Registered No 5562373

# FAIRFIELD ENERGY LIMITED

# CONSOLIDATED FINANCIAL STATEMENTS

# 31 DECEMBER 2009

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## Finance report



## Corporate information



Information about this report

This document constitutes the Annual Report and Accounts of Fairfield Energy Limited for the year ended 31 December 2009 in accordance with UK requirements and is dated 4 June 2010 The Annual Report and Accounts for the year ended 31 December 2009 contains the Directors' Report which consists of the business performance and governance reports on pages 3 to 11 The consolidated financial statements are on pages 14 to 40 and Company financial statements are on pages 43 to 54 The report of the auditor is on page 13 for the Group and page 42 for the Company

# Chairman's and Chief Executive's review

The Fairfield Group (Fairfield) has continued to make good progress during 2009 in the development of its North Sea business towards the goal of becoming the significant UK independent operator The Company completed its first full year as owner of the Dunlin Area Fields in the northern North Sea, ably supported by AMEC as Duty Holder Additional acreage was acquired from the majors and through the 25th Licencing Round while progress was made towards first oil and gas on all the other assets (except Maureen) in the portfolio

The oil price has recovered from $35/bbl at the end of 2008 to a closing price of $78/bbl The stronger oil price is a result of supply side discipline on the part of OPEC, coupled with continuing strong demand from non-OECD countries, particularly China Leading forecasters predict higher oil prices in 2010 and 2011 as the global economy comes out of recession In addition to the external environment, other revenues have been well supported by derivative financial instruments taken out in mid-2008 These instruments will continue to provide revenues in the event oil prices remain at current levels

The Dunlin Area Fields remain the only revenue producing assets, averaging 4,618 (YTD) net barrels per day The total sales entitlement volume for the year was 1 662 million barrels Two wells on the Osprey Field, drilled by the Sedco 704 rig, encountered unswept oil which has been put on production The Dunlin platform rig was totally refurbished ahead of an intensive drilling program on the main field planned for this year Finally, the Duty Holder relationship with AMEC has continued to mature and develop, providing a sound basis for operational confidence

Substantial progress has been made on all of Fairfield's other assets Static and dynamic models for both the Triassic and Tertiary reservoirs in the Crawford Field support revised oil-in-place and reserve estimates Development studies, with export through Marathon's East Brae facilities, are well advanced and an FDP will likely be submitted this year with first oil estimated for 2011 Half of Clipper South was farmed down to RWE Dea SNS UK Limited in July 2009 with the transfer of operatorship Commercial and technical work completed by the new partnership mean that an FDP will likely be submitted in 2010 with first gas estimated for 2012

The Core Area approach was fully implemented in 2009 with the acquisition of the Skye/Block 6 discoveries just to the west of Dunlin and exploration acreage to the east of Dunlin awarded in the 25th Round Further additions to the portfolio included the 25th Round Block 3/8d over the Staffa Field Originally developed by LASMO in 1992, the field produced only 4mmbo with production ceasing in 1994 Fairfield plans to proceed with the re-development by a single well subsea development tied-back to one of a number of nearby suitable host platforms The 25th Round Block 211/27e was also added to the portfolio along with the acquisition from BP and partners of two licences (P 184 and P 474) over the abandoned North West Hutton Field Based on detailed technical work, Fairfield believes there are substantial undeveloped volumes to the south of the old field Further detailed subsurface evaluation based on new 3D seismic this year and a programme of appraisal in 2011 will likely lead to a phased, sub-sea development tied back to Dunlin

Finally the Maureen acreage was farmed down to Endeavour Energy UK Ltd and Challenger Minerals Ltd in July 2009 The 16/29a-17 well was then drilled with much of Fairfield's share funded through an advance agreement with Gemini Oil and Gas Ltd Unfortunately the well was dry and the current licence owners are reviewing future options As a result of this and the uncertainty about future plans for Maureen, the Company has considered the asset to be impaired and has written off the carrying value accordingly

In 2010, the Company will continue to look at the most appropriate mechanisms of funding the development of its assets There remain a number of options available to the Company including existing SPC funding, raising debt and potentially taking the Company public via an Initial Public Offering

Fairfield commissioned an independent reserves report from Gaffney Cline and Associates for the Dunlin Area in mid-2009 and then a full review of the portfolio at the end of 2009

The HSE subcommittee of the Board met four times during the year to review the Company's standards, policies and procedures and overall performance in this critical area We are happy to report that there were no Lost Time Injuries in 2009 Three corporate level HSE audits were completed including a review of the arrangements for contracting and managing subsea intervention activities, a review of the HSE management interface between Fairfield and AMEC on the Dunlin asset and a review of pre-drilling assurance plans for the platform

Changes to the Non-Executive Directors on the Board saw the addition of Andrew Paterson in December 2008 while Fred Ponsonby resigned in July 2009 Fred has been with Fairfield throughout its evolution and we thank him for his input and commitment to making the Company as successful as possible Andrew has made an immediate impact on the Company, drawing on his extensive drilling and operational experience

As always the progress that the Company has made in 2009 is totally due to the efforts and commitment of the staff We appreciate their hard work and energy in delivering their individual and the corporate objectives for the year

# Business review

### *Health, safety and environment (HSE)*

Fairfield's health, safety and environmental policies set out a commitment to conduct our business in a manner that protects people from harm and preserves the environment Key actions from these policies include

- Maintaining an Environmental Management System certificated to the ISO 14001 standard,
- Prescribing annual performance targets and reporting regularly on those targets to the Board HSE subcommittee,
- Assessing HSE risks in the planning and execution of all operational activities,
- Ensuring the availability of specialist support and providing advice to the Executive and the Board, and
- Establishing responsibilities for HSE performance within the organisation

The Dunlin offshore installation is operated through AMEC as Duty Holder, appointed in accordance with the Safety Case Regulations

**Performance in 2009**

There were no Lost Time Injuries (LTI) recorded in 2009, a period that included more than six months mobile rig drilling operations and almost two months of diving support vessel operations, in addition to the continuous operation and maintenance of the Dunlin facilities

AMEC, as Duty Holder, conducted a Thorough Review of the Safety Case in accordance with Regulation 13 of the Safety Case Regulations An addendum to the Safety Case was also accepted by the Health and Safety Executive to enable platform based drilling operations, following a campaign to refurbish the drilling facilities

In February, the Department of Energy and Climate Change (DECC) investigated a reported spillage to sea of 3 3 tonnes of diesel during bunkering operations on the Dunlin installation

An emergency exercise, involving response to a simulated incident on the Dunlin installation, was successfully carried out during May involving response teams from Fairfield, AMEC and drilling services contractors

Three corporate HSE audits were carried out during 2009

- A review of the arrangements for contracting and managing subsea intervention activities,
- A review of the HSE management interface between Fairfield and AMEC on Dunlin, and
- A review of the pre-drilling assurance plans for the Dunlin installation

Variation Applications to the Pollution Prevention and Control (PPC) and Oil Pollution Prevention and Control (OPPC) certifications, following transfer to Fairfield of the Dunlin Installation from the previous owners and providing certification for 2009, were both successfully concluded and accepted by DECC

In February, Fairfield's appointed Verification Body, Det Norske Veritas (DNV), verified compliance of the Dunlin installation with the requirements of the European Union Emissions Trading Scheme for 2008

In accordance with the requirements of the Oslo-Paris Convention for the Protection of the Marine Environment of the North East Atlantic, an annual public statement on Fairfield's environmental performance for the year 2008 was submitted to DECC and published on the Company's website during June 2009

Two audits were carried out by DNV successfully confirming continued certification to the Environmental Management Standard ISO 14001

In July, the HSE served the Dunlin Duty Holder (AMEC) with two improvement notices following an inspection of fabric corrosion maintenance The first notice, requiring improved specification of maintenance criteria for fabric corrosion, was satisfactorily discharged in November 2009 The second notice, requiring enhancements to the planning process, was formally discharged by the end of March 2010

**Focus for 2010**

Asset integrity, environmental emissions monitoring and regulatory compliance tracking are the main focus for 2010

Providing assurance of asset integrity is a key element in the effective management of major hazards that are inherent in the process safety elements of oil and gas production This is particularly important on offshore production facilities in the late stage of their operating life cycle A major part of our asset integrity assurance will be an audit of the processes by which the Dunlin Safety Case is actively maintained by AMEC

Environmental emissions monitoring, and associated continuing improvement, is a key part of our long term environmental management strategy for the Dunlin facilities The emissions management programmes are also crucial to the ongoing maintenance of our ISO 14001 certification

Regulatory compliance tracking includes the development of systems and behaviours that ensure effective maintenance of the necessary certificates and permits that collectively provide our 'licence to operate' This will include promoting the awareness of crucial environmental certification conditions, the reporting of non-conformances, and providing periodic compliance and commitments reporting for management

### *Review of assets*

**Dunlin**

The Dunlin Area fields averaged 4,618 bopd of net production during 2009 while total water injection averaged 64,000 bwpd

Two successful subsea wells were drilled by the Sedco 704 drilling rig on the Osprey field, both encountering unswept oil The wells were successfully hooked up at the end of the planned 2009 shutdown The refurbishment of the Dunlin drilling rig was completed and drilling commenced on the first platform well An extensive inspection, repair and maintenance campaign was successfully completed on the subsea infrastructure, rectifying faults on the subsea control system and completing the hook up of the new Osprey production wells A programme of subsea intelligent pigging operations on the Osprey and Merlin lines was also completed as part of this campaign to gather data for extensions to the operating lives of these facilities

During the first half of 2010, a review of the Dunlin Area decommissioning liabilities is being carried out in accordance with the decommissioning cost provision deed (DCPD) held with the former owners of the Dunlin Area Assets While this review will not be finalised until the end of June 2010, the Company has agreed to provide an additional cash security of $77 million in addition to the existing $273 million security held by way of a letter of credit

**Staffa Field**
Licence P1607, Block 3/8d including the Staffa Field was awarded to Fairfield Cedrus Limited, with a one well drilling commitment, in the 25th Licensing Round announced on 12th November 2008 Originally developed by LASMO in 1992, the field produced only 4mmbo before pipeline blockages caused production to be ceased in 1994 Fairfield's detailed technical assessment has focused on understanding the fundamental causes for these flow assurance issues and on quantifying the redevelopment potential Fairfield plans to proceed with the redevelopment of Staffa via a single well subsea tie-back to one of a number of nearby suitable host platforms Commercial and technical discussions have commenced with potential host operators

**Crawford Field**
Fairfield Acer Limited (Operator) owns 52% of Licence P209 Block 9/28a which includes the Crawford Field Its partners are Valiant Exploration Ltd (29%) and Stratic Energy (UK) Ltd (19%) In Licence P1284, Block 9/27a, adjacent to the west, Fairfield Acer Limited (Operator) owns 25% with EnCore Petroleum Ltd (62 5%) and Granby Enterprises North Sea Ltd (Silverstone Energy) (12 5%)

During 2009, the reprocessed 3D seismic over Blocks 9/28a and 9/27a was used to update the mapping of the Tertiary and Triassic oil bearing reservoirs The updated static and dynamic Triassic reservoir models and a new static Tertiary reservoir model support revised oil-in-place, reserves and production forecasts for the Crawford Field A comprehensive geological and geophysical review has also resulted in the definition and documentation of a Tertiary prospect inventory across both blocks

The development of the Triassic reservoir will be through up to three production wells enhanced with multiple hydraulic factures or multi-lateral sidetracks A study programme to identify the preferred completion strategy is scheduled to be finished by the end of the first quarter of 2010

Studies and commercial arrangements for the facilities development via subsea tieback to Marathon's East Brae platform are also at a high degree of completion Engineering studies have confirmed the feasibility of this option Drilling will be by means of a jack-up rig which will also be used as a base for exporting oil and gas during the early years of production

A final development concept decision will be made during 2010

**Clipper South**
On 13th May 2009 Fairfield Acer Limited signed a farm in agreement with RWE Dea UK SNS Ltd (RWE) Under the terms of the agreement RWE carries Fairfield for certain development costs and paid a proportion of historic costs from the effective date of 1 July 2008 In return RWE earns operatorship and a 50% interest in the Clipper South Potential Producing Area which comprises Licence P008 (part Blocks 48/19a and 48/20a) and Licence P465 (Block 48/19c) Completion of this transaction occurred on 3rd July 2009

Following its assumption of operatorship, RWE has continued to refine the subsurface understanding and has revised the static and dynamic models of this Rotliegendes tight gas accumulation leading to increased gas-in-place volumes The preferred subsurface development concept envisages five horizontal multi-fractured wells produced through a wellhead platform

Engineering studies to define the field development concept to Front End Engineering Design level were continued in 2009 by Genesis Engineering The initial base case concept of a normally unmanned installation was amended to include accommodation for up to forty persons during the development drilling phase, when hydraulic fracturing and subsequent clean-up through coiled tubing will require a greater presence of personnel offshore This concept is also advantageous as it allows subsequent rig-less intervention during life of field operations This work was completed at the end of November 2009 and formed the basis of an invitation to tender for the detailed design and construction of the platform in December

It is envisaged that the produced gas will be exported via adjacent host infrastructure Detailed negotiations with the owners have continued through 2009 and firm offers for services received in November 2009 from two hosts are under evaluation

A draft Field Development Plan has been prepared by RWE for submission to DECC in 2010 Following discussions with DECC, P008 Blocks 48/19a and 48/20a are now classified as a Potential Producing Area and a licence extension to September 2012 has been agreed

**Darwin**
Block 211/27e was awarded to Fairfield Cedrus Limited, with a one well drilling commitment, in the 25th Licensing Round announced on 12 November 2008 In late 2009 agreements were signed to allow Fairfield to acquire 100% of the North West Hutton (NWH) interests in Licence P 184, Block 211/27a and Licence P474, Block 211/27c from the previous owners Amoco (U K ) Exploration Company, Amoco U K Petroleum Limited, Cieco Exploration and Production (UK) Limited, Enterprise Oil U K Limited and Mobil North Sea LLC

Based on detailed technical work completed over the past three years, Fairfield considers this combined acreage to be an undeveloped southern extension of the NWH Field New 3D seismic acquisition was completed in 2009 and has reinforced this understanding The prospective area has been provisionally called Darwin pending DECC approval

Development studies for the Darwin Area are underway and development options include a subsea tie-back to Fairfield's Dunlin platform (24km away) Engineering studies for the Dunlin tieback and modifications are well advanced A phased development concept is likely with phase 1 concentrating upon accessing proven but undeveloped oil in the southern part of NWH These areas were beyond the achievable drilling radius of the decommissioned platform Phase 2 would target further infill locations in NWH plus prospective volumes in the southern part of the Darwin area

**Skye & Block 6**
In 2009 Fairfield added further acreage in the Dunlin Area by completing an acquisition of the Skye/Block 6 area from Shell and Exxon (Licence P296 Block 211/23a) This acreage includes two discoveries and a number of prospects and leads In addition, an exploration area to the east of Dunlin (Licence P1681 Block 211/24c) was acquired in the 25th Licensing round

**Maureen**
At the beginning of the year Fairfield Cedrus Limited owned and operated 100% of Licence P110 Block 16/29a (Maureen field) and 81 14% of Licence 591 Blocks 16/24b and 16/29b In July 2009 Fairfield Cedrus Ltd signed a farm in agreement with Endeavour Energy UK Ltd and Challenger Minerals Ltd whereby both agreed to disproportionately fund Fairfield's share of Well 16/29a-17 Further funding was provided through an advance agreement with Gemini Oil and Gas Ltd

Well 16/29a-17 was drilled in August 2009 to a Palaeocene reservoir target within the boundaries of the Maureen Field The reservoir did not contain commercial hydrocarbons at the drilled location and the well was plugged and abandoned Following the drilling of the well, Challenger decided not to take up its working interest in December with Endeavour earning a 38 46% working interest in P110 and P591 and Fairfield retaining 61 54%

***Oil and gas reserves***

Oil and gas reserves (mmboe)

| | Proved | Proved and Probable |
|---|---|---|
| **2008** | | |
| Dunlin Area | 33 5 | 43 6 |
| Clipper South | 26 0 | 37 5 |
| Crawford | 8 7 | 13 5 |
| **2008 TOTAL** | **68 2** | **94 6** |
| **2009** | | |
| Dunlin Area | 16 1 | 33 3 |
| Darwin | 17 3 | 29 0 |
| Clipper South | - | 10 7 |
| Crawford | 9 3 | 14 3 |
| Staffa | 3 1 | 6 1 |
| **2009 TOTAL** | **45 8** | **93.4** |

