peso ("COP") against the U.S. dollar, which is the Company's functional currency. Foreign exchange gain for 2012 was a net amount of \$0.6 million, compared to a loss of \$39.9 million for the same period 2011. The immaterial effect of the foreign exchange in 2012 was due to an offset between the unrealized loss, related to foreign currency hedging contracts, and the appreciation of the COP against the U.S. dollar throughout 2012.

Incentive for early conversion of debentures

(in thousands of US\$)	Year Ended December		Three Months Ended December	
	2012	2011	2012	2011
Incentive for early conversion of debentures	\$ -	\$ 46,489	\$ -	\$ 46,489
\$ per boe	-	1.27	-	4.67

During the fourth quarter of 2011, the Company recognized the fair value of \$46.5 million of the incentive provided for the C\$236.2 million (or 98.9%) of the Debentures that were converted under the early conversion program. Debenture holders who did not convert during the early conversion period were not entitled to the benefit of the incentive conversion rate nor to receive the additional common shares.

Income Tax Expense

(in thousands of US\$)	Year Ended December		Three Months Ended December	
	2012	2011	2012	2011
Current income tax	\$ 469,217	\$ 513,302	\$ 122,916	\$ 186,543
Deferred income tax	(179,379)	(65,152)	(85,119)	3,015
Total Income Tax Expense	\$ 289,838	\$ 448,150	\$ 37,797	\$ 189,558
\$ per boe	7.27	12.22	3.42	19.04

The income tax rate in Canada was lowered to 26.5% for 2012 compared to 28.25% for 2011, and in Colombia the tax rate remained at 33% for the year 2012.

During September 2012, the Colombian Government (Colciencias) granted the Company a tax incentive for its investments in R&D on the STAR technology. The incentive will provide an additional 75% deduction on the expenditures incurred and the possibility to fully depreciate the asset in the first year. The resulting tax benefit on actual expenditures incurred is estimated to be \$22.9 million.

Colombian Congress approved a new tax law in December 2012. Effective January 1, 2013, the statutory income tax rate was reduced from 33% down to 25%. In addition, the law introduced an incremental 9% income tax surcharge to substitute the elimination of certain payroll taxes, primarily related to low income salaries. As a result, the newly approved income tax rate was increased to 34% (considering the additional 9%). The Company estimates that the increase in the income tax rate will in turn, increase the tax burden between 4 – 6% for 2013. Other changes introduced in the tax law may not materially impact the Company's tax expense.

The effective tax rate was 35% in 2012 compared to 44%, the decrease is primarily due to the non-taxable foreign exchange gains and the R&D special benefit deducted in 2012.

Net Earnings

(in thousands of US\$)	Year Ended December		Three Months Ended December	
	2012	2011	2012	2011
Net earnings	\$ 527,729	\$ 554,336	\$ (23,777)	\$ 80,834
\$ per boe	13.23	15.12	(2.15)	8.12

Net earnings for the year 2012 totaled \$527.7 million compared to net earnings of \$554.3 million in 2011. Net earnings for the year 2012 were primarily impacted by higher DD&A and impairment and overlift of \$92 million as compared to the same period of 2011, as well as by a number of non-cash items totaling \$125.1 million. These non-cash items are related to share-based compensation of \$32.90 million, foreign exchange gain of \$0.6 million, losses from equity investments of \$102.9 million and loss on risk management contracts of \$10.1 million. These non-cash items may or may not materialize in future periods. Excluding these items, the Company's adjusted net earnings were \$653 million (\$742 million in 2011) or \$2.22 per basic common share (\$2.73 in 2011).

Cash Flow from Operations

(in thousands of US\$)	Year Ended December		Three Months Ended December	
	2012	2011	2012	2011
Cash flow from operations	\$ 1,802,735	\$ 1,219,057	\$ 676,938	\$ 477,530
\$ per share, basic	6.12	4.48	2.28	1.70
\$ per share, diluted	5.95	4.09	2.23	1.66

The Company continued to generate positive cash flow from operations as a result of the increase in production together with the increase in the combined realized oil and gas price. The cash flow from operations during the year 2012 totaled \$1,802.7 million. This increase was driven by a significant increase in production and in realized prices during 2012.

Financial Position

EBITDA

EBITDA for the year 2012 totaled \$2,018.4 million, which represents an increase of 3.0% compared to \$1,959.1 million in 2011. The increase is attributable to increased revenue, mainly generated from international oil sales (89%); EBITDA from gas and domestic sales contributed 10% and 1%, respectively. EBITDA in the year 2012 represents a 52% margin in comparison to total revenues for the period (58% margin in 2011).

Debts and Credit Instruments

During the fourth quarter of 2011, the Company restructured its convertible debentures and senior notes, lowering the overall cost of borrowing and also providing the flexibility and capacity required for the Company to continue executing its business strategies. The Company was compliant with all of its debt covenants during the fourth quarter of 2012. The following debts are outstanding as at December 31, 2012:

2009 Senior Notes

The 2009 senior notes are direct, unsecured subordinated obligations with maturity dates of November 10, 2014 (33.3%), November 10, 2015 (33.3%), and November 10, 2016 (33.4%) and an interest rate of 8.75% payable semi-annually (the "2009 Senior Notes"). The 2009 Senior Notes are on the Official List of the Luxembourg Stock Exchange and trade on the Euro MTF. The principal amount outstanding on the 2009 Senior Notes as at December 31, 2012 was \$91.5 million.

2011 Senior Notes

The 2011 senior notes, due December 12, 2021, are direct, unsecured, subordinated obligations with an interest rate of 7.25% payable semi-annually (the "2011 Senior Notes"). The 2011 Senior Notes are on the Official List of the Luxembourg Stock Exchange and trade on the Euro MTF. As the December 31, 2012 the principal outstanding on the 2011 Senior Notes was \$712 million.