At 31st December 2009 the Group's share of Proved and Probable Reserves were determined by an independent expert, Gaffney Cline and Associates (GCA) in accordance with the definition of proven and probable reserves provided by the Society of Petroleum Engineers (SPE-PRMS) Reserve quantities in 2008 were estimated by the Group's petroleum engineers in accordance with the same rules A summary of the Company's reserve position relative to 2008 is set out in the tables above

**Dunlin Area**
Based on our experience of power supply reliability from Brent in 2009, both GCA and Fairfield engineers have taken a more conservative view of water injection volumes in the short term which reduces the production forecast This has had a proportionately larger impact on Proven Reserves Fairfield plans to import fuel gas from late 2011, making Dunlin self-sufficient in power generation and removing the unreliability of Brent power supply

Fairfield engineers and GCA agreed to build the benefits of this development in over several years rather than include an immediate impact which had been the previous assumption GCA takes a more conservative view than Fairfield engineers on the reserves developed from the Dunlin platform drilling programme, especially in the case of Proven Reserves Reserves are now included for the development of the Skye discovery following a work programme of geoscience and reservoir simulation

**Clipper South**
The 2008 Reserves were subject to independent audit by RPS Energy and were based on the 100% equity which Fairfield held at the time During 2009, 50% was farmed down to RWE in return for a partial development carry

RWE has taken over Operatorship of Clipper South and completed its own reserves evaluation and a revised development plan based on 5 production wells rather then the 6 wells in the Fairfield plan Reserves per well are similar in the RWE and Fairfield estimates

GCA has taken a more conservative view of the effectiveness of the frac programme than Fairfield, RPS or RWE

**Crawford**
Crawford has seen a small increase in reserves This is due to improvements in the development plan arising from the 2009 work programme The significant change is moving from hydraulic fracturing to multilateral drilling in order to maximize reservoir contact with the well bore This approach, combined with more definition on costs has improved the economic duration of the development

**Darwin**
Darwin is the provisional name for the development of the southern end of the North West Hutton field acquired from BP and the UKCS 25th Round acreage to the south of the field, both acquired in 2009 During 2009 an extensive subsurface work programme was completed and a Draft Field Development Plan written resulting in the assignation of reserves to the first phase of development by GCA

**Staffa**
The 2009 work programme on Staffa has generated a much improved knowledge of the subsurface expectations of the redevelopment, and as a result GCA has assigned Reserves to the development

# Financial review

The past year was an important period in the development of the Company with 2009 being the first full year managing Fairfield's producing assets following the acquisition of the Dunlin Area in April 2008. As well as significant progress being made with the Dunlin assets, a number of our evaluation assets took significant steps towards first gas and oil. Although operating performance did not reach internal targets with constraints to production, revenues have been well supported by treasury decisions taken in mid-2008 and will continue to provide revenues over the next 12 months should oil prices remain at current levels.

Over the past twelve months, the oil price has risen significantly, beginning the year near $35/bbl and closing around $78/bbl. The increased price reflects improved fundamentals with supply side discipline from OPEC and a continuation of strong demand from non-OECD countries such as China. Leading forecasters indicate oil prices will continue to increase over 2010 and 2011 as the global economy recovers. The pound strengthened against the US Dollar during 2009, moving from $1.4454 to $1.6135. The weakening dollar had a negative impact on results as revenues are generated in dollars, whilst costs are predominantly sterling denominated.

**Operating performance**

The Company generated earnings before interest and tax (EBIT) of $25 million in 2009 compared to $26 million in 2008. This result was impacted by higher operating costs associated with the initial running of the Dunlin 'A' platform, an extended shutdown period and the effect of the weaker US dollar. Production costs were $55/bbl.

Our swap and put-option contracts with a fixed weighted-average oil price of $116/bbl covered 99% of our production for the year and generated strong operating revenues despite oil prices beginning the year in the $30s. We have reported hedging revenues of $64 million but this amount excludes $28 million from our ineffective put options flowing through the fair value gain and loss on derivatives in the Income Statement. Total hedging revenues received for the year totalled $92 million. Additional detail relating to financial instruments is disclosed in Note 17 to the Consolidated Financial Statements.

Overhead costs were successfully managed to below 2008 levels in spite of the currency pressures and additional professional services and consultancy fees incurred during the year. The focus on strong cost control will continue and has been supported by the implementation of a new accounting system over the early months of 2010.

Over the course of the year, the Company has been actively managing the asset portfolio and as a result there have been several non-recurring revenues and expenses. In March the Mabel asset was sold to BP for $3.5 million generating a gain on sale of $2.9 million.

In July, Fairfield successfully farmed-out a 50% interest in Clipper South to RWE in exchange for a carried interest of on-going costs capped at £20 million as well as the reimbursement of £3 million of historical costs. As a result, our share of the incurred expenditure up to the cap will remain off our statement of financial position.

In July, Fairfield entered into a joint venture partially divesting our interests in the Maureen Area to Challenger Minerals and Endeavour Energy.

**Key Performance Indicators**

| Area | Target | 2009 | 2008 |
|---|---|---|---|
| HSE | LTIFR per 200,000 hrs | 0.0 | 0.83 |
| Operational | Net production | 1.7m | 1.1m |
| Financial | Cash operating cost per boe | $55 | $44 |

Over the following months, an appraisal well was unsuccessfully drilled in North East Maureen and was plugged and abandoned. A subsequent review of this asset has resulted in the decision to fully impair the carrying value of the Maureen Area. As a consequence, total net exploration and impairment write-offs of $14 million have been recorded with $7.2 million directly related to the North East Maureen drilling. Fairfield's capital outlay, however, was limited to $1 million with offsetting income received from an advance agreement entered into with the Gemini Oil and Gas fund in exchange for a royalty interest in future production. Gemini carried the risk of a dry-well.

**Net finance costs**

The Company is well funded, principally supported by a group of private equity companies who have contributed $300 million. Debt financing was provided by subsidiaries of Mitsubishi Corporation, to support the Dunlin acquisition in 2008 in the amount of $92 million. The private equity funding is quasi-equity but based on certain features has been classified as debt (Subordinated Preference Certificates and Preference Shares) for the purpose of IFRS reporting. Our funding sources have resulted in finance charges of $70 million for 2009, up from $41 million in 2008, as a result of the additional draw down of SPC funding and an $18 million charge resulting from an earlier anticipated conversion date associated with an Initial Public Offering. In the current year we have also incurred net fair value losses on derivatives of $28 million due to the increase in the oil price over the past year.

**Operating cash flows**

The Group generated operating cash flows of $79 million before investing and financing activities, up 371% from the $17 million generated in 2008.

**Investing and financing activities, net debt**

The Company invested $182 million in net capital activities in 2009, principally supporting the Dunlin Area with an investment of $149 million and expenditure of $34 million on our evaluation assets. Of the evaluation spend, $19 million related to the acquisition of the North West Hutton asset acquired in September 2009. A further $6 million is payable in future payments, with approximately $2 million payable in July 2010 and the remainder expected in the last quarter of 2011.

2009 saw a net financing inflow of $82 million (2008: $162 million) with Mitsubishi financing obtained in the latter period to fund the Dunlin acquisition. The 2009 inflow was generated principally from $100 million in investor cash calls offset by a $4 million reduction in the revolving credit facility to Mitsubishi Corporation and $14 million paid in interest and guarantee fees associated with all debt facilities.

Net debt was relatively consistent at $59 million at the end of the year compared to $40 million twelve months earlier.

During the course of the year, the Company has continued to look at funding alternatives to develop our assets. This process will continue in 2010, including evaluating an option to take the Company to the market.

# Corporate governance

The Board is committed to the highest standards of corporate governance and believes that such standards are essential to overall business integrity and performance As a private company the Company is not required to comply with the principles of the Combined Code on Corporate Governance, however, the Board has taken steps such that, where appropriate, the Company complies with aspects of the Combined Code

| Board of Directors | Private equity house |
|---|---|
| Christopher Alan Wright | Not applicable |
| Mark Francis McAllister | Not applicable |
| Simon William Caines Eyers* | 4D |
| Peter Kagan* | Warbug Pincus |
| David Krieger* | Warbug Pincus |
| David L Pearce* | Not applicable |
| Jeff van Steenbergen* | Kern Energy |
| Andrew Paterson* | Not applicable |
| Frederick Ponsonby* (resigned 31/7/09) | Not applicable |

* denotes Non-Executive Directors

The powers of the Directors are set out in the Company's Articles of Association (Articles) The roles of Chairman and Chief Executive are separate

**Board meetings**

The Board holds regular scheduled meetings throughout the year Unscheduled supplementary meetings also take place as and when necessary During 2009, the Company had four scheduled meetings and two unscheduled supplementary meetings The Board continually monitors the development of the Group's strategy and associated business plans and budgets Performance is reported through monthly reports and at scheduled meetings while the annual business plan and budget are discussed, reviewed and approved at the December meeting

Directors who were unable to attend specific Board or committee meetings reviewed the relevant Board briefing packs and provided their comments to the Chairman of the Board or committee, as appropriate

**Directors' indemnities and insurance**

In accordance with the Articles, the Company has granted a deed of indemnity, to the extent permitted by law, to each Director and officer of the Company The Company also maintains directors' and officers' liability insurance

**Board committees**

The Board has delegated authority to its committees to carry out certain tasks as defined in each committee's respective terms of reference

All of the Non-Executive Directors serve on one or more of the Audit, Remuneration and HSE Committees Minutes of committee meetings are made available to all Directors on a timely basis and the chairmen of each committee provide updates to the Board at subsequent Board meetings

**Audit Committee**

The members of the Audit Committee are Simon Eyers (Chairman, replacing Fred Ponsonby who resigned as a Director during 2009), David Pearce, David Krieger and Jeff van Steenbergen The key function of the Audit Committee is to review the effectiveness of the Company's financial reporting and internal control policies together with the procedures for the identification, assessment and reporting of risks The Committee is authorised by the Board to

- Monitor the integrity of the Company's financial statements, including a review of the significant financial reporting judgments contained therein,
- Review the Company's internal financial controls, internal control and risk management systems, and
- Establish and oversee the Company's relationship with the external auditors, including monitoring their independent status

During the year the Committee met on four occasions The Committee has met privately with the external auditors during the course of these meetings

In accordance with International Standard on Auditing (UK & Ireland) 260 and Ethical Statement 1 issued by the Accounting Practices Board, and as a matter of best practice, the external auditors have confirmed their independence as auditors of the Company, in a letter addressed to the Directors

**Remuneration Committee**

The members of the Remuneration Committee are Peter Kagan (Chairman), David Pearce, Simon Eyers and Andrew Paterson Fred Ponsonby stood down from the Committee in 2009 Andrew Paterson is considered independent (as was Lord Ponsonby), the other members of the committee are all investor directors The Remuneration Committee is responsible for determining the remuneration of the executive directors and senior employees and normally meets twice a year

The Committee acts within the agreed terms of reference in implementing the remuneration policy The remit of the Committee includes

- Determination and agreement of the remuneration policy for executive directors and senior employees,
- Consideration and determination of total compensation for executive directors and senior employees in accordance with the remuneration policy,
- Approval of the principles of, and the targets contained within, the Company's annual bonus plan,
- Approval of the design and structure of the Company's long-term incentive plan and the corresponding awards to be made in accordance with the plan, and
- Determination of the remainder of the remuneration package including pension arrangements and other non-cash benefits for executive directors and senior employees

The Remuneration Committee met once in 2009 to review the 2009 Corporate Performance Contract, to review and approve the revised 2009 basic salary provisions for all staff, to review and approve the 2008 performance bonus award recommendations for all staff and to approve benefits enhancements for all staff During the course of the year the Committee was kept regularly informed by Executive Management on matters including organisational development, senior employee performance and organisational capacity It was asked to approve, out of committee, a mid-year share options award to staff

**Health, Safety and Environment (HSE) Committee**

The members of the HSE Committee are David Pearce (Chairman), David Krieger and Simon Eyers Members of the committee are all investor directors

The key purpose of the HSE Committee is based upon *Leadership Actions For Directors & Board Members* Guidance issued by the Institute of Directors and CBI on 29th October 2007, and is specifically enhanced in order to make reference to the management of asset integrity and major hazard risk management Its charter is to,

- Examine whether the health, safety and environmental policies reflect Fairfield's current priorities, plans and targets,
- Examine whether asset integrity, major hazard risk management and other health, safety and

environmental management systems have been effectively reported to the board,

- Report health, safety and environmental shortcomings, and the effect of all relevant board and management decisions,
- Decide actions to address any weaknesses and a system to monitor their implementation,
- Consider immediate reviews in the light of major shortcomings or events

During 2009 there were four meetings where the key topics discussed were

- The Dunlin Safety Case – Review & Revision (status) and Drilling Addendum (status)
- Dunlin Critical Documentation Review Plan (status)
- Asset Integrity Management (Status)
- The Role and Reports of the Verification Body
- The status of environmental incidents
- A review of the 2009 Corporate KPIs and Targets
- Regular review of the Corporate Risk Register
- A review of the Dunlin Flare Header incident of 10 April
- A review of the Dunlin 'Safety Culture'
- A review of the Dunlin Enforcement Notices issued by Regulatory Authorities

In addition, the Committee also considered the organisational development of the Fairfield professional HSE function, and reported regularly to the Board, including an annual HSE Performance Report and a report on the development of Corporate KPIs for HSE

**Risk management and internal control**

The Board regards the identification and assessment of risks, together with the mitigating internal controls, to be fundamental to achieving the Group's strategic objectives The Board has overall responsibility for the Group's system of internal control and risk management which is designed to manage rather than eliminate the risk of failure to achieve its objectives and can provide only reasonable, and not absolute, assurance against material misstatement or loss As part of the management process the Group has identified the key risks facing the Group and those risks with a high level of potential impact and occurrence are summarised in the Risk Register which is reviewed by the Board on a quarterly basis

Fairfield, as an appraiser, developer and operator in the North Sea oil and gas industry faces a variety of risks The nature of these risks may be strategic, operational and/or financial Many of these risks are outside the Group's control Key risks the Group faces include those set out in the table below

**Strategic risks**

| Risk | Description and mitigation strategy |
|---|---|
| Reserve replacement | Future oil and gas production is dependent on identifying and obtaining rights to new reserves and bringing those reserves into oil and gas production The Group mitigates the depletion of existing reserves by developing existing exploration and evaluations assets and assessing opportunities in the market to acquire new rights as they arise via license rounds and merger and acquisition activity |
| Geographical area | Fairfield is a North Sea specialist focused on understanding the subsurface of identified hydrocarbon resources better than its competitors The Group is subject to the political, regulatory and environmental risks related to this area |
| Human resources | Fairfield recognises that future success requires it to retain, develop and attract highly skilled personnel To meet this objective, the Group<br>• Assesses its remuneration packages against external benchmarks,<br>• Offers an employee share option plan, and<br>• Provides annual and spot bonuses following the achievement of individual performance contracts and/or excellent performance |

**Operational risks**

| Risk | Description and mitigation strategy |
|---|---|
| Production | Existing production flows entirely through the Dunlin Area assets via the Brent System and is exported from Sullom Voe Terminal As all production is processed from one platform, oil revenues would cease immediately should a catastrophic disaster occur to the infrastructure of the Dunlin area To mitigate this risk, Fairfield has obtained business interruption insurance and seeks opportunities to add additional production facilities |
| Health, safety and environment | The Group operates in a dangerous and hazardous industry The Company has committed to meet international health, safety and environmental standards HSE performance is reported monthly to executive management and a sub-committee of the Board The Company recognises the reputational risk it faces in the event of an HSE disaster |
| Information technology (IT) | IT is critical in carrying out the business's day-to-day activities The Group regularly reviews its business continuity and IT disaster recovery plans to minimise risks to its knowledge base |