Revolving Credit Facility

On September 13, 2012, the Company entered into two Revolving Credit and Guaranty Agreements: (i) \$400 million Revolving Credit and Guaranty Agreement (the "**U.S. Dollar Facility**") with a syndicate of international lenders and Bank of America, N.A., as administrative agent; and (ii) Meta Petroleum Corp. Colombia Branch and Pacific Stratus Energy Corp. Colombia Branch, entered into a Colombian peso equivalent of \$300 million Revolving Credit Agreement as borrowers (the "**Colombian Peso Facility**"), with a syndicate of Colombian lenders and Sociedad Fiduciaria Bogotá, S.A., as administrative agent.

These revolving credit facilities have an interest rate determined in accordance with the ratings assigned to the Company's senior debt securities by Standard & Poor's Ratings Group, Moody's and Fitch Inc. Based on the Company's credit rating as at December 31, 2011 and March 31, 2012, the interest rate was LIBOR plus 2.75% under the U.S. Dollar facility and DTF + 2.25% under the Colombian Peso Facility. In addition, the Company is required to pay commitment fees of 0.95% on the unutilized portion under the U.S. Dollar Facility and 0.40% under the Colombian Peso Facility of any outstanding commitments under the two facilities. As at December 31, 2012, the Company has drawn down \$353.6 million on the U.S. Dollar Facility and \$24.9 million on the Colombian Peso Facility.

Itau Credit Facility

On February 6, 2013, the Company entered into a Committed Credit Facility of a total amount of \$100 million with Banco Itau BBA. S.A. This credit facility has an interest rate of LIBOR + 2.4%. In addition, the Company is required to pay a commitment fee of 0.7% of the unutilized portion. The Company has not yet drawn down on the facility.

Convertible Debentures

The Company has outstanding convertible unsecured subordinated debentures due August 29, 2013 (the "Debentures") of C\$2.7 million in face amount as at December 31, 2012. The Debentures bear interest at 8% annually and are payable semi-annually. The outstanding Debentures are convertible into common shares of the Company at the rate of C\$12.83 (2011 – C\$12.83) per share, being equivalent to 77.9423 (2011 – 77.9423) common shares per C\$1,000 face amount of Debentures, subject to adjustments pursuant to the indenture. As at December 31, 2012 the principal outstanding on the Debentures was C\$2.7 million.

Letters of Credit

As at December 31, 2012, the Company has issued letters of credit and guarantees for exploration and operational commitments for a total of \$257 million.

Outstanding Share Data

Common Shares

As at December 31, 2012, 318,369,088 common shares were issued and outstanding.

The Company does not have shares subject to escrow restrictions or pooling agreements.

Stock Options and Warrants

As at December 31, 2012, nil warrants to acquire an equal number of common shares were outstanding and exercisable and 24,858,465 stock options were outstanding, of which all were exercisable.

Liquidity and Capital Resources

Liquidity

Funds provided by operating activities for the year 2012 totaled \$1,802.7 million (\$1,219.1 million in 2011). The increase in cash flow in 2012 was the result of the increase in production and higher combined crude oil and gas sale prices. The Company has been generating cash flows from operations from the sale of crude oil and natural gas and continues to plan for increased future production.

As of December 31, 2012, the Company had working capital of \$-305.4 million, mainly comprised of \$243.7 million of cash and cash equivalents, \$777.1 million of account receivables, \$125 million of inventory, \$42.3 million of income tax receivable, \$1.9 million of prepaid expenses, \$1,209.3 million of accounts payable and accrued liabilities, \$258.5 million of income tax payable, \$7.4 million of current portion of long term debt and \$20.2 million of finance lease obligations.

As at December 31, 2012, the Company has drawn down \$353.6 million under the available \$400 million U.S. Dollar Facility and has drawn down \$24.9 million under the available \$300 million Colombian Peso Facility.

During February 2013 the Company entered into a new credit facility with Banco Itau for \$100 million. The Company has not drawn down on the facility.

The Company believes it has adequate resources to fund its capital plan for 2013, with the Company's cash flows from operations and current debt facilities. With respect to the Company's broader integration strategy, the Company will pay for the expansion plan with its own cash flow. However, if additional resources are required, there are possible sources of funds available to the Company to finance additional capital expenditures and operations including the revolving credit facility, existing working capital incurring new debt, and the issuance of additional common shares, if necessary.

10. Commitments and Contingencies

As part of the Company's normal course of business, the Company entered into arrangements that will impact the Company's future operations and liquidity. The principal commitments of the Company are ship or pay arrangements on crude oil and gas transportation, asset retirement obligations, debt repayments, service contracts with suppliers in relation to the exploration and operation of oil properties and engineering and construction contracts, among others.

Disclosure concerning the Company's significant commitments can be found in Note 20 to the audit consolidated financial statements. The Company has no off-balance sheet arrangements.

11. Risk Management Contracts

The Company enters into derivative financial instruments to reduce the exposure to unfavorable movements in commodity prices, interest rates and foreign exchange rates. The Company has established a system of internal controls to minimize risks associated with its derivative program and does not intend to use derivative financial instruments for speculative purposes.

Commodity price risk

Commodity price risk is the risk that the cash flows and operations of the Company will fluctuate as a result of changes in commodity prices. Significant changes in commodity prices can also impact the Company's ability to raise capital or obtain additional debt financing. Commodity prices for crude oil are impacted by world economic events that dictate the levels of supply and demand. From time to time the Company may attempt to mitigate commodity price risk through the use of financial derivatives. The Company recognizes the fair value of its derivative instruments as assets or liabilities on the statement of financial position. None of the Company's commodity price derivatives currently qualify as fair value hedges or cash flow hedges, and accordingly, changes in their fair value are recognized in net earnings.

The Company has the following commodity price risk management contracts outstanding (fair value in thousands):

As at December 31, 2012

Asset

Instrument	Term	Volume (bbl)	Floor/ceiling or strike price (\$/bbl)	Benchmark	Fair value
Zero cost collars	January to June 2013	1,200,000	80 - 115/118	WTI	\$ 1,023
Total					\$ 1,023
Current					1,023
Total					\$ 1,023

Liabilities

Instrument	Term	Volume (bbl)	Floor/ceiling or strike price (\$/bbl)	Benchmark	Fair value
Zero cost collars	January to June 2013 extendible July to December 2013	5,280,000	80 / 111-121	WTI	\$ (3,176)
Total					\$ (3,176)
Current					(3,176)
Total					\$ (3,176)

As at December 31, 2011

Liabilities

Instrument	Term	Volume (bbl)	Floor/ceiling or strike price (\$/bbl)	Benchmark	Fair value
Call option	February 2012 to December 2012	8,790,000	109.50 -120	WTI	\$ (29,353)
Sold put	August 2012 to December 2012	5,350,000	61.5 - 64	WTI	(8,732)
Zero cost collars	January 2012 to December 2012	10,051,404	70-80 / 115-121	WTI	(1,798)
Total					\$ (39,883)
Current					\$ (39,883)
Total					\$ (39,883)

For the year ended December 31, 2012, the Company recorded a gain of \$7.1 million (2011 \$8.8 million) on commodity price risk management contracts in net earnings. Included in these amounts were \$37.7 million in unrealized gain (2011: \$13.4 million) representing the change in the fair value of the contracts, and \$30.6 million (2011:\$4.6 million) of realized loss resulting from premiums paid.

If the forward WTI crude oil price estimated at December 31, 2012 had been \$1/bbl higher or lower, the unrealized gain or loss on these contracts would change by approximately \$3 million (2011: \$0.7 million).

Foreign currency exchange risk

The Company is exposed to foreign currency fluctuations in Colombian pesos (COP). Such exposure arises primarily from expenditures that are denominated in currencies other than the functional currency. The Company monitors its exposure to foreign currency risks. To reduce its foreign currency exposure associated with operating expenses incurred in COP, the Company may enter into foreign currency derivatives to manage such risks. The Company has the following currency risk management contracts outstanding (fair value in thousands):

As at December 31, 2012

Asset

Instrument	Term	Notional amount	Floor-ceiling (COP/\$)	Fair value
Currency collar	January to December 2013	\$ 525,000	1825-1986	\$ 22,590
Forward	March to December 2013	17,500	1,890	1,699
Forward	May 2013 to February 2014	17,500	1,910	1,348
		\$ 560,000		\$ 25,637
Current				\$ 25,367
Non-current				270
Total				\$ 25,637

As at December 31, 2011

Liability

Instrument	Term	Notional amount	Floor-ceiling (COP/\$)	Fair value
Currency collar	January to December 2012	\$ 650,400	1805 - 1975	\$ (27,504)
Currency collar	January to December 2013	120,000	1870 - 1930	(5,397)
		\$ 770,400		\$ (32,901)
Current				\$ (27,504)
Non-current				(5,397)
Total				\$ (32,901)

The Company has designated currency collars as cash flow hedges. The effective portion of the change in the fair value of the currency collars is recognized in other comprehensive income as unrealized gains or losses on cash flow hedges. The effective portion is re-classified as production and operating expenses in net earnings in the same period as the hedged operating expenses are incurred. During the year ended December 31, 2012, \$70 million of unrealized gains

(2011 - \$14.5 million of unrealized losses) were initially recorded in other comprehensive income, and \$18.5 million (2011 - \$9.6 million) were subsequently transferred to production and operating cost when the gains became realized. The Company excludes changes in fair value due to the time value of the investments and records these amounts along with hedge ineffectiveness in foreign exchange gains or losses in the period that they arise. During 2012, \$13.2 million (2011 - \$19.5 million) of ineffectiveness was recorded as foreign exchange loss.

The currency forwards are COP-US dollar forwards that provide an early termination option to the counterparty when certain thresholds are reached. The currency forwards have not been designated as hedges and the change in fair value is recorded in profit or loss. For the year ended December 31, 2012, the Company recorded an unrealized gain of \$3 million (2011: Nil) representing the change in the fair value of the forward currency price risk management contracts in net earnings.

12. Selected Quarterly Information

(in thousands of US\$)	2012				2011			
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Financials:								
Net sales	\$ 1,046,689	\$ 870,369	\$ 1,035,854	\$ 931,850	\$ 1,011,476	\$ 828,285	\$ 957,509	\$ 583,549
Net earnings (loss) for the period	(23,777)	68,817	224,344	258,345	80,834	193,720	349,375	(69,593)
Earnings (loss) per share								
- basic	(0.08)	0.23	0.76	0.88	0.29	0.71	1.30	(0.26)
- diluted	(0.08)	0.23	0.74	0.85	0.28	0.65	1.17	(0.26)

13. Related-Party Transactions

According to IFRS, parties are considered to be related if one party has the ability to “control” (financially or by share capital) the other party or have significant influence (management) on the other party in making financial, commercial and operational decisions. On May 31, 2012, the board of directors of the Company created the New Business Opportunities Committee (the “**NBOC**”) to review and approve related party transactions. The NBOC is comprised of the following independent directors: Miguel Rodriguez (Chair), Dennis Mills, Victor Rivera and Hernan Martinez. The NBOC is apprised of related party transactions prior to implementation, engages independent legal counsel, as needed, and meets *in camera* to deliberate. The NBOC also reviews the business rationale for the transaction and ensures that the transaction is in compliance with applicable securities laws and the Company’s debt covenants.

The Company’s internal audit and legal compliance departments also monitor related party transactions. The audit and legal compliance teams work together to compose a list of potential related parties. This list is cross-checked against the Company’s list of suppliers and other creditors.