**Financial risks**

| Risk | Description and mitigation strategy |
|---|---|
| Oil price | Fairfield's primary source of revenue is from the sale of oil products The Fairfield Commodity Price Hedging Policy has been designed to help manage adverse price volatility by entering into commodity hedges The Company adopts hedge accounting principles in accordance with IAS 39 The Group's commodity hedging contracts are held by AA-creditworthy counterparties |
| Foreign currency | The functional currency of the Company is US dollars As an operator in the UK, the Group incurs significant operating and capital expenditure denominated in Sterling The Group's Foreign Exchange Policy seeks to mitigate this exposure by<br>• Contracting in US$ where there is no cost disadvantage, and<br>• Enabling management to forward hedge a proportion of the currency exposure using forward contracts and options |
| Credit | The Group transacts with various parties and as a consequence faces third party credit risk To mitigate this risk, Fairfield contracts with recognised, creditworthy parties<br>Key exposures arise as a result of the Group's joint venture relationships These relationships are governed by the terms of joint operating agreements which set out terms that minimise risk if one party defaults Where the Group is the operator, funding is made in advance The Group may have significant cash balances arising from capital calls and its operating activities at any particular time Cash is maintained on deposit with the Royal Bank of Scotland |
| Liquidity and funding | The nature of the Group's business exposes it to irregular cash flows To manage liquidity and funding shortfalls, the Group prepares an annual budget and quarterly forecasts which are subsequently measured against actual cashflows in its monthly management reporting to Executive Management and its equity investors<br>Equity funding is provided via Subordinated Preference Certificates and Preference Shares Before additional funding is obtained, Board approval is required The Board regularly assesses the Group's future capital requirements and seeks appropriate finance to meet its needs For financial reporting purposes these instruments are treated as debt |

# Directors' remuneration report

**Introduction**
As a private company, Fairfield Energy is not required to adhere to the Directors' Remuneration Report Regulations 2002 and the requirements of the 2008 Combined Code on Corporate Governance, but has where possible followed the relevant principles

**Remuneration Policy**
The Group's remuneration policy is to provide appropriate levels of remuneration to attract, motivate and retain high calibre Executive Directors and senior employees capable of achieving corporate objectives, and to encourage and appropriately reward superior performance in a manner that enhances shareholder value Accordingly, the Group has established a remuneration policy that ensures there is a clear link to business strategy and a close alignment with shareholder interests and aims to ensure that Executive Directors and senior employees are rewarded fairly for their contribution to business performance Consequently, the Group takes account of remuneration paid to Executive Directors and senior employees of comparable companies

The elements of remuneration for Executive Directors and senior employees are basic salary, annual bonus, non-cash benefits, pension payments and participation in the Company's long-term incentive scheme These elements of remuneration are described in detail below

**Executive Directors' Remuneration**
**Basic Salary**
Basic salaries are based on market conditions, and take into account the scope and responsibilities associated with the position, as well as the skills, experience and performance of the Executive Director Basic salaries are reviewed annually with effect from 1 January and set by reference to external benchmarking data for other similar companies engaged in oil and gas exploration and production The comparator group is chosen with regard to

- Companies in the same industry,
- The size of the Company including turnover, profit and the number of employees,
- The diversity and complexity of the business, and
- The business growth and expansion

Following a review from 1 January 2009, the basic salary of each Executive Director is as follows

| Executive Director | 2009 Basic salary | % Increase from 2008 |
|---|---|---|
| Mark Francis McAllister | £250,000 | 25% |
| Christopher Alan Wright | £134 000 | 0% |

In setting basic salaries, the Committee's general policy is to keep percentage increases broadly in line with those across the rest of the Group and to continue to ensure that a significant proportion of executive remuneration is linked to performance However, account was taken of the comparative data within the Mercer Oil & Gas Exploration and Production Survey that showed that the basic salary for the Chief Executive Officer was 33% below the median level

Consequently, the Committee determined that his basic salary should be increased to £250,000 to achieve better alignment with the relevant peer group The salary for the Chairman was unaltered in 2009

**2009 Annual Bonus Plan**
Each Executive Director is entitled to participate in the annual bonus plan In 2009 neither the Chairman nor the CEO participated in the annual bonus plan

The Group considers that the annual bonus is an important part of the remuneration package where associated performance targets reflect the key drivers for value creation and growth in shareholder value
Bonus awards are intended to encourage superior individual performance whilst fostering effective teamwork and maintaining a clear focus on corporate business objectives
Individual bonus awards are based on

- Assessment of delivery versus objectives contained within the individual performance contract,
- Assessment of individual contribution to the success of others, and
- Individual contribution to corporate deliverables

The following table details the various elements of the annual bonus plan and the manner in which this translates into the corresponding individual bonus awards

| Delivery of Performance contract (DPC) | Team Contribution (TC) | Corporate Deliverables (CD) |
|---|---|---|
| Delivery of all aspects of the individual Performance Contract equates to a bonus of 20% of annual basic salary (DPC = 0 20) subject to the Team Contribution and Corporate Deliverables multipliers<br>Exceptional performance beyond the objectives of the Performance Contract may lead to a bonus of up to 30% of annual basic salary | The Team Contribution multiplier recognises individual contribution to the success of others in achieving their objectives This multiplier is on a scale between 0 and 2 A multiplier of 1 applies when an individual shows the required commitment and performance in helping others to achieve their objectives | The Corporate Deliverables multiplier recognises material contribution to the achievement of the corporate objectives This may take the form of increased reserves in an asset, reduction in drilling costs, achieving more favourable tax status for a development or significant reduction in G&A This multiplier is on a scale between 1 and 2 |

Individual bonus payments are capped at 50% of annual basic salary In the event that the sum of all individual bonuses exceeds 30% of the total payroll for the year then all bonuses will be reduced pro-rata or in exceptional circumstances the Committee will be requested to exceed the limit

**Benefits**
The Company will either contribute 17% of basic salary to the personal pension plans of the executive directors or alternatively, will pay the sum as income, subject to deduction of income tax and National Insurance Contributions In addition, the Group's executive directors receive a range of benefits including 25 days of annual leave, private medical insurance, private dental insurance, personal accident insurance, group income protection and life assurance benefits The Group also reimburses the Executive Directors in respect of all expenses reasonably incurred by them in the normal performance of their duties

**Summary of Actual Remuneration**

A summary of the Directors' remuneration for the year ended 31 December 2009 and 2008 is provided in the table below

| | 2009 | 2008 |
|---|---|---|
| | $000 | $000 |
| Salaries | 717 | 797 |
| Bonuses | (2) | 75 |
| Social security costs | 96 | 114 |
| Pension costs | 67 | 63 |
| Insurance (medical and life) | 8 | 4 |
| Share-based payments | 619 | 261 |
| | 1,505 | 1,314 |
| Defined contributions schemes | | |
| Number of directors claiming benefits | 1 | 1 |

The remuneration of each Director, excluding long-term, share-based incentive awards, for the year ended 31 December 2009 compared with 2008 is set out in the table below

**Summary of Directors' Remuneration**

| | Fees/basic salary | Bonus in cash | Benefit in kind | 2009 Total | 2008 Total |
|---|---|---|---|---|---|
| | $000 | $000 | $000 | $000 | $000 |
| M F McAllister | 391 | - | 5 | 396 | 446 |
| C A Wright | 246 | - | - | 246 | 358 |
| Executive Director Total | 637 | - | 5 | 642 | 804 |
| S W C Eyers | - | - | - | - | - |
| P Kagan | - | - | - | - | - |
| D Krieger | - | - | - | - | - |
| D L Pearce | 31 | - | - | 31 | 34 |
| A Paterson (appointed 1/12/08) | 31 | - | - | 31 | 2 |
| F M T Ponsonby (resigned 31/07/09) | 18 | - | - | 18 | 36 |
| J van Steenbergen | - | - | - | - | - |
| Non-Executive Director Total | 80 | - | - | 80 | 72 |
| Director Remuneration Total | 717 | - | 5 | 722 | 876 |

The Chief Executive Officer also received a pension contribution in 2009 of $67,000 (2008 $37,000)

**Summary of Directors' Interests in Shares Held Under Option**

| Date of Grant | Awards to 31 December 2008 | Granted during 2009 | Lapsed in 2009 |
|---|---|---|---|
| | $000 | $000 | $000 |
| M F McAllister | | | |
| $5 options | 84 | 145 | - |
| $12 options | 60 | 75 | - |
| | 144 | 220 | - |
| C A Wright | | | |
| $5 options | 66 | 160 | - |
| $12 options | 60 | 80 | - |
| | 126 | 240 | - |
| S W C Eyers | - | - | - |
| P Kagan | - | - | - |
| D Krieger | - | - | - |
| D L Pearce* | See note below | - | - |
| A Paterson (appointed 1/12/08) | - | - | - |
| F M T Ponsonby (resigned 31/07/09) | - | - | - |
| J van Steenbergen | - | - | - |

* David Pearce has been awarded a future cash bonus in lieu of and equivalent to 64,000 share options

# Statement of directors' responsibilities for the consolidated financial statements

The Directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable United Kingdom law and those International Financial Reporting Standards (IFRSs) as adopted by the European Union

The Directors are required to prepare financial statements for each financial year which present fairly the financial position, financial performance and cash flows of the Group for that period In preparing those financial statements, the Directors are required to

- Select suitable accounting policies and then apply them consistently,
- Present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information,
- Provide additional disclosures when compliance with the specific requirements in IFRSs is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Group's financial position and financial performance, and
- State that the Group has complied with IFRSs, subject to any material departures disclosed and explained in the financial statements

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Group and enable them to ensure that the financial statements comply with the Companies Act 2006 They are also responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities

The Directors confirm that they have complied with these requirements and, having a reasonable expectation that the Group have adequate resources to continue in operational existence for the foreseeable future, will continue to adopt the going concern basis in preparing the accounts

Having made the requisite enquiries, so far as the directors are aware, there is no relevant audit information (as defined by Section 418(3) of the Companies Act 2006) of which the Group's auditors are unaware, and the directors have taken all the steps they ought to have taken to make themselves aware of any relevant audit information and to establish that the Group's auditors are aware of that information

Mark McAllister
Chief Executive Officer
Date 4 June 2010

# Independent auditor's report

## TO THE MEMBERS OF FAIRFIELD ENERGY LIMITED

We have audited the Group financial statements of Fairfield Energy Limited for the year ended 31 December 2009 which comprise the Consolidated Income Statement, the Consolidated Statement of Comprehensive Income, Consolidated Statement of Financial Position, the Consolidated Statement of Changes in Equity, the Consolidated Statement of Cash Flows and the related notes 1 to 34 The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006 Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed

### Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement set out on page 12, the directors are responsible for the preparation of the Group financial statements and for being satisfied that they give a true and fair view Our responsibility is to audit the Group financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland) Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors

### Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error This includes an assessment of whether the accounting policies are appropriate to the Group's circumstances and have been consistently applied and adequately disclosed, the reasonableness of significant accounting estimates made by the directors, and the overall presentation of the financial statements

### Opinion on financial statements

In our opinion the Group financial statements

- Give a true and fair view of the state of the Group's affairs as at 31 December 2009 and of its loss for the year then ended,
- Have been properly prepared in accordance with IFRSs as adopted by the European Union, and
- Have been prepared in accordance with the requirements of the Companies Act 2006

### Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report for the financial year, for which the Group financial statements are prepared, is consistent with the Group financial statements

### Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion

- Certain disclosures of directors' remuneration specified by law are not made, or
- We have not received all the information and explanations we require for our audit

### Other matter

We have reported separately on the parent company financial statements of Fairfield Energy Limited for the year ended 31 December 2009

Ernst & Young LLP

Ken Williamson (Senior statutory auditor)
for and on behalf of Ernst &Young LLP, Statutory Auditor
London

4 June 2010

# Consolidated income statement

for the year ended 31 December

| | Notes | 2009 $000 | Restated* 2008 $000 |
|---|---|---|---|
| Revenue | 6 | 174,644 | 103,106 |
| Cost of sales | | (127,918) | (62,990) |
| **Gross profit** | | **46,726** | **40,116** |
| Administrative expenses | | (17,307) | (17,696) |
| Gain on disposal of intangible assets | 20 | 2,875 | - |
| Net other operating income | 7i | 6,377 | 4,631 |
| Exploration and impairment losses | 7iii | (13,954) | (838) |
| **Operating profit** | | **24,717** | **26,213** |
| (Loss) / Gain on derivatives | 7iv | (27,514) | 42,346 |
| Finance income | 7v | 5,001 | 1,516 |
| Finance costs | 7vi | (84,421) | (66,944) |
| **(Loss) / Profit before tax** | | **(82,217)** | **3,131** |
| Income tax benefit / (expense) | 8 | 18,164 | (26,225) |
| **Loss after tax** | | **(64,053)** | **(23,094)** |
| **Earnings per share** | 9 | | |
| basic, loss for the year attributable to ordinary equity holders of the parent | | ($27 85) | ($10 04) |
| diluted, loss for the year attributable to ordinary equity holders of the parent | | ($27 85) | ($10 04) |

* Certain numbers shown above do not correspond to the 2008 financial statements as a result of retrospective adjustments and reclassifications set out in Note 4

# Consolidated statement of comprehensive income

for the year ended 31 December

| | 2009 $000 | Restated* 2008 $000 |
|---|---|---|
| **Loss for the period** | **(64,053)** | **(23,094)** |
| **Other comprehensive income** | | |
| Exchange differences on the translation of foreign operations | 4,933 | (12,216) |
| Fair value (loss) / gain on cash flow hedges | (17,064) | 125,329 |
| Recycling of effective cash flow hedges | (64,155) | - |
| Income tax benefit / (expense) relating to cash flow hedges | 40,610 | (62,665) |
| (Loss) / gain on cash flow hedges, net of tax | (40,609) | 62,664 |
| **Other comprehensive (loss) / income, net of tax** | **(35,676)** | **50,448** |
| **Total comprehensive / (loss) income** | **(99,729)** | **27,354** |

* Certain numbers shown above do not correspond to the 2008 financial statements as a result of retrospective adjustments and reclassifications set out in Note 4

# Consolidated statement of financial position

as at 31 December

| | Notes | 2009 $000 | Restated* 2008 $000 |
|---|---|---|---|
| **Non-current assets** | | | |
| Oil and gas properties | 10 | 487,983 | 415,240 |
| Exploration and evaluation assets | 11 | 102,951 | 68,803 |
| Property, plant and equipment | 12 | 891 | 1,277 |
| Goodwill and other intangible assets | 13 | 10,440 | 13,800 |
| Investments | 15 | 2,405 | 2,881 |
| Derivative financial instruments | 17b | 2,492 | 105,044 |
| | | **607,162** | **607,045** |
| **Current assets** | | | |
| Inventory | 21 | 2,312 | 2,800 |
| Trade and other receivables | 18 | 12,134 | 17,448 |
| Prepayments and accrued income | 19 | 43,875 | 18,586 |
| Derivative financial instruments | 17b | 64,831 | 93,469 |
| Cash and short-term deposits | 22 | 35,531 | 53,590 |
| | | **158,683** | **185,893** |
| Assets held for sale | 20 | - | 609 |
| **Total assets** | | **765,845** | **793,547** |
| **Current liabilities** | | | |
| Trade and other payables | 23 | 5,814 | 14,273 |
| Deferred income and accruals | 24 | 46,076 | 32,672 |
| Loans and borrowings | 26 | 94,349 | 93,355 |
| Provisions | 25 | 2,117 | 4,426 |
| | | **148,356** | **144,726** |
| **Non-current liabilities** | | | |
| Subordinated preference certificates | 27i | 350,671 | 202,159 |
| Preference shares | 27ii | 49,319 | 46,593 |
| Decommissioning provision | 25 | 283,834 | 318,829 |
| Provisions | 25 | 5,939 | - |
| Deferred tax liabilty | 8iv | 43,792 | 102,565 |
| Derivative financial instruments | 17b | 2,788 | - |
| | | **736,343** | **670,146** |
| **Total liabilities** | | **884,699** | **814,872** |
| **NET (LIABILITIES)** | | **(118,854)** | **(21,325)** |
| **Equity** | | | |
| Founder shares | 28 | 23 | 23 |
| Founder share premium | 28 | 198 | 198 |
| Cash flow hedge reserve | 28 | 22,055 | 62,664 |
| Foreign currency translation reserve | 28 | (7,898) | (12,831) |
| Retained deficit | 28 | (133,232) | (71,379) |
| **TOTAL EQUITY** | | **(118,854)** | **(21,325)** |

* Certain numbers shown above do not correspond to the 2008 financial statements as a result of retrospective adjustments and reclassifications set out in Note 4