The related party transactions listed below were in the normal course of operations and were measured at fair value, which are the amounts of consideration established and agreed to by the related parties and which, in the opinion of management and the NBOC, are considered similar to those negotiable with third parties.

The following sets out the details of the Company’s related party transactions as measured at the exchange amount (\$ thousands, or unless otherwise stated):

- a) In June 2007, the Company entered into a 5-year lease agreement with Blue Pacific Assets Corp. (“**Blue Pacific**”) for administrative office space in one of its Bogota, Colombia locations. Monthly rent expense of \$57 is payable to Blue Pacific under this agreement. Messrs. Arata, de la Campa, Iacono (directors and officers of the Company) and von Siegmund (an officer of the Company) of the Company control, or provide investment advice to the holders of, 67.2% of the shares of Blue Pacific. During 2011, the lease was amended to include additional space in Bogota for a 10-year term with a monthly rent of \$0.4 million, and assignment of the lessor to an entity controlled by Blue Pacific.
- b) As at December 31, 2012, the Company had trade accounts receivable of \$4.4 million (December 31, 2011 - \$2.4 million) from Proelectrica, in which the Company has a 24.9% indirect interest and which is 31.49% owned by Blue Pacific. The Company’s and Blue Pacific’s indirect interests are held through Pacific Power Corp. Revenue from Proelectrica in the normal course of the Company’s business was \$39.3 million for the year ended December 31, 2012 (2011 - \$25.6 million).

In October, 2012, the Company and Ecopetrol signed two build, own, manage, and transfer (“**BOMT**”) agreements with Consorcio Genser Power-Proelectrica (“**Genser-Proelectrica**”) to acquire certain power generation assets for the Rubiales field. Genser-Proelectrica is a joint venture between Proelectrica and Genser Power Inc. which is 51% owned by Pacific Power Generation Corp. Total commitment under the BOMT agreements is \$229.7 million over ten years. At the end of the Rubiales Association Contract in 2016, the

Company's obligations along with the power generation assets will be transferred to Ecopetrol. As of December 2012, those assets are under construction and the Company has not made any payment.

- c) During the year ended December 31, 2012, the Company paid \$40.7 million (2011 - \$47.1 million) to Transportadora Del Meta S.A.S. ("**Transmeta**") in crude oil transportation costs. In addition the Company has accounts receivable of \$2.4 million (2011 - \$3.2 million) from Transmeta and accounts payable of \$8.5 million (2011 - \$5.5 million) to Transmeta as at December 31, 2012. Transmeta is controlled by Mr. German Efromovich, a director of the Company.
- d) Loans receivable from related parties in the aggregate amount of \$179 (2011 - \$490) are due from three directors and three officers (2011 - three directors and three officers) of the Company. The loans are non-interest bearing and payable in equal monthly payments over 48-month terms. The loans were issued to these individuals in connection with costs incurred by them as a result of their relocations.
- e) The Company has entered into aircraft transportation agreements with Petroleum Aviation Services S.A.S. ("**PAS**"), a Company controlled by Mr. Efromovich. During 2012, the Company paid \$14.3 million (2011 - \$9.5 million) in fees as set out under the transportation agreements. The Company's accounts payable to PAS as at December 31, 2012 are \$2.8 million (2011 - Nil).
- f) During the year ended, December 31, 2012, the Company paid \$125.8 million to ODL (2011 - \$80.2 million) for crude oil transport services under the pipeline take or pay agreement, and has accounts payable of \$5 million to ODL as at December 31, 2012 (2011 - \$1 million). In addition, the Company received \$0.8 million from ODL during the year ended December 31, 2012 (2011 - \$1.6 million) with respect to certain administrative services and rental equipment and machinery. The Company's accounts receivable from ODL as at December 31, 2012 was \$0.2 million (2011 - Nil).
- g) The Company will make subordinated loans to OBC for up to \$237.3 million, \$140 million of which have been made as of December 31, 2012. The principal of the subordinated loan will be repaid in 10 equal semi-annual installments starting in 2025, after OBC has repaid its bank loans in full. The loans carry an annual interest rate of 7.32% with semi-annual interest payments. As at December 31, 2012 the balance of loans outstanding to the Company under the agreement is \$32 million, (December 31, 2011: \$102.3 million). The Company has received \$2.1 million as at December 31, 2012 (2011: Nil) with respect to certain administrative services and rental equipment and machinery. As at December 31, 2012 the Company has Nil as short-term advance (December 31, 2011 - \$8 million) to OBC to fund on-going work commitments. Interest income of \$5.8 million was recognized and \$5.7 million was paid on the loan during 2012 (December 31, 2011: \$0.3 and Nil).
- h) As at December 31, 2012, the Company has accounts payable of Nil (December 31, 2011 \$0.4 million) due to Helicol with respect to air transportation services and paid during the year \$2.5 million for this service (2011 - \$1.3 million). Helicol is controlled by Mr. Efromovich a director of the Company.
- i) In October 2012 the Company entered into an agreement and consent with Pacific Coal, Blue Advanced Colloidal Fuels Corp. ("**Blue ACF**"), Alpha Ventures Finance Inc. ("**Alpha**"), and an unrelated party whereby the Company acquired from Pacific Coal a right to a 5% equity interest in Blue ACF for cash consideration of \$5 million. Blue ACF is a Company engaged in developing colloidal fuels, and is currently 100% owned by Alpha which is controlled by Blue Pacific. As part of the purchase Pacific Coal has also assigned to the Company the right to acquire up to an additional 5% equity interest in Blue ACF for an additional investment of up to \$5 million. The Company currently has a 14.4% equity interest in Pacific Coal.

14. New IFRS issued

Standards issued but not yet effective up to the date of issuance of the Company's financial statements that are likely to have an impact on the Company are listed below. This listing is of standards and interpretations issued, which the Company reasonably expects to be applicable at a future date. The Company intends to adopt those standards when they become effective.

IFRS 9 Financial Instruments: Classification and Measurement

In November 2009, the IASB issued IFRS 9, which covers classification and measurement as the first part of its project to replace IAS 39. In October 2010, the Board also incorporated new accounting requirements for liabilities. The standard introduces new requirements for measurement and eliminates the current classification of loans and receivables, available-for-sale and held-to-maturity, currently in IAS 39. There are new requirements for the accounting of financial liabilities as well as carryover of requirements from IAS 39. The Company does not anticipate early adoption and will adopt the standard on the effective date of January 1, 2015. The Company has not determined the impact of the new standard on the consolidated financial statements.

IFRS 10 Consolidated Financial Statements

IFRS 10 replaces the portion of IAS 27 Consolidated and Separate Financial Statements that addresses the accounting for consolidated financial statements. It also addresses the issues covered by SIC-12 Consolidation - Special Purpose Entities. This standard becomes effective for annual periods beginning on or after January 1, 2013.

IFRS 10 establishes a single control model that applies to all entities including structured entities (previously referred to as special purpose entities). The changes introduced by IFRS 10 will require management to exercise significant judgement to determine which entities are controlled and therefore are required to be consolidated by a parent, compared with the requirements in IAS 27. Based on the preliminary analysis performed, IFRS 10 is not expected to have any impact on the investments currently held by the Company.

IFRS 11 Joint Arrangements

IFRS 11 replaces IAS 31 Interests in Joint Ventures and SIC-13 Jointly-controlled Entities - Non-monetary Contributions by Venturers. This standard is effective for annual periods beginning on or after January 1, 2013.

IFRS 11 removes the option to account for certain types of jointly controlled entities (JCEs) using proportionate consolidation. Instead, JCEs that meet the definition of a joint venture must be accounted for using the equity method. Based on the preliminary analysis performed, IFRS 11 is not expected to have any impact on the investments currently held by the Company.

IFRS 12 Disclosure of Interests in Other Entities

IFRS 12 includes all of the disclosures that were previously in IAS 27 related to consolidated financial statements, as well as all of the disclosures that were previously included in IAS 31 and IAS 28. These disclosures relate to an entity's interests in subsidiaries, joint arrangements, associates and structured entities. A number of new disclosures are also required but will have no impact on the Company's financial position or performance. IFRS 12 is effective for annual periods beginning on or after January 1, 2013.

IFRS 13 Fair Value Measurement

IFRS 13 establishes a single source of guidance under IFRS for all fair value measurements. IFRS 13 does not change when an entity is required to use fair value, but rather provides guidance on how to measure fair value under IFRS when fair value is required or permitted. The Company is currently assessing the impact that this standard will have on the financial position and performance. Based on the preliminary analyses, no material impact is expected. This standard is effective for annual periods beginning on or after January 1, 2013.

15. Internal Controls over Financial Reporting ("ICFR")

In accordance with National Instrument 52-109 Certification of Disclosure in Issuers' Annual and Interim Filings ("**NI 52-109**") of the Canadian Securities Administrators ("**CSA**"), quarterly the Company issues a "Certification of Interim Filings" ("**Certification**"). The Certification requires certifying officers to state that they are responsible for establishing and maintaining Disclosure Controls and Procedures (DC&P) and Internal Control Over Financial Reporting (ICFR).

The Certification requires certifying officers to state that they designed DC&P, or caused it to be designed under their supervision, to provide reasonable assurance that: (i) material information relating to the Company is made known to the certifying officers by others; and (ii) information required to be disclosed by the Company in reports filed with, or submitted to, securities regulatory authorities is recorded, processed, summarized and reported within the time periods specified under Canadian securities legislation. In addition, the Certification requires certifying officers to state that they have designed ICFR, or caused it to be designed under their supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes.

The Company's Corporate Internal Audit department provides support to the Board of Directors, Audit Committee, and management, and contributes to the continuous improvement strategies of the organization. The corporate audit process provides reasonable assurance over the:

- Evaluation of design and operating effectiveness of internal controls over financial reporting and disclosure controls and procedures as promulgated by NI 52-109 as issued by the CSA,
- Effectiveness and efficiency of operations,
- Reliability of internal and external reporting, and
- Compliance with applicable laws and regulations.

On a quarterly basis, Corporate Audit evaluates the effectiveness of the DC&P and ICFR, encompassed within the requirements of NI 52-109. During this quarter, the evaluation was performed for 561 controls over 31 corporate processes. According to NI 52-109 PRE maintains documentary evidence sufficient to provide reasonable support for certification of DC&P and ICFR evaluation that included:

- A description and control matrix for each process evaluated.
- Determinable extent of testing for each of the 561 controls tested.
- A description of the evaluation tools applied according to sections 7.6 and 7.7 of the National Instrument.
- Conclusion about the operating effectiveness of the controls evaluated.
- Certification provided by owners regarding the conclusions and results of testing.

From this evaluation the Company concluded that there are no material weaknesses or significant deficiencies in the design and effectiveness of the controls evaluated. The identified control deficiencies and opportunities to improve the ICFR are in the following main areas:

- Contracts approved without the appropriate level of authorization.
- Equipment and facilities were not included into the operational maintenance program.
- Materials received without the review of quality certifications.
- Permits to transport crude by truck were not cancelled and reported on time after the delivery.