Mark McAllister
Chief Executive Officer
Date 4 June 2010

# Consolidated statement of changes in equity

for the year ended 31 December

| | Notes | Founder shares $000 | Founder share premium $000 | Cash flow hedge reserve $000 | Foreign currency translation reserve $000 | Retained deficit $000 | Total $000 |
|---|---|---|---|---|---|---|---|
| At 1 January 2009 (as previously reported) | | 23 | 198 | 62,664 | (12,831) | (73,098) | **(23,044)** |
| Retrospective adjustment | | - | - | - | - | 1,719 | **1,719** |
| **At 1 January 2009 (restated)** | | 23 | 198 | 62,664 | (12,831) | (71,379) | **(21,325)** |
| Total comprehensive income | | - | - | (40,609) | 4,933 | (64,053) | **(99,729)** |
| Transactions with owners, recorded directly in equity | | | | | | | |
| Share-based payment transactions | 30 | - | - | - | - | 2,200 | **2,200** |
| **Balance at 31 December 2009** | **28** | **23** | **198** | **22,055** | **(7,898)** | **(133,232)** | **(118,854)** |

for the year ended 31 December (restated*)

| | Notes | Founder shares $000 | Founder share premium $000 | Cash flow hedge reserve $000 | Foreign currency translation reserve $000 | Retained deficit $000 | Total $000 |
|---|---|---|---|---|---|---|---|
| **At 1 January 2008** | | 23 | 198 | - | (615) | (49,754) | **(50,148)** |
| Total comprehensive income (as previously reported) | | - | - | 62,664 | (12,216) | (24,813) | **25,635** |
| Retrospective adjustment, net of tax | 4 | - | - | - | - | 1,719 | **1,719** |
| Total comprehensive income (restated) | | - | - | 62,664 | (12,216) | (23,094) | **27,354** |
| Transactions with owners, recorded directly in equity | | | | | | | |
| Share-based payment transactions | 30 | - | - | - | - | 1,469 | **1,469** |
| **Balance at 31 December 2008** | **28** | **23** | **198** | **62,664** | **(12,831)** | **(71,379)** | **(21,325)** |

* Certain numbers shown above do not correspond to the 2008 financial statements as a result of retrospective adjustments and reclassifications set out in Note 4

# Consolidated statement of cash flows

for the year ended 31 December

| | Notes | 2009 $000 | Restated* 2008 $000 |
|---|---|---|---|
| **Operating activities** | | | |
| (Loss) / Profit before tax | | (82,217) | 3,131 |
| *Adjustments for* | | | |
| SPC interest expense and unwinding costs | 27 | 50,954 | 30,339 |
| Fair value adjustment of derivatives | | 55,426 | (42,346) |
| Discount unwind | 25 | 13,454 | 9,414 |
| Depreciation, depletion, amortisation and impairment | | 50,164 | 15,785 |
| Gain on disposal of intangibles | | (2,891) | - |
| Share based payments | | 2,200 | 1,469 |
| Net finance costs | | 15,594 | (7,766) |
| *Working capital adjustments* | | | |
| (Increase) / decrease in trade and other receivables | | 5,314 | (5,691) |
| (Increase) / decrease in prepayments and accrued income | | (25,943) | (8,927) |
| (Increase) / decrease in inventory | | 256 | (30) |
| Increase / (decrease) in trade and other payables | | (7,577) | (6,145) |
| Increase / (decrease) in deferred income and accruals | | 4,859 | 28,400 |
| Increase / (decrease) in provisions | | (349) | (796) |
| **Net cash inflow from operating activities** | | **79,244** | **16,837** |
| **Investing activities** | | | |
| Proceeds from the sale of intangible assets | | 3,500 | - |
| Finance revenue | | 411 | 1,498 |
| Expenditure on oil and gas assets** | | (148,844) | (110,280) |
| Expenditure on property, plant and equipment | | (1,061) | (1,238) |
| Expenditure on evaluation and exploration assets | | (33,500) | (11,695) |
| Purchase of derivatives | | (2,666) | (27,582) |
| **Net cash outflow from investing activities** | | **(182,160)** | **(149,297)** |
| **Financing activities** | | | |
| Proceeds from issue of preference shares | | 2,726 | 5,604 |
| Proceeds from issue of SPCs | | 97,558 | 74,804 |
| Proceeds from borrowings | | 70,000 | 121,560 |
| Repayment of borrowings | | (74,307) | (25,000) |
| Interest paid | | (13,623) | (9,505) |
| Transaction costs (Facilities A, B and C) | | - | (5,800) |
| **Net cash inflow from financing activities** | | **82,354** | **161,663** |
| **(Decrease) / Increase in cash and cash equivalents** | | **(20,562)** | **29,203** |
| Net foreign exchange difference | | 2,503 | (3,669) |
| Cash and cash equivalents at beginning of the period | | 53,590 | 28,056 |
| **Cash and cash equivalents at the end of the period** | 22 | **35,531** | **53,590** |

* Certain numbers shown above do not correspond to the 2008 financial statements as a result of retrospective adjustments and reclassifications set out in Note 4

** In 2008, $70 2 million of the total $110 3 million related to the acquisition of Dunlin Area assets acquired as part of a business combination See Note 5 for additional details

## Notes to the consolidated financial statements

### 1 Significant accounting policies

**a) Reporting entity**
Fairfield Energy Limited is principally a holding and service company for the Fairfield Energy Group The consolidated financial statements for the year ended 31 December were authorised for issue in accordance with a resolution of the directors on 29 April 2010 The Group is a limited company incorporated and domiciled in England and Wales The registered office is located at Ash House, Staines, Middlesex, United Kingdom

**b) Basis of preparation**
The consolidated financial statements of the Group for the year ended 31 December 2009 have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union (EU) and as applied in accordance with the provisions of the Companies Act 2006 The accounting policies adopted are consistent with those applied in the financial statements for the year ended 31 December 2008, other than those detailed in section cc) Certain prior year adjustments were identified during the year These are set out in Note 4 Other reclassifications of prior year disclosures have been made to increase comparability and understandability of the financial statements

**c) Statement of compliance**
The consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards (IFRS) and adopted by the EU

**d) Basis of measurement**
The financial statements have been prepared under the historical cost convention except for certain financial assets and liabilities that have been measured at fair value

**e) Presentation and functional currencies**
The consolidated financial statements are presented in United States dollars, which is also the parent company's functional currency Each entity in the Group determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency

The financial statements are rounded to the nearest thousand ($000) unless stated otherwise

**f) Basis of consolidation**
The consolidated financial statements comprise the financial statements of the Company and its subsidiaries as at 31 December 2009 Subsidiaries are fully consolidated from the date on which control is transferred to the Group, and cease to be consolidated from the date at which control is transferred out of the Group Control exists when an entity has the power to govern the financial and operating policies of an entity so as to obtain benefit from its activities The financial statements of the subsidiaries are prepared for the same reporting period as the parent company, using consistent accounting policies All intra-group balances, income and expenses, unrealised gains and losses and dividends resulting from intra-group transactions have been eliminated in full

**g) Interests in joint ventures**
The Group's interests in jointly controlled assets are accounted for by recognising its proportionate share in assets and liabilities from joint ventures, except where as operator Fairfield takes on the role as independent contractor In these instances, receivables and payables relating to jointly controlled operations are brought to account on a gross basis Joint venture expenses and the Group's entitlement to production are recognised on a pro rata basis according to the Group's joint venture interest

**h) Business combinations and goodwill**
Business combinations are accounted for using the purchase method Contingent consideration is recognised if, and only if, the Group has a present obligation, the economic outflow was more likely than not and a reliable estimate is determinable A subsequent adjustment to the contingent consideration results in an adjustment to goodwill

Goodwill is initially measured at cost being the excess of the consideration transferred over the Group's net identifiable assets acquired and liabilities assumed If this consideration is lower than the fair value of the net assets of the subsidiary acquired, the difference is recognised in profit and loss

After the initial recognition, goodwill is assumed to have an indefinite life and is measured at cost less any accumulated impairment losses For the purpose of impairment, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units that are expected to benefit from the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units

Where goodwill forms part of a cash generating unit and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained

**i) Revenue recognition**

*Oil sales*
Revenue from the sale of oil is recognised when the significant risks and rewards of ownership have been transferred to the customer Revenue is therefore recognised when volumes are physically lifted from Sullom Voe Terminal The Group has adopted the entitlements method of accounting for oil and gas production Due to the fact that the Group follows the entitlement basis, adjustments in respect of overlift (liftings greater than production entitlement) and underlift (production entitlement greater than liftings) are recorded against cost of sales at market value Revenue earned under a lease or licence conferring ownership rights to production in which the Group has a working interest with other producers, is recognised in earnings on the basis of the Group's interest in the relevant lease or licence

*Rendering of services*
Income received as operator from joint ventures is recognised on an accruals basis in accordance with joint venture agreements and is included within 'other operating income' in the consolidated income statement

**j) Foreign currency translation**

*Transactions and balances*
Transactions in foreign currencies are initially recorded by the Group entities in their functional currencies at the spot exchange rate Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency spot rate of exchange ruling at the reporting date

*Group companies*
The assets and liabilities of foreign operations are translated into the presentation currency at the closing balance Statement of Financial Position dates and their Income Statements are translated at rates approximating the monthly average The exchange differences arising on the translation are recognised in other comprehensive income through the foreign currency translation reserve On disposal of a foreign operation, the component of other comprehensive income relating to that particular foreign operation is recognised in the Income Statement

The repayment of intercompany loans is neither planned nor considered likely in the foreseeable future Foreign exchange differences arising on the translation of parent company monetary assets or liabilities where repayment is considered neither planned nor likely are recognised in the Statement of Comprehensive Income, as part of the Company's net investment in the relevant operation in accordance with IAS 21

**k) Evaluation, exploration assets and oil and gas properties**
The Group follows a successful efforts accounting policy for oil and gas assets The success or failure of each exploration or appraisal effort is assessed on a well-by-well basis

*Exploration and evaluation expenditure*
Expenditure incurred prior to obtaining legal rights to explore an area is expensed immediately to the Income Statement. Exploration and evaluation expenditure associated with an exploration well, including acquisition costs related to exploration and evaluation activities are initially capitalised as intangible

assets Certain expenditures such as geological and geophysical exploration costs are expensed If the prospects are subsequently determined to be successful on completion of evaluation, the relevant expenditure including licence acquisition costs are capitalised as oil and gas assets If the prospects are subsequently determined to be unsuccessful, the associated costs are expensed in the period in which that determination is made

The Group may enter into farm-in or farm-out arrangements where it may introduce partners to share in the development of an asset For transactions involving assets at the exploration and evaluation phase, the Group adopts an accounting policy as permitted by IFRS 6 such that the Group does not record any expenditure made on its behalf under a 'carried interest' and does not recognise a gain or loss from any cash consideration received The value of the cash consideration is credited against costs previously incurred Farmed-out oil and gas properties are accounted for in accordance with IAS 16

*Oil and gas properties*

Oil and gas properties are carried at cost net of accumulated depletion and include construction, installation or completion of production and infrastructure facilities such as pipelines and platforms, capitalised borrowing costs, transferred exploration and evaluation assets, development wells, and the cost of dismantling and restoration Subsequent capital costs, including major maintenance, are included in the asset's carrying amount only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably Depreciation is charged on a unit of production basis against proven and probable reserves

**l) Property, plant and equipment**

Plant and equipment is stated at cost, net of accumulated depreciation and any provisions for impairment, if any Depreciation is calculated on a straight-line basis over the estimated useful life of the asset as follows

| | |
|---|---|
| IT equipment | 3 years |
| Furniture and fittings | 3 years |

**m) Intangible assets**

Intangible assets are measured on initial recognition at cost and carried net of accumulated depreciation Gains or losses arising from de-recognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in the Income Statement when the asset is derecognised Depreciation is calculated on a straight-line basis over an estimated useful life of 3 years

**n) Investments**

Investments are initially recognised at the cost of acquisition and carried net of accumulated depreciation and any provisions for impairment The assets are amortised based on units of production

**o) Impairment of assets**

*Exploration and evaluation assets*

Exploration and evaluation assets are assessed for indicators of impairment in accordance with the Group's accounting policy under IFRS 6 Exploration and evaluation assets are only assessed for impairment where the facts and circumstances suggest that the carrying amount of the asset may exceed its recoverable amount Indications that the carrying amount of the asset may exceed its recoverable amount include

- Substantive expenditure on further exploration and evaluation activities on the asset or group of assets is neither budgeted nor planned,
- The entity has decided to discontinue activities on the asset or group of assets as a result of failing to find commercially viable quantities of hydrocarbons, and
- The entity has sufficient data indicating that the carrying amount of the asset or group of assets is unlikely to be recovered in full from successful development or by sale

*Oil and gas assets*

Oil and gas assets are evaluated each reporting period to determine whether there are any indications of impairment If any such indication exists, a formal estimate of the recoverable amount is performed and an impairment loss recognised to the extent that carrying amount exceeds recoverable amount The recoverable amount of an asset or cash generating unit (CGU) is measured at the higher of fair value less costs to sell and value in use A CGU comprises the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups thereof Possible indicators of impairment include significant adverse changes in oil or gas reserves and/or long-term oil or gas prices

*Goodwill*

Goodwill is reviewed for impairment annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired Impairment is determined by assessing the recoverable amount of the CGU, or groups of CGU, to which the goodwill relates Where the recoverable amount of the CGU, or groups of CGU, is less than the carrying amount, an impairment loss is recognised

*Financial assets*

A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it is impaired A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset

*Impairment reversals*

Any impairments recognised to assets other than goodwill may be reversed if the circumstances leading to the impairment no longer exist or have decreased, by increasing the carrying value of the asset to its recoverable amount This may not exceed the carrying value that would have been determined, net of depreciation, had no impairment loss previously been recognised Impairments to goodwill cannot be reversed in accordance with IAS

Further details of the Group's impairment testing is disclosed in Note 14

**p) Derivative financial instruments and hedge accounting**

*Derivative financial instruments*

The Group uses derivative financial instruments such as swaps, options, futures and forward contracts to hedge its risks associated with commodity price fluctuations Derivatives assets and liabilities are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured to their fair value in line with market fluctuations The unrealised gain or loss on remeasurement is immediately recognised in the Income Statement, except where hedge accounting applies The fair values of derivative financial instruments that are traded on an active market are based on quoted market prices at the balance sheet date The fair value of financial instruments not traded on an active market is determined using appropriate valuation techniques

*Hedge accounting*

When a derivative is designated as a hedge for accounting purposes, the relationship between the derivative and the hedged item is documented, as is its risk management objective and strategy for undertaking the hedge transaction Also documented is the assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions have been, and will continue to be, highly effective in offsetting changes in fair values or cash flows of hedged items

For the purposes of hedge accounting, hedges are classified as cash flow hedges Cash flow hedges are those hedges that mitigate exposure to variability in cash flows that is either attributable to a particular risk associated with a recognised asset or liability or a highly probable forecast transaction or the foreign currency risk in an unrecognised firm commitment The effective portion of changes in the fair value of derivatives are recognised in equity in the hedging reserve The gain or loss relating to any ineffective portion is recognised in the Income Statement immediately Amounts accumulated in equity are taken to the Income Statement in the periods when the hedged item affects income, for instance, when the forecast sale that is hedged takes place

Hedge accounting is discontinued when the hedging instrument expires, no longer qualifies for hedge accounting or is terminated At that point in time, any cumulative gain or loss on the hedging instrument recognised in equity remains in equity until the forecasted transaction occurs

**q) Cash and short-term deposits**
Cash and short-term deposits in the Statement of Financial Position comprise cash at bank and on hand, restricted cash holdings (cash held in joint ventures and escrow accounts) and short-term deposits with an original maturity of three months or less For the purposes of the Consolidated Statement of Cash Flows, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts

**r) Trade and other receivables**
Trade and other receivables, including receivables from related parties, are initially recognised at fair value and subsequently measured at amortised cost less an allowance for uncollectable amounts Collectability and impairment are assessed on a regular basis Subsequent recoveries of amounts previously written off are credited against other expenses in the Income Statement

**s) Inventories**
Inventories include consumable supplies and maintenance spares Inventories are valued at the lower of cost and net realisable value Cost is determined on a weighted average basis and includes direct costs and an appropriate portion of fixed and variable overheads where applicable Inventories determined to be obsolete or damaged are written down to net realisable value

**t) Non-current assets held for sale**
Non-current assets and disposal groups classified as held for sale are measured at the lower of carrying amount and fair value less costs to sell Non-current assets and disposal groups are classified as held for sale if their carrying amounts will be recovered through a sale transaction rather than through continuing use This condition is regarded as met only when the sale is highly probable and the asset or disposal group is available for immediate sale in its present condition