During the year 2012, Corporate Audit continued activities focused on identifying, evaluating, and addressing critical and material risks for the organization. Following are some of the most significant risks reviewed, as well as the actions initiated by management to mitigate them:

- Regulatory compliance: Some of the activities included the review and update of the governance programs, which included the Corruption of Foreign Public Officials Act (“**CFPOA**”), anti-money laundering training program, and the update of all regulatory obligations the Company has in different countries.
- Price and exchange rate volatility: The review was focused on hedging process and strategies, improving the automated environment to gain greater control of the Cash Flows at Risk.
- Potential increased of fraud risk: an updated fraud risk assessment was performed in the Q4 to identify fraud risks schemes related to asset misappropriation, corruption and financial fraud and included the launch of a e-learning employee fraud awareness training to help maintain fraud-resistance. The results were used to prioritize fraud detection efforts toward key current fraud risks, and review of segregation of duties controls and other fraud controls.
- Data security and privacy protection: The review was focused on the implementation of tools to protect the access to the network and the implementation of application security, the use of tools for continuous auditing and monitoring, and the strengthening of the IT control environment in accordance with the standards.
- Stakeholder relations: The Company has established a secure support and understanding among multiple stakeholders preparing and managing emerging issues.
- Security: The analysis and understanding of the security issues that has increased in different areas where the Company has operations initiated the implementation of programs to mitigate them.
- Replacement of proved oil and gas reserves: future oil and gas production will depend on Company ability to acquire, explore, and negotiate current contracts of new proved reserves.
- Operations are exposed to a wide range of health, safety, and environmental risks: the Company engaged with a zero tolerance HSE program. It is focused on training and monitoring activities to our own and contractor employees.
- Major project delivery: delivering complex projects face challenges requiring adequate engineering, environmental permits, skilled labour, and regulatory conditions among other risks. The Company continuously is improving its ability to manage these challenges strengthening project management standards.

16. Outlook

The Company will continue implementing its growth strategy, expanding its resource and reserve base and developing its production and transport capacity. Capital expenditures in 2013, estimated at of \$1.7 billion, are focused on: (1) increased development drilling and production facilities in Colombia and Peru; and (2) expanded exploration activity in Brazil, Peru, Guatemala, Papua New Guinea and Colombia.

Highlights for the 2013 program include:

- It is likely that 2013 production growth for Pacific Rubiales and other companies in Colombia will continue to be affected by the pace of environmental permitting approval. However, in an attempt to take a prudent and realistic view on this issue over which we have no control, we are starting the year by targeting 15 to 30% overall average production growth in 2013. The Company has a stronger than expected beginning to 2013 as we are currently

producing above plan at approximately 308 Mboe/d gross total field or 129 Mboe/d net after royalty (including the acquired C&C volumes), and we expect to be able to update the range as the year progresses

- Total capital expenditures of \$1,7 billion, an increase of approximately 30% over 2012 expenditures, largely driven by the expanded exploration activities outside Colombia and increased development drilling in Colombia and Peru. The capital program is expected to be funded by internally generated cash flow in an expected WTI oil price environment of \$85-\$90.
- Exploration expenditures of \$495 million, includes drilling an additional 35 gross exploration wells, seismic data acquisition and early facilities. In the total drill program, approximately 19 exploration wells are targeting high impact prospects, including the Company's first exploration wells in Peru, Brazil, Guatemala and Papua New Guinea.
- \$520 million drilling a planned 283 gross (excluding workovers and water injection wells) development wells, a significant increase over 2012, with activity driven by development of Cajua field, continued on-going infill drilling in the Quifa SW and Rubiales fields, stepped up light oil development in the Cubiro Block in Colombia and a significant program of development drilling on Block Z-1 in Peru.
- \$555 million in facilities and infrastructure, with approximately 85% directed to the Company's core producing Rubiales, Quifa SW, Cajua and Sabanero heavy oil fields and the remainder 15% for the planned development of the CPE-6 Block as well as other mostly light oil field development in Colombia.

17. Additional Financial Measures

This report contains the following financial terms that are not considered Measures under IFRS: operating netback, net adjusted net earnings from operations, funds flow from operations, adjusted earnings from operations and EBITDA. These non-IFRS Measures do not have any standardized meaning and therefore are unlikely to be compared to similar Measures presented by other companies. These non-IFRS financial Measures are included because management uses the information to analyze operating performance, leverage and liquidity. Therefore, these non-IFRS financial Measures should not be considered in isolation or as a substitute for Measures of performance prepared in accordance with IFRS.

a) Funds Flow

The following table shows the reconciliation of funds flow from operations to cash flow from operating activities for the year and three months ended December 31:

(in thousands of US\$)	Year Ended December		Three Months Ended December	
	2012	2011	2012	2011
Cash flow from operating activities	\$ 1,802,735	\$ 1,219,057	\$ 676,938	\$ 477,530
Changes in non-cash working capital	415,191	(149,542)	445,406	125,770
Funds flow from operations	\$ 1,387,544	\$ 1,368,599	\$ 231,532	\$ 351,760

b) EBITDA

A reconciliation of Net Earnings to EBITDA follows:

(in thousands of US\$)	Year Ended December		Three Months Ended December	
	2012	2011	2012	2011
Net earnings	\$ 527,729	\$ 554,336	\$ (23,777)	\$ 80,834
Adjustments to net earnings				
Income taxes expense	289,838	448,150	37,797	189,558
Foreign exchange (gain) loss	(577)	39,894	(13,421)	(1,947)
Finance cost	91,299	86,469	24,333	15,501
Incentive for early conversion of debenture	-	46,489	-	46,489
Gain on risk management contracts	(10,130)	(8,831)	13,663	46,458
Loss (gain) from equity investment	102,933	(6,829)	60,851	(5,059)
Other expense	30,897	13,207	21,382	8,369
Share-based compensation	32,902	48,783	853	316
Equity tax	-	68,446	-	-
Depletion, depreciation and amortization	851,444	656,912	233,332	174,086
Impairment of E&E Assets	102,060	12,066	74,028	12,066
EBITDA	\$ 2,018,395	\$ 1,959,092	\$ 429,041	\$ 566,671

c) Adjusted Earnings

Adjusted earnings from operations are a non-IFRS financial measure that represents net earnings adjusted for certain items of a non-operational nature including non-cash items. The Company evaluates its performance based on adjusted net earnings from operations. The reconciliation, "Adjusted Net Earnings from Operations", lists the effects of certain non-operational items that are included in the Company's financial results and may not be comparable to similar measures presented by other companies.

18. Sustainability Policies

The Company has established guidelines and management systems to comply with the laws and regulations of Colombia and other countries in which it operates, and beyond that to ensure sustainable development is one of the Company's priorities. In the past, the Company has engaged with its various stakeholders to ensure that as the Company grows, its consideration for the environment, its employees, and other stakeholders also continues. The Company devotes significant time and resources to achieve its environmental, social, transparency, human rights, and safety performance goals, among others.

The Company is committed to the promotion and respect of human rights in its operations, and with this in mind, the Company has initiated activities related to strengthen and align security process and systems with the key elements for managing potential human rights. The Company has also initiated human rights training for private security in Bogotá and its different fields around Colombia and has created a Gender Committee at a managerial level, responsible for leading the process of integrating a gender perspective in policies, programs, processes and systems of the Company, and implementing best practices.

In June 2011, the Company announced its support for the Extractive Industries Transparency Initiative (the "EITI"). The EITI is an international non-profit organization formed in 2002 at the World Summit for Sustainable Development in South Africa. The EITI supports improved governance in resource-rich countries through the verification and full publication of Company payments and government revenues from oil, gas and mining. Currently, more than fifty of the largest oil, gas and mining companies have chosen to become EITI supporting companies. Pacific Rubiales is the first Company in Colombia internationally committed to the EITI standards and is focusing efforts in taking a leading role in the implementation of EITI in Colombia by collaborating with all stakeholders within the EITI in Canada, which is an EITI supporting country, and Peru and Guatemala, which are EITI candidate countries, Pacific Rubiales is committed to actively supporting EITI processes.

With respect to how the Company manages the impacts of climate change, in 2012 Pacific Rubiales disclosed information in the Carbon Disclosure Project. Accordingly, Pacific Rubiales will integrate into its business strategy the need to document, control and eventually reduce carbon emissions.

In 2011, the Board of Directors appointed a Sustainability Committee to assist the Board of Directors in carrying out the

Company's corporate sustainability policies, including environmental, social, health, safety and ethical matters. This Committee is responsible for advising the Board of Directors, committees of the Board of Directors and executive management on such matters.

The Jantzi Social Index of the Canadian Stock Market added Pacific Rubiales Energy on September 24, 2012. The JSI, a socially screened, market capitalization-weighted common stock index modeled on the S&P/TSX 60 consists of 60 Canadian companies that pass a set of broadly based environmental, social, and governance rating criteria. This inclusion recognizes that the Company has demonstrated strong policies and management systems to mitigate the risks associated with operating in high-risk countries.

Pacific Rubiales became a signatory to the UN Global Compact in January 2011, is a founding member of a regional network supporting the Global Compact in Latin American and the Caribbean, and an active member of the Global Compact local network.

The Company has an integrated health, safety, environment, and quality management system which is certified to ISO 14001, ISO 9001, and OSHAS 18001 and has developed a management and monitoring program for atmospheric emissions and air quality.

Since September 24, 2012, the Company is also a component of the STOXX® Global ESG Leaders indices – an innovative series of environmental, social, and governance (ESG) equity indices that are based on a completely transparent selection process.

This index model allows investors to understand which factors determine a Company's ESG rating and why these factors are important.

In addition, on September 21, 2012, the Chartered Institute of Purchasing and Supply (CIPS) from the United Kingdom and a member of the Royal Charter, has awarded the Company with the Purchasing, Policies and Procedures (PPP) Certificate, after a professional evaluation and analysis on best practices and continuous improvement in the Supply Chain Management processes and procedures. PRE is now one of the 104 companies certified around the world in different industries; 16 of them in energy.

The Company was also recognized by World Finance as the "Best Oil & Gas Sustainable Company- Latin America 2012" because of its social, environmental and governance practices, and won the CSR and Sustainability Colombian Award which recognized the Company's sustainability model and its integration with the corporate strategy.

Finally, through the Social Investment Pioneer Awards, the Company received the Responsible Business award, a recognition for companies that commit to social, economic, and environmental sustainability while balancing the interests of diverse stakeholders, an initiative of the Principles for Social Investment Secretariat and United Nations Global Compact.

For further details regarding the Company's sustainability policies, please see our Sustainability Report, which is available on our website. The Sustainability Report for 2012 is expected to be ready by early May, 2013.

19. Legal Notice – Forward-Looking Information and Statements

Certain statements in this MD&A constitute forward-looking statements. Often, but not always, forward-looking statements use words or phrases such as: "expects", "does not expect" or "is expected", "anticipates" or "does not anticipate", "plans" or "planned", "estimates" or "estimated", "projects" or "projected", "forecasts" or "forecasted", "believes", "intends", "likely", "possible", "probable", "scheduled", "positioned", "goal", "objective" or state that certain actions, events or results "may", "could", "would", "might" or "will" be taken, occur or be achieved. Such forward-looking statements, including but not limited to statements with respect to anticipated levels of production, the estimated costs and timing of the Company's planned work programs and reserves determination involve known and unknown risks, uncertainties and other factors which may cause the actual levels of production, costs and results to be materially different from estimated levels of production, costs or results expressed or implied by such forward-looking statements. The Company believes the expectations reflected in these forward-looking statements are reasonable but no assurance can be given that these expectations will prove to be correct and such forward-looking statements should not be unduly relied upon. Factors that could cause actual results to differ materially from those anticipated in these forward-looking statements are described under the caption "Risks and Uncertainties". Although the Company has attempted to take into account important factors that could cause actual costs or operating results to differ materially, there may be other unforeseen factors to cause costs to the Company's program and results may not to be as anticipated, estimated or intended.