**u) Loans and borrowings**
Loans and borrowings represent amounts drawn under the Group's working capital loan facilities, classified according to the length of time remaining under the respective facility Loans are initially measured at fair value less directly attributable transaction costs After initial recognition, interest-bearing loans are subsequently measured at amortised cost using the effective interest method

Following repayment of the Mitsubishi loans (Facility A and B), there will be an ongoing obligation to pay royalties in respect of the Dunlin Areas At inception of the loan, royalties were deemed to be attached to Facility B This loan is accounted for at amortised cost whereby the discount is applied throughout the life of the loan At each reporting period, the Group reassess future cash flows associated with the repayment which leads to value changes that are required to be taken to the income statement Refer to Note 17 for impact on income statement

**v) Provisions and contingencies**

*General*

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects, where appropriate, the risks specific to the liability Where discounting is used, the increase in the provision due to the passage of time is recognised as a finance cost

A contingent liability is disclosed where the existence of an obligation will only be confirmed by future events or where the amount of the obligation cannot be measured reliably except where the contingent liability results as part of a business combination Continent liabilities identified as part of a business combination are recorded in the consolidated financial statements at its fair value Contingent assets are not recognised but disclosed where an inflow of economic benefits is probable

*Decommissioning liabilities*

Liabilities for decommissioning costs are recognised when the Group has an obligation to dismantle and remove a facility or an item of plant and to restore the site on which it is located, and when a reliable estimate of that liability can be made The amount recognised is the present value of the estimated future expenditure determined in accordance with local conditions and requirements The unwinding of the discount is expensed as incurred and recognised in the income statement as a finance cost The estimated future costs of decommissioning are reviewed annually and adjusted as appropriate

On recognition of a liability, a decommissioning asset is also recognised and included within oil and gas assets The decommissioning asset is amortised using the unit of production method, based on proven and probable reserves

**w) Subordinated Preference Certificates (SPC) and convertible preference shares**

The Group issues financial instruments referred to as investment strips These instruments are required to be accounted for as financial liabilities under IAS 39 Each investment strip contains two components SPCs and "A" or "B" preference shares The SPCs are measured at amortised cost The difference between the net proceeds and amortised cost equate to the preference share value Refer to Note 27 for further detail

**x) Borrowing costs**

Borrowing costs are recognised in the Income Statement in the period in which they are incurred except for borrowing costs incurred on borrowings directly attributable to development projects that are capitalised within the development/producing asset

**y) Leases**

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement at inception date Depending on the nature of the agreement, the lease will be treated as either a financing or operating lease

**z) Share-based payment transactions**

Employees (including senior executives) and Directors of the Group receive remuneration in the form of share-based payment transactions, whereby employees render services as consideration for equity instruments ('equity-settled transactions')

*Equity settled transactions*

The cost of equity settled transactions with employees and Directors are measured by reference to the fair value at the date at which they are granted and are recognised as an expense over the vesting period, which ends on the date on which the relevant holders become fully entitled to the award Fair value is determined by an independent external valuer using an appropriate pricing model In valuing equity-settled transactions, no account is taken of any vesting conditions, other than conditions linked to the price of the shares of the Company (market conditions)

No expense is recognised for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition, which are treated as vesting irrespective of whether or not the market condition is satisfied, provided that all other performance conditions are satisfied

Forfeiture as defined in IFRS 2 and the specific conditions of the Group's share based payments refers to the failure to satisfy vesting conditions other than market conditions The fair values determined by the independent valuer do not make any advance allowance for employees leaving service before the vesting date and forfeiting their options However, where employees leave before vesting, the expenses in the relevant period reflect the actual experience of leavers before vesting

At each balance sheet date before vesting, the cumulative expense is calculated, representing the extent to which the vesting period has expired and the management's best estimate of the achievement or otherwise of non-market conditions number of equity instruments that will ultimately vest or in the case of an instrument subject to a market condition, be treated as vesting as described above The movement in cumulative expense since the previous balance sheet date is recognised in the income statement, with a corresponding entry in equity

**aa) Pension and other post-employment benefits**
The Company operates a defined contribution pension scheme Amounts payable to the pension plan are charged to the income statement in the same period in which the services have been rendered by the employees

**bb) Taxation**
The tax expense represents the sum of current tax and deferred tax

*Current income tax*
Current income tax is provided at amounts expected to be paid (or recovered) using tax rates and laws that have been enacted or substantively enacted by the date of the statement of financial position

*Deferred income tax*
Deferred income tax is recognised on temporary differences arising between the tax base of assets and liabilities and their carrying amounts in the consolidated financial statements

A deferred income tax liability is not recognised if a temporary difference arises on initial recognition of an asset or liability in a transaction (other than a business combination), that at the time of the transaction, affects neither, accounting nor taxable profit or loss

Deferred income tax assets are recognised to the extent that it is probable that future income tax profit will be available against which the temporary differences can be utilised

Deferred income tax is provided on temporary differences arising on investments in subsidiaries, jointly controlled entities and associates, except where the timing of the temporary difference can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future

Deferred tax assets and liabilities are measured based on tax rates and laws enacted or substantively enacted at the statement of financial position date Deferred tax liabilities may be offset against deferred tax assets within the same tax entity and tax jurisdiction Measurement of deferred tax liabilities and assets reflect the tax consequences expected to arise from the manner in which the asset or liability is recovered or settled

*Petroleum Revenue Tax*
Current UK Petroleum Revenue Tax (PRT) is charged as a tax expense on chargeable field profits included in the income statement and is deductible for UK corporation tax Deferred PRT is calculated and provided for on temporary differences included in the Consolidated Statement of Financial Position

**cc) Changes in accounting policy and disclosures**
The accounting policies adopted are consistent with those of the previous financial year except as follows

- *Amendments to IFRS 2 Share-based Payment - Group Cash-settled Share-based Payment Transactions* - This amendment clarifies the definition of vesting conditions and prescribes treatment for an award that is cancelled (Effective date 1 January 2009)
- IFRS 7 *Financial Instruments Disclosures* - Changes in disclosures such that fair value measurements are to be disclosed by the source of inputs using a three-level hierarchy For impact of this new disclosure on the financial statements refer to Note 17 Liquidity risk management has not been effected by this disclosure change
- IFRS 8 *Operating Segments* - Changes in disclosures Refer to Note 3 for impact of this standard
- IAS 1(R) *Presentation of financial statements* - Changes in disclosures and the additional requirement to report the Statement of Comprehensive Income Also, within the Statement of Changes in Equity owner and non-owner changes in equity are required to be disclosed separately
- IAS 23(R) *Borrowing Costs* – Changes in treatment of borrowing costs such that the option to expense costs incurred to finance the construction of a qualifying asset has been removed and therefore must be capitalised

**dd) New Standards and Interpretations not yet adopted**
A number of new standards, amendments to standards and interpretations are not yet effective for the year ended 31 December 2009, and have not been applied in preparing these consolidated financial statements and are expected to impact the Group upon adoption

- IFRS 3 *Business Combinations* (revised 2008) – Costs of acquisitions are to be expensed where previously they were capitalised (Effective date for acquisitions in annual periods beginning on or after 1 July 2009)
- IAS 24 *Related Party Disclosures* (revised 2009) - Requires additional disclosure (Effective date 1 January 2011)
- IFRS 9 *Financial Statements* retains but simplifies the mixed measurement model and establishes two primary measurement categories for financial assets, amortised cost and fair value The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset (Effective date 1 January 2013) This standard is yet to be adopted by the EU and consequently the Group has not determined when the standard will be implemented

The impact of the changes in accounting standards are not expected to have a material impact on the accounting policies of the Group

## 2 Critical accounting estimates, assumptions and judgements

**a) Critical accounting estimates and assumptions**

**i Impairment**

Impairment of assets is assessed in accordance with Note 1(o) For oil and gas assets, the recoverable amount is calculated using the expected future cash flows based on reserves, future production profiles, commodity prices and costs

**ii Commercial reserve quantities**

Commercial reserves are proven and probable oil and gas reserves, which are defined as the estimated quantities of crude oil, which geological, geophysical and engineering data demonstrate with a specified degree of certainty to be recoverable in future years from known reservoirs and which are considered commercially producible Reserve quantities have been estimated by Gaffney Cline & Associates (GCA) GCA has extensive experience conducting reserves and resource estimations utilising the Securities Exchange Commission (SEC) rules and definitions promulgated by the Society of Petroleum Engineers (SPE)

Commercial reserve quantities and the associated cessation of production assumptions impact various items in the financial statements, including depreciation, depletion and amortisation, impairment testing (refer Note 14), decommissioning assets and liabilities (refer to notes 10, 15 and 25) and the amortised cost of the overriding royalty interest association with the term loan facility (refer to Note 26)

**iii Decommissioning liabilities**

The decommissioning of oil and gas assets is not due to occur for many years into the future Consequently, judgement is required in relation to the estimated cash flows, removal date, environmental legislation, and the liability specific discount rate used to determine the present value of these cash flows

**iv Loans and borrowings**

Following the repayment of loan facilities A and B, there will be an ongoing obligation to pay royalties in relation to the Dunlin Areas In calculating this obligation management is required to exercise judgement in relation to the discount rate, future cash flows, estimated life of the loan and future LIBOR rates

**b) Critical judgements in applying the Group's accounting policies**

**i Exploration and evaluation**

The Group accounts for exploration and evaluation assets in accordance with the policy set out in Note 1(k) In applying this policy, management are required to make certain estimates and assumptions in relation to the assessment of whether reserves are commercially viable Where costs have been capitalised in accordance with Note 1(k) and are subsequently considered unsuccessful, amounts are written off to the Income Statement

**ii SPCs and preference shares**

SPCs and preference shares are funding instruments sourced from private equity The value of these instruments is based on estimated future cash flows and are impacted by the expected conversion date As at the balance sheet date, the Group has made the judgment that conversion will occur on the expected Initial Public Offering date, May 2010

## 3 Segmental reporting

In accordance with IFRS 8 *Operating Segments,* the Group is required to report separately information about each reportable segment The Group has several operating segments that are aggregated into a single reporting segment as each of the segments have similar economic characteristics, and are similar in each of the following respects the nature of the products and their production processes, the type of customers, the methods in which products are distributed and the nature of the regulatory environment The Group's operations are limited to the North Sea and oil revenue is currently generated from one customer

## 4 Restatements and reclassifications

### i Retrospective restatements

The following retrospective restatements have been made to the 2008 comparative information

a) Revenue entitlements – During 2009, the Group identified overlift and underlift positions acquired as part of the Dunlin acquisition at 1 May 2008 that were incorrectly excluded from its revenue entitlements calculation as at 31 December 2008 The impacts on the consolidated financial statements were to increase the net profit after tax and net assets by $1 7 million Additional detail is set out in the tables below

b) Balance sheet adjustments – The Group identified a process error that occurred when recording the Group's share of the Dunlin Area assets in its subsidiary entities The error resulted in a misstatement of accounts payable, cash and short-term deposits and accounts receivable Additional detail is set out in the tables below

An opening statement of financial position for the comparable period has not been presented as both of the restatements relate to the Dunlin area assets, which were only acquired part way through 2008

| Effect on the income statement | Previously stated 2008 | (a) Revenue entitlements 2008 | (b) Balance sheet adjustments 2008 | Restated 2008 |
|---|---|---|---|---|
| Selected lines | $000 | $000 | $000 | $000 |
| Cost of sales | 66,428 | (3,438) | - | **62,990** |
| **Loss before tax** | (307) | 3,438 | - | **3,131** |
| Income tax expense / (benefit) | (24,506) | (1 719) | - | **(26,225)** |
| **Net loss after tax** | **(24,813)** | **1,719** | **-** | **(23,094)** |
| **Effect on the statement of financial position** | | | | |
| Selected lines | | | | |
| Cash | 72,215 | - | (18,625) | **53,590** |
| Trade and other receivables, prepayments and accruals | 35,103 | (1,303) | 2,234 | **36,034** |
| Current assets | 203 587 | (1,303) | (16,391) | **185,893** |
| **Total assets** | 811,241 | (1,303) | (16,391) | **793,547** |
| Trade and other payables, deferred income and accruals | (68,078) | 4,742 | 16,391 | **(46,945)** |
| Current liabilities | (165,859) | 4,742 | 16,391 | **(144,726)** |
| Deferred tax liabilities | (100,846) | (1 719) | - | **(102,565)** |
| Non-current liabilities | (668,427) | (1,719) | - | **(670,146)** |
| **Total liabilities** | (834,286) | 3,023 | 16,391 | **(814,872)** |
| Retained deficit | (73,098) | 1,719 | - | **(71,379)** |
| **Total equity** | (23,044) | 1,719 | - | **(21,325)** |
| **Effect on the cash flow statement** | | | | |
| Profit / (Loss) from operations before taxation | (307) | 3,438 | - | **3,131** |
| Non-cash adjustments | 23,382 | - | (16,707) | **6,675** |
| (Increase) / decrease in trade and other receivables | (5,691) | - | - | **(5,691)** |
| (Increase) / decrease in prepayments | (7 998) | 1 305 | (2,234) | **(8,927)** |
| (Increase) / decrease in inventory | (30) | - | - | **(30)** |
| Increase / (decrease) in trade and other payables | 43,389 | (4,743) | (16,391) | **22,255** |
| Increase / (decrease) in provisions | (576) | - | - | **(576)** |
| *Net cash flow from operating activities* | 52,169 | - | (35,332) | **16,837** |
| *Net cash flow from investing activities* | (149,297) | - | - | **(149,297)** |
| *Net cash flow from financing activities* | 161,663 | - | - | **161,663** |
| Increase in cash and cash equivalents | 64 536 | - | (35,333) | **29,203** |
| Net foreign exchange difference | (20,377) | - | 16,708 | **(3,669)** |
| Cash and cash equivalents at beginning of the period | 28,056 | - | - | **28,056** |
| **Cash and cash equivalents at period end** | **72,215** | **-** | **(18,625)** | **53,590** |

### ii Reclassifications

The Group has made certain reclassifications to the presentation set out within in its 2008 financial statements to assist users of its financial statements Significant reclassifications are described below

*Consolidated Income Statement*

- Foreign exchange gains and losses – Realised and unrealised foreign exchange gains and losses have been reclassified from administrative expenses to either finance income or finance costs This reclassification has been made to help users of the accounts to better understand changes to administrative expenses by removing fluctuations caused only by foreign exchange The impacts of these changes are disclosed in notes 7v and 7vi, and
- Exploration write-offs – Exploration write-offs have been reclassified from cost of sales to a separate component of the operating profit below the gross profit line As exploration write-offs and impairment losses have been grouped together in 2009 (refer to notes 13 and 14), it was considered more appropriate to disclose this line item below gross profit The impact of this change is disclosed on the face of the Income Statement

*Consolidated Statement of Financial Position*

- Exploration and evaluation assets and goodwill and other intangible assets – In 2008 the Group presented its exploration and evaluation assets and website costs as one line item, referred to as "intangible assets" In the current period, the Group now considers it more meaningful to users of its accounts to separately disclose its investment in exploration and evaluation assets and combine "goodwill and other intangible assets" The impact of these changes can be identified on the face of the Statement of Financial Position and within notes 11 and 13, and

- Prepayments and accrued income, and deferred income and accruals – The Group has disaggregated these current assets and current liabilities from trade and other receivables and trade and other payables respectively, to separate line items accounts as they contain items with greater volatility (i e overlift and underlift positions and income accrued for hedging positions) The impact of these changes on the consolidated financial statements can be identified on the face of the Statement of Financial Position and within notes 18, 19, 23 and 24

*Consolidated Statement of Cash Flows*

- Fair value adjustment on derivatives – This non-cash item has been reclassified from investing activities to a non-cash item within operating activities to better reflects its nature The impact of this adjustment can be identified on the face of the Statement of Cash Flows,
- Net foreign exchange difference – Realised foreign exchange gains and losses of $16 7 million charged to the Income Statement (refer to Note 7vi) have been reclassified from net foreign exchange differences to net finance costs This presentation shows net foreign exchange differences that reflect unrealised gains and losses arising from changes in foreign exchange rates in accordance with IAS 7 Statement of Cash Flows, and
- Grouping of similar items – The number of line items on the Statement of Cash Flows has been reduced by grouping similar items together This principle has been applied to finance income and expense items, depreciation, depletion and amortisation items and expenditure on certain oil and gas assets