Statements concerning oil and gas reserve estimates may also be deemed to constitute forward-looking statements to the extent they involve estimates of the oil and gas that will be encountered if the property is developed. The estimated

values disclosed in this MD&A do not represent fair market value. The estimates of reserves and future net revenue for individual properties may not reflect the same confidence level as estimates of reserves and future net revenue for all properties, due to the effects of aggregation.

20. Risks and Uncertainties

The business operations and earnings of the Company could be impacted by the occurrence of risks of all kinds including financial, operational, technological and political, that might affect this Industry. Our Enterprise Risk Management program identifies, assess and provides action plans and controls to mitigate the occurrence of the risks described below, which can potentially affect businesses and hence the profitability and value of the shares of the Company.

The business and operations of the Company will be subject to a number of risks. The Company considers the risks set out below to be the most significant to potential investors in the Company, but does not include all of the risks associated with an investment in securities of the Company:

- Fluctuating oil and gas prices;
- Global financial conditions;
- Exploration and development;
- Operating hazards and risks;
- Security risks;
- Reserves estimates;
- Transportation costs;
- Cash flows and additional funding requirements;
- Disruptions in production;
- Political risk;
- Environmental factors;
- Title matters;
- Payment of dividends;
- Dependence on management;
- Ability to attract and retain qualified personnel;
- Changes in legislation;
- Litigation
- Repatriation of earnings;
- Enforcement of civil liabilities;
- Competition;
- Environmental licenses & required permits;
- Partner relationship;
- Oil & gas transportation;
- Availability of diluents;
- Water disposal;
- Labor relations;
- HSE works;
- Community relations;
- Fraud;
- Foreign exchange rate fluctuation;
- Business continuity;
- Regulatory compliance; and
- Shareholder relations.

If any of these risks materialize into actual events or circumstances or other possible additional risks and uncertainties of which the Company is currently unaware or which it considers not to be material in relation to the Company's business, actually occur, the Company's assets, liabilities, financial condition, results of operations (including future results of operations), business and business prospects, are likely to be materially and adversely affected. In such circumstances, the price of the Company's securities could decline and investors may lose all or part of their investment. For more information, please see the Company's Annual Information Form which is available at www.sedar.com.

21. Advisories

Finding Costs

The aggregate of the finding costs incurred in the most recent financial year and the change during that year in estimated future finding costs generally will not reflect total finding costs related to reserves additions for that year.

Boe Conversion

The term "boe" is used in this MD&A. Boe may be misleading, particularly if used in isolation. A boe conversion ratio of cubic feet to barrels is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. In this MD&A we have expressed boe using the Colombian conversion standard of 5.7 Mcf: 1 bbl required by the Colombian Ministry of Mines and Energy.

All of the Company's natural gas reserves are contained in the La Creciente, Guama and other bocks in Colombia as well as in the Piedra Redonda field in Block Z-1, Peru. For all natural gas reserves in Colombia, boe's have been expressed using the Colombian conversion standard of 5.7 Mcf: 1 bbl required by the Colombian Ministry of Mines and Energy. For all natural gas reserves in Peru, boe's have been expressed using the Canadian conversion standard of 6.0 Mcf: 1 bbl. If a conversion standard of 6.0 Mcf: 1 bbl was used for all of the Company's natural gas reserves, this would result in a reduction in the Company's net 1P and 2P reserves of approximately 4.2 and 4.7 MMBoe respectively.

Prospective Resources

Readers should give attention to the estimates of individual classes of resources and appreciate the differing probabilities of recovery associated with each class. Estimates of remaining recoverable resources (unrisked) include prospective resources that have not been adjusted for risk based on the chance of discovery or the chance of development and contingent resources that have not been adjusted for risk based on the chance of development. It is not an estimate of volumes that may be recovered. Actual recovery is likely to be less and may be substantially less or zero.

Prospective Resources are those quantities of petroleum estimated, as of a given date, to be potentially recoverable from undiscovered accumulations by application of future development projects. Prospective Resources have both an associated chance of discovery and a chance of development. Prospective Resources are further subdivided in accordance with the level of certainty associated with recoverable estimates, assuming their discovery and development, and may be sub-classified based on project maturity. There is no certainty that any portion of the resources will be discovered. If discovered, and they would be technically and economically viable to recover; there is no certainty that the Prospective Resource will be discovered. If discovered, there is no certainty that any discovery will be technically or economically viable to produce any portion of the resources.

Translations

This MD&A was prepared originally in the English language and subsequently translated into Spanish and Portuguese. In the case of any differences between the English version and its translated versions, the English document shall prevail and be treated as the governing version.

22. Abbreviations

The following list of abbreviations is used in this document

1P	Proved reserves (also known as P90).	MMcf/d	Million cubic feet per day
2P	Proved reserves + Probable reserves.	MD	Measured depth
3P	Proved reserves + Probable reserves + Possible reserves.	MMbbl	Million barrels
Bbl	Barrels	Mmboe	Million barrels of oil equivalent
bbl/d	Barrels per day	MMBtu	Million British thermal units
Bcf	Billion cubic feet	MMcf	Million cubic feet
boe	Barrels of oil equivalent	MMcf/d	Million cubic feet per day
boe/d	Barrels of oil equivalent per day	Mmscf/d	Million standard cubic feet per day
Btu	British thermal units	Mw	Megawatts
Bwpd	Barrels of water per day	NGL	Natural gas liquids
CBM	Cubic Billion Meter	OOIP	Original oil in place
ESP	Electro-Submersible Pump	Tcf	Trillion cubic feet
GDP	Gross Domestic Product	TD	Total depth
km	Kilometers	TVDSS	True vertical depth below sea level
KWh	Kilowatt Hour	USGC	US Gulf Coast
Mbbl	Thousand barrels	WTI	West Texas Intermediate index
Mboe	Thousand barrels of oil equivalent		