**iii Other presentation changes**

Certain presentational changes have been made to assist users of the financial statements These changes include

- The Company accounts of Fairfield Energy Limited have been presented separately following the consolidated financial statements to simplify the presentation of the accounts, and
- A Statement of Comprehensive Income has been prepared in accordance with to the revised International Accounting Standard IAS 1 The presentation of this statement impacts the presentation of the statement of changes in equity The impacts of these changes can be seen on the face of the respective financial statements

## 5 Business combinations

**Acquisitions in 2009**

There have been no transactions involving business combinations during the year ended 31 December 2009

**Acquisitions in 2008**

On 21 December 2007, Group entities Fairfield Betula Limited and Fairfield Fagus Limited and subsidiaries of Mitsubishi Corporation (together the "Purchasers") signed sale and purchase agreements to acquire Dunlin, Dunlin South West, Merlin and Osprey fields, collectively referred to as the Dunlin Area, from Shell U K Limited, Esso Exploration and Production UK Limited, Statoil (UK) Limited and OMV (UK) Limited (together the "Sellers") The purchase was completed on 30 April 2008 with an effective date of 1 January 2008 The date of acquisition was deemed to be 30 April 2008 for the following reasons

- The transaction was not unconditional until that date and could not be reversed,
- Whilst management had significant rights to control certain decisions in respect of the Fields, the SPA did not explicitly provide control over all areas, and
- Management did not view the Fields as being practically controlled on 21 December 2007 and whilst the Group benefited from the assets from 1 January 2008, no significant changes in control conditions arose between those dates

Key terms to the agreement included

i The Group acquired a 70 percent interest in the Dunlin Area fields with the remaining 30 percent acquired by subsidiaries of Mitsubishi Corporation,

ii Total consideration of $98 8 million for the Dunlin area fields was paid acquiring property and equipment, licence interests, working capital balances and decommissioning liabilities The Group's share of the consideration was $69 1 million,

iii The Group incurred additional acquisition costs of $2 3 million (with $1 5 million being prepaid in 2007),

iv The security for the decommissioning liability was based on the United Kingdom Offshore Operators Association decommissioning and security agreement guidelines The guidelines provide the principles for calculation of decommissioning liabilities The security took the form of an irrevocable standby letter of credit,

v A subsidiary of Mitsubishi Corporation provided the guarantee to procure the letters of credit required under the decommissioning security, and

vi The Group's share of the consideration paid was financed through a $72 million term loan provided by a financing subsidiary of Mitsubishi Corporation The remainder of the purchase consideration was funded through interest-free parent company loans

The fair value of the identifiable assets and liabilities of the Dunlin Area fields as at the date of acquisition were

| | Group consideration | Fair value adjustment | Fair value on acquisition |
|---|---|---|---|
| | $000 | $000 | $000 |
| Oil and gas properties | 81,736 | - | 81,736 |
| Decommissioning asset | - | 304,500 | 304,500 |
| Inventories | 2,771 | - | 2,771 |
| Other current assets | 1,946 | - | 1,946 |
| Total assets | 86,453 | 304,500 | 390,953 |
| Other current liabilities | (14,681) | - | (14,681) |
| Decommissioning provision | - | (304,500) | (304,500) |
| Deferred tax liabilities | - | (8,493) | (8,493) |
| Total liabilities | (14,681) | (312,993) | (327,674) |
| **Net assets** | **71,772** | **(8,493)** | **63,279** |
| Goodwill arising on acquisition | | | 8,493 |
| **Total consideration** | | | **71,772** |

Represented by

| | |
|---|---|
| Cash consideration | 70,216 |
| Non-cash consideration | 1,556 |
| Total consideration | 71,772 |

It is not possible to disclose the carrying values of the assets, liabilities and contingent liabilities immediately before the combination as this information was not provided by the vendors Goodwill on acquisition resulted due to the recognition of deferred tax liabilities created from the difference between the fair value of the assets acquired and their tax basis

## 6 Revenue

| | 2009 | 2008 |
|---|---|---|
| | $000 | $000 |
| Oil revenue from the sale of goods | 110,489 | 103,106 |
| Gain / (loss) on realisation of cash flow hedges | 64,155 | - |
| **Total revenue** | **174,644** | 103,106 |

## 7 Other income / expenses

### i Other operating income

| | 2009 | 2008 |
|---|---|---|
| | $000 | $000 |
| Joint venture recoveries | 4,832 | 4,534 |
| Other income | 1,545 | 97 |
| **Total other operating income** | **6,377** | 4,631 |

### ii Depreciation, depletion and amortisation

| | 2009 | 2008 |
|---|---|---|
| | $000 | $000 |
| Included in cost of sales | | |
| Depreciation of Sullom Voe Terminal and Brent System | 226 | 91 |
| Depreciation, depletion and amortisation of oil and gas properties | 35,239 | 14,090 |
| Included in administrative expenses | | |
| Amortisation of intangible assets | 55 | 42 |
| Depreciation of property, plant and equipment | 690 | 724 |
| **Total depreciation, depletion and amortisation** | **36,210** | 14,947 |

### iii Exploration and impairment losses

| | 2009 | 2008 |
|---|---|---|
| | $000 | $000 |
| Included in exploration and impairment losses | | |
| Impairment of goodwill | 4,062 | - |
| Release of advance | (6,000) | - |
| Exploration write-offs during the year | 7,735 | 380 |
| Exploration write-offs previously capitalised | 8,157 | 458 |
| **Total exploration and impairment losses** | **13,954** | 838 |

During the period, Fairfield Cedrus Limited received an advance of $6 million from Gemini Oil & Gas Fund II (Gemini) for the development of the North East Maureen appraisal well The amount was repayable commencing the first sale of oil As Gemini carried the risk of unsuccessful drilling, and drilling was proven unsuccessful, the amount was recognised in the income statement

In the consolidated financial statements for 2008, exploration write-offs were recorded as a separate line item within Gross Profit These balances have been reclassified in 2009

### iv Derivative financial instruments

| | 2009 | 2008 |
|---|---|---|
| | $000 | $000 |
| Ineffective portion of effective options | (13,852) | (5,875) |
| Fair value change of instruments not designated as hedges | (13,662) | 51,476 |
| Fair value adjustment on lapse of contract | - | (3,255) |
| **(Loss) / Gain on derivatives** | **(27,514)** | 42,346 |

Additional information regarding the impact of derivative financial instruments on the consolidated financial statements is set out in Note 17

### v Finance income

| | 2009 | 2008 |
|---|---|---|
| | $000 | $000 |
| Interest income | 413 | 1,516 |
| Foreign exchange gains | 4,006 | - |
| Discount unwind reversal | 582 | - |
| **Total finance income** | **5,001** | 1,516 |

### vi Finance costs

| | 2009 | 2008 |
|---|---|---|
| | $000 | $000 |
| Interest on loans and other finance costs | 20,013 | 10,484 |
| Interest and finance costs on SPCs (Note 27) | 50,513 | 30,109 |
| Discount unwinding | 13,454 | 9,413 |
| Amortisation of SPC transaction costs (Note 27) | 441 | 230 |
| Foreign exchange losses | - | 16,708 |
| **Total finance costs** | **84,421** | 66,944 |

### vii Operating leases

| | 2009 $000 | 2008 $000 |
|---|---|---|
| Minimum lease payments recognised as an expense | 1,300 | 978 |

The future minimum lease payments at 31 December 2009 are shown in the table below

| | 2009 $000 | 2008 $000 |
|---|---|---|
| Payable within | | |
| One year | 1,225 | 1,059 |
| One to five years | 1,206 | 1,060 |
| More than five years | - | - |
| | 2,431 | 2,119 |

There were no contingent rentals or sub-lease payments relating to the operating leases The operating leases relate to rental office accommodation

### viii Auditors' remuneration

| | 2009 $000 | 2008 $000 |
|---|---|---|
| Fees payable to auditors Ernst & Young | | |
| Fees payable for the audit of the Company's statutory accounts* | 480 | 527 |
| Fees payable for the audit of the Company's subsidiaries pursuant to legislation | 347 | 382 |
| Fees payable for other services pursuant to legislation | 192 | - |
| Fees payable for tax services | 694 | 416 |
| Fees payable for transactional services | 483 | 3 |
| | 2,196 | 1,328 |

*Fees in respect of the audit of the accounts of Fairfield Energy Limited including the Group's consolidated financial statements

### ix Employee benefits expense

| | 2009 $000 | 2008 $000 |
|---|---|---|
| Wages and salaries | 6,781 | 7,191 |
| Bonuses | 1,013 | 1,110 |
| Social security costs | 1,079 | 1 007 |
| Pension costs | 1,201 | 1,203 |
| Insurance (medical and life) | 3 | 167 |
| Share-based payments | 2,200 | 1 469 |
| | 12,277 | 12,147 |

| | | |
|---|---|---|
| **Average number of employees** | | |
| Directors | 2 | 2 |
| Finance and administration | 19 | 13 |
| Technical | 28 | 27 |
| | 49 | 42 |

Additional information regarding the remuneration of key management is set out in Note 32vi

## 8 Income tax

The major components of income tax expense for the years ended 31 December 2009 and 2008 are

### i Income statement

| | 2009 $000 | 2008 $000 |
|---|---|---|
| **Current income tax** | | |
| Current income tax expense | - | - |
| **Deferred tax** | | |
| Relating to the origination and reversal of temporary differences | (16,298) | 29,738 |
| Prior year adjustments | (1,866) | (3,513) |
| **Income tax (benefit) / expense reported in the income statement** | (18,164) | 26,225 |

### ii Statement of comprehensive income

| | 2009 $000 | 2008 $000 |
|---|---|---|
| **Deferred tax related to items directly charged or credited within equity** | | |
| Income tax benefit / (expense) | 40,610 | (62,665) |
| **Income tax benefit / (expense) charged directly to equity** | 40,610 | (62,665) |

### iii Reconciliation of accounting loss before tax to tax benefit / expense recorded in the consolidated income statement

A reconciliation between tax expense and the product of accounting profit multiplied by the UK standard income tax rate for the year ended 31 December 2009 is as follows

| | 2009 $000 | 2008 $000 |
|---|---|---|
| Accounting (loss) / profit before income tax | (82,217) | 3,131 |
| Accounting (loss) / profit multiplied by the UK standard rate of corporation tax of 50% (Group) | 41,109 | (1,566) |
| Expenditure not deductible for tax purposes | (21,639) | (12,794) |
| Non-taxable income | 10,240 | 13,413 |
| Benefit of previously unrecognised temporary differences | 2,966 | 3,513 |
| Temporary differences not recognised | (8,382) | (12,135) |
| Group relief for no consideration | 924 | - |
| Differences relating to supplementary charge on ring fence profits | (12,982) | (16,656) |
| Release on impairment of asset acquired as a business combination | 4,062 | - |
| Prior year adjustments | 1,866 | - |
| **Income tax benefit / (expense) charged to the consolidated income statement** | 18,164 | (26,225) |

In 2008 the Group acquired interests in various producing fields in the UK North Sea The standard tax rate used above of 50% is the rate that applies to the Group's business of exploring for and exploiting hydrocarbons within the UK and its designated areas and is comprised of corporation tax of 30% plus a supplementary charge of 20%

The Group has unrecognised temporary differences in respect of UK tax losses of $23,328,000 (2008 $59,601,000) that should be available to carry forward indefinitely against future taxable profits of the companies in which the losses arose In addition, the Group has unrecognised temporary differences in respect of pre-trading ring fence expenditure of approximately $71,065,000 (2008 $6,053,000) which should be deductible in the companies in which they arose provided these companies commence trading in the next two to six years

Deferred tax assets have not been recognised in respect of temporary differences of Group companies that have either not yet started to trade or are not expected to make profits in the foreseeable future against which these temporary differences can be offset

**iv Deferred income tax**

Deferred income tax relates to the following

| | 2009 | 2008 |
|---|---|---|
| | $000 | $000 |
| At start of year | 102,565 | 5,182 |
| Expense to the Income Statement | (18,164) | 26 225 |
| Deferred tax arising from business combinations | - | 8,493 |
| Expense / (benefit) on fair value movements on hedges taken directly to equity | (40,609) | 62,665 |
| **Deferred tax liability** | 43,792 | 102,565 |

In 2008 the Group recognised a deferred tax liability of $8,493,000 as a result of the acquisition, during the year, of the Dunlin, Dunlin SW, Osprey and Merlin producing oil fields The deferred tax liability arose as a result of the difference between the fair values and the tax bases of the assets acquired The calculation of the deferred tax liability arising in respect of the business combination assumed a tax rate of 50%, representing the Company's estimate of the tax rate at which the temporary differences are expected to unwind in the future

The Dunlin Field is subject to Petroleum Revenue Tax ("PRT") Deferred PRT liabilities are provided on temporary differences of the field as at the statement of financial position The Company had PRT losses of approximately $150,000,000 as at 31 December 2009 (2008 $57,000,000) available to offset any other temporary differences

The movement in the deferred tax balances is set out below

**Year ended 31 December 2009**

| | Accelerated capital allowances | Provisions | Tax losses | Fair value movement on hedge | Other temporary differences | Total |
|---|---|---|---|---|---|---|
| | $000 | $000 | $000 | $000 | $000 | $000 |
| At 1 January 2009 | 207,620 | (159 413) | (37,728) | 85,466 | 6,620 | 102,565 |
| Adjustments in respect of prior years | - | - | (13 385) | 11,347 | 172 | (1,866) |
| Expense / (benefit) for the period | 38,088 | 17,496 | (42,029) | (25,723) | (4,130) | (16,298) |
| Expense / (benefit) taken directly to equity | - | - | - | (40,609) | | (40,609) |
| **At 31 December 2009** | 245,708 | (141,917) | (93,142) | 30,481 | 2,662 | 43,792 |

**Year ended 31 December 2008**

| | Accelerated capital allowances | Provisions | Tax losses | Fair value movement on hedge | Other temporary differences | Total |
|---|---|---|---|---|---|---|
| | $000 | $000 | $000 | $000 | $000 | $000 |
| At 1 January 2008 | - | - | - | - | 5,182 | 5,182 |
| Expense / (benefit) for the period | 199 127 | (159,413) | (37,728) | 22,801 | 1,438 | 26,225 |
| Expense from business combinations | 8 493 | - | - | - | - | 8,493 |
| Expense / (benefit) taken directly to equity | - | - | - | 62,665 | - | 62,665 |
| At 31 December 2008 | 207,620 | (159 413) | (37,728) | 85,466 | 6,620 | 102,565 |

## 9 Earnings per share

Basic earnings per share amounts are calculated by dividing net profit or loss for the year attributable to ordinary equity holders of the parent by the weighted average number of ordinary shares outstanding during the year

Diluted earnings per share amounts are calculated by dividing the net profit or loss attributable to ordinary equity holders of the parent by the weighted average number of ordinary shares that would be issued on conversion of all the dilutive potential ordinary shares into ordinary shares Potential ordinary shares shall be treated as dilutive when, and only when, their conversion to ordinary shares would decrease earnings per share or increase the loss per share from continuing activities As potential ordinary shares will not be treated as dilutive, the basic and diluted earnings per share are equivalent

The following reflects the income and share data used in the basic and diluted earnings per share calculations

| | 2009 | 2008 |
|---|---|---|
| | $000 | $000 |
| Net loss attributable to ordinary equity holders of the parent for basic and diluted earnings | (64,053) | (23,094) |
| Weighted average number of ordinary shares for basic earnings per share | 2,300,090 | 2,300,090 |
| The following reflects potential dilutive shares | | |
| Number of options in issue at the reporting period end | 3,947,500 | 1,998,200 |
| Convertible preference shares in issue at the reporting period end | 30,930,333 | 20,902,008 |
| **Total** | 34,877,833 | 22,900,208 |

## 10 Oil and gas properties

| | Oil and Gas Assets | Decommissioning Asset | Total |
|---|---|---|---|
| | $000 | $000 | $000 |
| **Year ended 31 December 2009** | | | |
| Net carrying amount at 1 January 2009 | 112,806 | 302,434 | **415,240** |
| Additions | 156,086 | - | **156,086** |
| Depreciation and impairment | (22,272) | (12,967) | **(35,239)** |
| Change in decommissioning asset | - | (48,104) | **(48,104)** |
| **Net carrying amount** | **246,620** | **241,363** | **487,983** |
| At 31 December 2009 | | | |
| Historical cost | 277,885 | 259,427 | **537,312** |
| Accumulated depreciation | (31,265) | (18 064) | **(49,329)** |
| **Net carrying amount** | **246,620** | **241,363** | **487,983** |

Acquisitions from business combinations are further disclosed in Note 5

| | Oil and Gas Assets | Decommissioning Asset | Total |
|---|---|---|---|
| | $000 | $000 | $000 |
| **Year ended 31 December 2008** | | | |
| Net carrying amount at 1 January 2008 | - | - | - |
| Additions | 121,800 | 304,500 | 426,300 |
| Depreciation and impairment | (8,994) | (5 096) | (14,090) |
| Change in decommissioning asset | - | 3,030 | 3,030 |
| Net carrying amount | 112,806 | 302,434 | 415,240 |
| **At 31 December 2008** | | | |
| Historical cost | 121,800 | 307,530 | 429,330 |
| Accumulated depreciation | (8,994) | (5,096) | (14,090) |
| Net carrying amount | 112,806 | 302,434 | 415,240 |

## 11 Exploration and evaluation assets

| | 2009 | 2008 |
|---|---|---|
| | $000 | $000 |
| Net carrying amount at 1 January | **68,803** | 52,534 |
| Additions | **45,468** | 11,621 |
| Provision adjustment | **(2,431)** | - |
| Exploration write-offs (Note 14) | **(15,892)** | (838) |
| Exchange rate adjustments | **7,003** | 6,095 |
| Non-current assets held for sale | - | (609) |
| **Carrying amount at 31 December** | **102,951** | 68,803 |

The exploration write-offs recorded for 2009 are discussed in detail in Note 14

## 12 Property, plant and equipment

| | IT equipment | Furniture | Total |
|---|---|---|---|
| | $000 | $000 | $000 |
| **Year ended 31 December 2009** | | | |
| Net carrying amount at 1 January 2009 | 1,267 | 10 | **1,277** |
| Additions | 302 | 2 | **304** |
| Depreciation and impairment | (683) | (7) | **(690)** |
| **Carrying amount at 31 December 2009** | **886** | **5** | **891** |
| At 31 December 2009 | | | |
| Historical cost | 2,849 | 41 | **2,890** |
| Accumulated depreciation | (1,963) | (36) | **(1,999)** |
| Net carrying amount | **886** | **5** | **891** |
| **Year ended 31 December 2008** | | | |
| Net carrying amount at 1 January 2008 | 1,047 | 10 | 1,057 |
| Additions | 932 | 12 | 944 |
| Depreciation and impairment | (712) | (12) | (724) |
| Carrying amount at 31 December 2008 | 1,267 | 10 | 1,277 |
| At 31 December 2008 | | | |
| Historical cost | 2,542 | 41 | 2,583 |
| Accumulated depreciation | (1,275) | (31) | (1,306) |
| Net carrying amount | 1,267 | 10 | 1,277 |

## 13 Goodwill and other intangible assets

| | Goodwill | Website costs | Software | Total |
|---|---|---|---|---|
| | $000 | $000 | $000 | $000 |
| **Year ended 31 December 2009** | | | | |
| Net carrying amount at 1 January 2009 | 13 675 | 125 | - | **13,800** |
| Additions | - | - | 757 | **757** |
| Amortisation and impairment | (4,062) | (55) | - | **(4,117)** |
| **Carrying amount at 31 December 2009** | **9,613** | **70** | **757** | **10,440** |
| **At 31 December 2009** | | | | |
| Historical cost | 13,675 | 167 | 757 | **14,599** |
| Accumulated amortisation and impairment | (4,062) | (97) | - | **(4,159)** |
| Net carrying amount | **9,613** | **70** | **757** | **10,440** |

Goodwill impairment is discussed in detail in Note 14

| | Goodwill | Website costs | Software | Total |
|---|---|---|---|---|
| | $000 | $000 | $000 | $000 |
| **Year ended 31 December 2008** | | | | |
| Net carrying amount at 1 January 2008 | 5,182 | 93 | - | 5,275 |
| Additions | 8,493 | 74 | - | 8,567 |
| Amortisation and impairment | - | (42) | - | (42) |
| Carrying amount at 31 December 2008 | 13,675 | 125 | - | 13,800 |
| **At 31 December 2008** | | | | |
| Historical cost | 13,675 | 167 | - | 13,842 |
| Accumulated amortisation and impairment | - | (42) | - | (42) |
| Net carrying amount | 13,675 | 125 | - | 13,800 |

The Group carries goodwill as a result of previous business combinations with Acorn Oil & Gas Limited and the acquisition of the Dunlin Area fields In all cases the goodwill created was equal to the deferred tax liabilities arising from the business combination Goodwill is tested annually for impairment – see Note 14

## 14 Impairment

The Group is required to test its assets for indicators of impairment under IFRS 6 and IAS 36 and goodwill annually in accordance with IAS 36 If an indicator of impairment exists, or for the testing of the goodwill, the recoverable amount of the CGU, groups of CGUs or goodwill (depending of the test carried out) must be higher than its carrying value Recoverable amount is the higher of fair value less costs to sell and value in use

**Assets (excluding goodwill)**

In the current period, the drilling of a dry-well in the North East Maureen area was an indicator of impairment for the exploration and evaluation assets associated with the Maureen Area As a consequence, it was determined that all capitalised costs in the Maureen Area would be tested for impairment as it is management's expectation that further development of the Maureen Area will not be pursued The testing carried out indicated that the recoverable amount for the Maureen Area (P110 and P591) to be approximately zero using both measurement bases (value in use and fair value less costs to sell) The excess of the carrying value over the recoverable amount was charged to the consolidated income statement as below

| | | | 2009 | 2008 |
|---|---|---|---|---|
| | | | $000 | $000 |
| **Asset** | **Related Fairfield subsidiary** | **Description** | | |
| Maureen | Fairfield Cedrus Ltd | E&E costs prior to 2009 | 1,640 | - |
| Maureen | Fairfield Energy Holdings Ltd | E&E costs prior to 2009 | 6,517 | |
| Maureen | Fairfield Cedrus Ltd | E&E 2009 expenditure | 7,735 | - |
| | | | 15,892 | - |

There were no impairments recognised in the consolidated financial statements for the year ended 31 December 2008 Exploration write-offs of $838,000 recorded in the consolidated income statement for the ended 31 December 2008 were written off in accordance with the Group s exploration and evaluation accounting policy

**Goodwill**

The Group performs goodwill impairment testing on an annual basis or more frequently if there are indicators of impairment The most recent test was performed at 31 December 2009 In assessing whether the goodwill has been impaired, the carrying amount of the cash-generating unit was compared with its recoverable amount The goodwill allocated to each cash-generating unit is set-out in the table below

| | | 2009 | 2008 |
|---|---|---|---|
| | | $000 | $000 |
| **Asset** | **Related Fairfield subsidiary(s)** | | |
| Maureen | Fairfield Cedrus Limited | - | 4,062 |
| Crawford | Fairfield Acer Limited | 1,083 | 1 083 |
| Dunlin Area | Fairfield Betula Limited and Fairfield Fagus Limited | 8,530 | 8,530 |
| | | 9,613 | 13,675 |

*Key assumptions*

The value in use calculations, for the purpose of impairment testing, require the use of estimates and assumptions such as discount rates, exchange rates, commodity prices, future capital requirements and future operating performance The key assumptions adopted include

a) Cash flows – Value in use calculations are based on cash flows expected to be generated by projected oil production profiles up to the expected dates of cessation of production of each field Cash flows are based on those set out in the Group's annual 3-year business plan and thereafter estimated through to the cessation of production date

b) Oil prices – In 2009, oil prices were estimated using prices adopted by the Group's external reserves engineer In 2008, prices were based on external market forecasts The specific prices are set out in the table below

| Year ($/bbl) | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | Thereafter |
|---|---|---|---|---|---|---|---|---|
| **2009 testing** | N/a | $81 | $86 | $88 | $87 | $87 | $88 | 2015 + 2% |
| **2008 testing** | $55 | $75 | $75 | $75 | $75 | $75 | $75 | $75 |

c) Production and reserves – The production and reserve profiles were based on proved and probable reserves based on an external report completed as at 31 December 2009 by Gaffney Cline and Associates Internal estimates were used as the basis for reserves adopted in 2008

d) Pre-tax discount rate – Management assessed its weighted average cost of capital as at 31 December 2009 in determining an appropriate pre-tax discount rate for impairment purposes The rate adopted was 16% (2008 20%)

*Testing outcomes*

The impairment testing indicated an impairment to the goodwill allocated to the Maureen area The value of goodwill recorded at the end of 2008 of $4 1 million was fully impaired in the income statement for the year ended 31 December 2009 There were no impairments of goodwill recognised in 2008

*Sensitivities*

The key sensitivities to the goodwill impairment test are oil prices, production reserves profiles and the discount rate adopted The Group has performed sensitivity analysis to determine if a reasonably possible change would eliminate the excess of the recoverable amount over the carrying value ('headroom') of each cash-generating unit This analysis identified that the existing headroom of the Dunlin Area assets of approximately $255 million would be eliminated if the forward oil price curve was reduced by approximately 18% each year The testing carried out did not identify any reasonably possible change that would impair the Crawford goodwill

## 15 Investments

| | 2009 | 2008 |
|---|---|---|
| | $000 | $000 |
| **Year ended 31 December** | | |
| Net carrying amount at 1 January | 2,881 | - |
| Additions | - | 2,972 |
| Depreciation | (226) | (91) |
| Change in decommissioning asset | (250) | - |
| **Carrying amount at 31 December** | **2,405** | 2,881 |
| At 31 December | | |
| Historical cost | 2,722 | 2 972 |
| Accumulated depreciation | (317) | (91) |
| **Net carrying amount** | **2,405** | 2,881 |

The Group holds a non-controlling interest in the Sullom Voe Terminal (SVT) and Brent System (BS) in order to provide an export route for oil production from the Dunlin Area Assets

## 16 Joint ventures

The Group has the following joint venture interests

| | | As at December 2009 | As at December 2008 |
|---|---|---|---|
| | Holding interest | Equity interest | Equity interest |
| Block 9/27a | Fairfield Acer Limited | **25 0%** | 25 0% |
| Clipper South | Fairfield Acer Limited | **50 0%** | 100 0% |
| Crawford | Fairfield Acer Limited | **52 0%** | 52 0% |
| Dunlin Area (Dunlin, Dunlin SW, Merlin, Osprey, Skye) | Fairfield Betula Limited<br>Fairfield Fagus Limited | **70 0%** | 70 0% |
| Maureen Area P110 | Fairfield Cedrus Limited | **61 54%** | 100 00% |
| Maureen Area P591 | Fairfield Cedrus Limited | **49 93%** | 81 14% |

On 1 July 2009, Fairfield Acer Limited (FAL) completed a farm-out agreement with RWE Dea UK SNS Limited (RWE) Under the terms of the agreement RWE acquired 50% of FAL's interest in Clipper South Discovery area comprising License P 465 Block 48/19c and License P 008 Blocks 48/19a and 48/20a The consideration received from RWE included the reimbursement of £2 9 million of historical costs and future funding development expenditure capped at £20 million ("carried interest") At 31 December 2009 £1 1 million of carried interest had been utilised Reimbursement of historical costs was credit against the associated exploration and evaluation and operating cost accounts

On 27 July 2009, Fairfield Cedrus Limited (FCL) signed a farm-out agreement assigning 48 96% of its participating interest in its Maureen Area to Endeavour Energy UK Limited (38 46%) and Challenger Minerals (North Sea) Limited (CML) (10 5%) to fund the development of an appraisal well Drilling was carried-out during the year Following the unsuccessful drilling, CML elected not to take-up its assigned interest which reverted back to FCL

## 17 Financial instruments

### a) Financial management

The Group holds a portfolio of commodity derivative contracts, with various counterparties, covering the underlying oil business The use of financial derivatives is governed by the Group's policies approved by the Board of Directors The Group does not enter into or trade financial instruments, including derivative financial instruments, for speculative purposes

### b) Fair value of derivative instruments

| | 2009 | 2008 |
|---|---|---|
| | $000 | $000 |
| Cash flow hedges | | |
| Commodity swaps | **33,072** | 95,485 |
| Option contract | **14,071** | 41,528 |
| | **47,143** | 137,013 |
| Non-designated hedges | | |
| Option contracts | **17,392** | 61,500 |
| | **17,392** | 61,500 |
| Total derivative financial asset and liabilities | **64,535** | 198,513 |

| | | |
|---|---|---|
| Current assets | **64,831** | 93,469 |
| Non-current assets | **2,492** | 105,044 |
| Non-current liability | **(2,788)** | - |
| | **64,535** | 198,513 |

**c) Fair value of financial assets and liabilities**

***(i) Fair values***

Set out below is a comparison by category of carrying amounts and fair values of all of the Group's financial instruments that are carried in the financial statements

| | Carrying Amount | | Fair Value | |
|---|---|---|---|---|
| | 2009 | 2008 | 2009 | 2008 |
| | $000 | $000 | $000 | $000 |
| *Financial assets* | | | | |
| Trade and other receivables | 11,118 | 12,437 | 11,118 | 12,437 |
| Prepayments and accrued income | 35 626 | 13,288 | 35,626 | 13,288 |
| Derivative financial instruments (current) | 64,831 | 93,469 | 64,831 | 93,469 |
| Derivative financial instruments (non-current) | 2,492 | 105,044 | 2,492 | 105,044 |
| Cash and short-term deposits | 35,531 | 53,590 | 35,531 | 53,590 |
| *Financial liabilities* | | | | |
| Trade and other payables | 5,814 | 14,273 | 5,814 | 14,273 |
| Deferred income and accruals | 22,578 | 18,840 | 22,578 | 18,840 |
| Loans and borrowings | 94,439 | 93,355 | 94,439 | 93,355 |
| Derivative financial instruments | 2,788 | - | 2,788 | - |
| Subordinated preference certificates | 350,671 | 202,159 | 353,212 | 220 200 |
| Preference shares | 49,319 | 46,593 | 158,827 | 52 255 |

The fair value of the financial assets and liabilities are included at the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale The following methods and assumptions were used to estimate the fair values

- Cash and short term deposits, trade and other receivables, prepayments and accrued income, trade and other payables, deferred income and accruals approximate their carrying values largely due to the short-term maturities of these instruments,
- Derivative financial instruments are based on mark-to-market valuations provided by the issuing investment bank,
- Loans and borrowings approximate their carrying values Additional details regarding loans and borrowings are described in Note 26, and
- Subordinated preference certificates and preference shares are valued based on assessments carried-out by an independent third party

***(ii) Financial instrument fair value hierarchy***

The below table shows the hierarchical classification of financial instruments measured at fair value as at 31 December 2009 Categorisation within the hierarchy has been determined on the basis of the lowest level input that is significant to the fair value measurement of the relevant asset as follows

Level 1 - Valued using quoted prices in active markets for identical assets
Level 2 - Valued by reference to valuation techniques using observable inputs other than quoted prices included within Level 1
Level 3 - Valued by reference to valuation techniques using inputs that are not based on observable market data

| | 2009 | | | | 2008 | | | |
|---|---|---|---|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total | Level 1 | Level 2 | Level 3 | Total |
| | $000 | $000 | $000 | $000 | $000 | $000 | $000 | $000 |
| **Financial assets** | | | | | | | | |
| Derivative financial instruments | - | 67,323 | - | **67,323** | - | 198,513 | - | **198,513** |
| **Financial liabilities** | | | | | | | | |
| Derivative financial instruments | - | 2,788 | - | **2,788** | - | - | - | - |

The fair value of derivative commodity assets and liabilities are estimated by discounting the difference between the contractual forward price and the current market forward prices for the residual maturity of the contract using a discount rate based on LIBOR plus an appropriate risk premium, and applying this to the contracted volumes

**d) Credit risk**

Credit risk represents the loss that would be recognised if the counterparties to financial instruments fail to perform as contracted The Group trades only with recognised, creditworthy third parties The majority of the Group's revenue comes through the sale of hydrocarbons to Petro Diamond Company Limited (Petro Diamond), which is a subsidiary of Mitsubishi Corporation In the event that Petro Diamond was not able to pay an invoice, the presence of a limited parent company guarantee from Mitsubishi Corporation to all of Petro Diamond s creditors ensures that the Group s credit risk from non-payment is reduced

The remainder of the Group's income comes in the form of recharges to joint venture partners Credit risk associated with this relationship is managed within the framework of the Joint Operating Agreements by committing to spending on projects when the funds from all operators are already in place

The Group may have significant cash balances arising from capital calls and its operating activities at any particular time Cash is maintained on deposit with the Royal Bank of Scotland

The Group's commodity contracts are held by two S&P AA- counter parties with the largest holding 77% of the exposure The option and commodity contract specify minimum credit rating criteria below which counter parties are required to provide additional security in the form of collateral or to transfer the contracts to alternative counter parties meeting the minimum credit criteria

The Group's maximum exposure to credit risk is limited to the carrying value of financial assets as disclosed in Note 17(c)

**e) Currency exposure**

***(i) Exposure to currency risk***

The Group's statement of financial position and income statement are affected by movements in USD/GBP exchange rates Currency exposure arises from sales or purchases in currencies other than functional currency During 2009, the Group did not engage in foreign currency hedging transactions The Group's exposure to foreign currency is as follows

| | 2009 | 2008 |
|---|---|---|
| | £000 | £000 |
| Cash and short-term deposits | 7,321 | 38,512 |
| Trade receivables | 4,674 | 710 |
| Trade payables | (18,569) | (1,932) |
| Net exposure | (6,574) | 37,290 |

The following significant exchange rates applied during the year

| | Average rate 2009 | 2008 | Reporting date spot rate 2009 | 2008 |
|---|---|---|---|---|
| USD GBP | 0 6391 | 0 5367 | 0 6198 | 0 6919 |

***(ii) Sensitivity analysis***

The following table demonstrates the sensitivity to a reasonably possible change in the Sterling exchange rate, with all other variables held constant, of the Group's profit before tax (due to movement in the foreign exchange component of costs)

| | Increase / decrease in £ US$ rate | Increase / (decrease) on lost before tax $000 |
|---|---|---|
| 2009 | +10% | 1,061 |
| | -10% | (1,061) |
| 2008 | +10% | (6,017) |
| | -10% | 6,017 |

***Methods and assumptions***

Sensitivity analysis was performed by applying a percentage increase/decrease to cash and short-term deposits, accounts receivable and accounts payable that were denominated in currencies other than functional currency The 10% level of change was considered to be realistic based upon the rates exhibited over the period

**f) Commodity price risk management**

The Group is exposed to commodity price volatility on oil sales The Group may enter into oil futures and swap contracts to hedge future production in order to reduce the Group's exposure to movements in the spot oil price In 2008, the Group purchased contracts covering production for 2009 and 2010 During 2009 the Group entered into certain derivative contracts to manage the commodity price risk for 2011 for a base level of forecast production The premium paid for new hedges taken out in 2009 was $2 7 million (2008 $27 6 million) The Group has designated these financial instruments as cash flow hedges The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges are deferred in equity The gain or loss relating to the ineffective portion is recognised immediately in profit or loss

The change in value of the financial instruments recognised directly in equity was a loss of $40 6 million (2008 gain of $62 7 million) In 2009, this was represented by a change in a loss in the fair value of $17 1 million (2008 gain of $125 3 million), a loss on recycling of effective cash flow hedges of $64 2 million (2008 $nil) offset by an income tax benefit of $40 6 million (2008 $62 7 million)

(i) The following table sets out a summary of the bbls of derivative contracts hedging commodity price risks at 31 December 2009 and 31 December 2008

| 31 December 2009 | Average Hedge Price US$ / bbl | 6 mths or less Volume (bbl) | 6-12 mths Volume (bbl) | 12-18 mths Volume (bbl) | 18 mths + Volume (bbl) | Total Volume (bbl) |
|---|---|---|---|---|---|---|
| Swaps (received fixed pay floating) | 108 51 | 345 801 | 320,764 | 346 200 | 288,500 | **1,301,265** |
| Puts purchased | 105 00 | 572,438 | 536,580 | - | - | **1,109,018** |
| Calls purchased | 153 00 | 345,801 | 320,764 | 346 200 | 288,500 | **1,301,265** |
| Total | | 1,264,040 | 1,178,108 | 692,400 | 577,000 | **3,711,548** |

| 31 December 2008 | Average Hedge Price US$ / bbl | 6 mths or less Volume (bbl) | 6-12 mths Volume (bbl) | 12-18 mths Volume (bbl) | 18 mths + Volume (bbl) | Total Volume (bbl) |
|---|---|---|---|---|---|---|
| Swaps (received fixed pay floating) | 134 60 | 309,348 | 309,350 | 345,801 | 266,722 | **1,231,221** |
| Puts purchased | 105 00 | 595,017 | 455,323 | 572,438 | 446,178 | **2,068,956** |
| Calls purchased | 185 00 | 309,348 | 309,350 | 345,801 | 266,722 | **1,231,221** |
| Total | | 1,213,713 | 1,074,023 | 1,264,040 | 979,622 | **4,531,398** |

(ii) Sensitivity Analysis – Sensitivity of the Net Loss to changes in the oil price

The table below summarises the impact of changes in the hedged oil price on the net loss of the Group,

| | | Profit before tax 2009 $000 | 2008 $000 |
|---|---|---|---|
| Oil Price ($US/barrel) | +/- $20 00 | +/- 25,327 | +/- 18,088 |

The Group has estimated that a $20 00 change in the oil price would lead to a reduction in the cash flow hedge reserve of $17 2 million

**g) Interest rate risk management**
Financial instruments exposed to interest rate risk include loan facilities B and C (linked to LIBOR) and cash held on deposit (interest bearing accounts at market rates) SPCs, have a fixed annual rate of interest of 8% for the first 7 years and 14% thereafter and therefore are not affected by external changes in interest rates

The Group's exposure to interest rate risk and sensitivity analysis on a change of 100 basis points in interest rates on balances of which interest is charged at 31 December 2009 is set out below

| | | | | Sensitivity Analysis | | | |
|---|---|---|---|---|---|---|---|
| | | | | Profit and Loss | | Equity | |
| Interest rate risk exposures 31 December 2009 | Floating interest rate $000 | Fixed interest rate $000 | **Total $000** | 100 Bp increase $000 | 100 bp decrease $000 | 100 bp increase $000 | 100 bp decrease $000 |
| Financial assets | | | | | | | |
| Cash | 35 531 | - | **35,531** | (355) | 355 | - | - |
| Financial liabilities | | | | | | | |
| Loan facilities | (94,349) | (273,000) | **(367,349)** | (920) | 920 | - | - |
| Provisions | (4,840) | - | **(4,840)** | (48) | 48 | - | - |
| **Net financial assets/(liabilities)** | **(63,658)** | **(273,000)** | **(336,658)** | | | | |

| | | | | | Sensitivity Analysis | | | |
|---|---|---|---|---|---|---|---|---|
| | | | | | Profit and Loss | | Equity | |
| Interest rate risk exposures 31 December 2008 | Notes | Floating interest rate $000 | Fixed interest rate $000 | **Total $000** | 100 bp Increase | 100bp decrease | 100bp increase | 100 bp decrease |
| Financial assets | | | | | | | | |
| Cash | | 53,590 | - | **53,590** | (536) | 536 | - | - |
| Financial liabilities | | | | | | | | |
| Loan facilities | | (93,355) | (273,000) | **(366,355)** | (966) | 966 | - | - |
| **Net financial assets/(liabilities)** | | **(39,765)** | **(273,000)** | **(312,765)** | | | | |

**h) Liquidity risk management**

The Group currently relies on drawing capital from its shareholders and investors to manage its funding requirements The annual budget is the basis for forecasting capital requirements and capital is called on the basis of it as adjusted for changes indicated in monthly and quarterly management reports Liquidity risk is managed by ensuring capital calls are issued well in advance to meet payment of expenses as they arise Capital calls require Shareholders and Investors to subscribe in US dollars to the issuance of additional Preference Shares and SPCs Until utilised, capital drawn down is held on short term deposits and on the current account

The following are the contractual maturities of financial liabilities, including estimated interest payments and excluding the impact of netting agreements

| **31 December 2009** | **Carrying Amount $000s** | **Contractual cash flows $000s** | **6mth or less $000s** | **6-12 months $000s** | **1-2 years $000s** | **2-5 years $000s** | **More than 5 years $000s** |
|---|---|---|---|---|---|---|---|
| **Non-derivative financial liabilities** | | | | | | | |
| Loans and borrowings | 94,349 | (97,064) [1] | (57,087) | (31,426) | (8,551) | - | - |
| Trade and other payables | 5,814 | (5,814) | (5,814) | - | - | - | - |
| Provisions | 291,890 | (517,795) | - | (1,614) | (5 939) | (504) | (509,738) |
| Subordinated preference certificates | 350,671 | (364,614) | - | - | - | - | (364,614) |
| Preference shares | 49,319 | (49,319) | - | - | - | - | (49,319) |
| | **792,133** | **(1,034,606)** | **(62,901)** | **(33,040)** | **(14,490)** | **(504)** | **(923,671)** |

| **31 December 2008 $000s** | **Carrying Amount** | **Contractual cash flows** | **6mth or less** | **6-12 months** | **1-2 years** | **2-5 years** | **More than 5 years** |
|---|---|---|---|---|---|---|---|
| **Non-derivative financial liabilities** | | | | | | | |
| Loans and borrowings | 93,355 | (95,355) [1] | (24,308) | (71,047) | - | - | - |
| Trade and other payables | 17,104 | (17,104) | (17,104) | - | - | - | - |
| Provisions | 323,255 | (495,663) | - | - | (975) | (3,451) | (491,237) |
| Subordinated preference certificates | 202,159 | (293,086) | - | - | - | - | (293,086) |
| Preference shares | 46,593 | (46,593) | - | - | - | - | (46,593) |
| | 682,466 | (947,801) | (41,412) | (71,047) | (975) | (3,451) | (830,916) |

[1]Loans and borrowings includes repayment of the term loan Facility B Payments are contingent upon production and the resulting cash flows which are inherently difficult to forecast accurately Additional details regarding the repayment of the facility is provided in Note 26

[2]Post the balance sheet date, a review of decommissioning liabilities was carried out The impacts of this review are discussed in Note 34

## 18 Trade and other receivables

| | 2009 | 2008 |
|---|---|---|
| | $000 | $000 |
| Trade receivables | 11,118 | 12 437 |
| VAT receivable | 1,016 | 5,011 |
| | 12,134 | 17,448 |

All trade and other receivables at 31 December 2009 are not past due or impaired

## 19 Prepayments and accrued income

| | 2009 | 2008 |
|---|---|---|
| | $000 | $000 |
| Prepayments | 6,586 | 7,186 |
| Accrued income | 37,289 | 11,400 |
| | 43,875 | 18,586 |

As at 31 December 2009 accrued income predominantly includes outstanding receipts from exercised hedging contracts, accrued oil sales, and payment and quantity lifting adjustments

## 20. Assets held for sale

During 2008 the Group actively marketed Licence P110 Block 16/29a Mabel Area It was subsequently sold to BP subject to a Sales and Purchase Agreement dated 23rd December 2008 which was completed on 20th March 2009 for a consideration of $3 5 million The asset is required to be disclosed at the lower of carrying value or fair value less costs to sell The carrying value of the Mabel asset at 31 December 2008 was $609,000 The gain recorded in the income statement during 2009 was $2,875,000 There were no disposals in 2008

## 21 Inventory

| | 2009 | 2008 |
|---|---|---|
| | $000 | $000 |
| Maintenance and replacement spares | 2,312 | 2 567 |
| Oil inventories | - | 233 |
| | 2,312 | 2,800 |

Inventories includes a provision of $909,000 (2008 $814,000) for consumables and maintenance stocks where it is considered that the carrying value exceeds its net realisable value

## 22 Cash and short-term deposits

| | 2009 | 2008 |
|---|---|---|
| | $000 | $000 |
| Cash at bank and in hand | 31,951 | 27,909 |
| Cash held in joint venture accounts | 3,580 | 25 681 |
| | 35,531 | 53,590 |

Cash held in joint venture accounts represent the Group share of total joint venture cash balances Restricted cash, other than cash held in joint venture accounts at the end of 2008 and 2009 was $9 5 million and $2 2 million respectively

## 23 Trade and other payables

| | 2009 | 2008 |
|---|---|---|
| | $000 | $000 |
| Trade payables | 3,704 | 4,194 |
| Joint Venture creditors | 2,110 | 10,079 |
| | 5,814 | 14,273 |

Trade payables are non-interest bearing and normally settled on 25-day terms For terms and conditions relating to related parties, refer to Note 31 For the Group's credit risk management process, refer to Note 17

## 24 Deferred income and accruals

| | 2009 | 2008 |
|---|---|---|
| | $000 | $000 |
| Deferred Income | 23,499 | 13 832 |
| Accruals | 22,577 | 18,840 |
| | 46,076 | 32,672 |

Accruals include amounts held payable in joint venture entities of $19 1 million (2008 $7 5 million) For the year 2008, accruals also include items relating to the acquisition of the Dunlin Area Assets ($1 6 million)

Deferred income for the period principally relates to over-lift and under-lift positions associated with the entitlements method of revenue recognition

## 25 Provisions

| For the year ended 2009 | Decommissioning | Deferred payments | Contingent payments | Total |
|---|---|---|---|---|
| | $000 | $000 | $000 | $000 |
| At 1 January 2009 | 318,829 | 975 | 3,451 | 323,255 |
| New or increased provisions | - | 5,979 | - | 5,979 |
| Unwinding of discount | 13,359 | 95 | - | 13,454 |
| Change in parameters | (48,354) | - | - | (48,354) |
| Deletions | - | - | (2,549) | (2,549) |
| Exchange adjustments | - | - | 105 | 105 |
| **At 31 December 2009** | 283,834 | 7,049 | 1,007 | 291,890 |
| Of which | | | | |
| Current | - | 1,614 | 503 | 2,117 |
| Non-current | 283,834 | 5,435 | 504 | 289,773 |

| For the year ended 2008 | Decommissioning | Deferred payments | Contingent payments | Total |
|---|---|---|---|---|
| | $000 | $000 | $000 | $000 |
| At 1 January 2008 | - | 902 | 4,100 | 5,002 |
| New or increased provisions | 306,607 | - | - | 306,607 |
| Unwinding of discount | 9,192 | 73 | 149 | 9,414 |
| Change in discount rate | 3,030 | - | - | 3 030 |
| Exchange adjustments | - | - | (798) | (798) |
| **At 31 December 2008** | 318,829 | 975 | 3,451 | 323,255 |
| Of which | | | | |
| Current | - | 975 | 3,451 | 4,426 |
| Non-current | 318,829 | - | - | 318,829 |

**Decommissioning**

Decommissioning liabilities relate to abandonment provisions acquired as part of the acquisition of Dunlin area fields and associated investment in the Brent System and SVT The Group estimates the future removal costs of offshore oil and gas platforms, production facilities, wells and pipelines at the time of installation of the assets This requires judgemental assumptions regarding removal date, future environmental legislation, the extent of reclamation activities required, the engineering methodology for estimating cost, removal cost, and liability specific discount rates to determine the present value of these cash flows It has been assumed that derogation from the requirement to remove the Dunlin platform concrete gravity base will be granted by the Department of Energy and Climate Change (DECC) at a future point in time Key assumptions adopted are set out in the table below

| Key assumptions | 2009 | 2008 |
|---|---|---|
| Reserves base | Proven and probable | Proven and probable |
| Economic end date of Dunlin fields | 2024 | 2019 |
| Inflation | 2 0% | 2 5% |
| Discount rate | 4 0% | 4 0% |

**Deferred payments**

An earn out payment of $1 million is payable to the former owner of the Crawford field upon attaining a certain level of oil production or the sale of the field subsequent to submitting a development plan with a certain level of reserves being booked

The Group acquired the North West Hutton Area asset on 25 September 2009 for £16 million with £12 million paid during 2009 and a further £4 million payable in two future payments The first payment of £1 million is due at the earlier date of mobilisation of the rig or 31 July 2010 Management believe the rig will not be mobilised before this date The second payment is payable on Step 2 completion which has a back-stop date of 31 December 2012 This component attracts interest from the date of the agreement up to Step 2 completion at the rate of LIBOR plus 1% Management believe completion of Step 2 will occur in November 2011 The value of this second payment is approximately £3 1 million and is discounted using Group's pre-tax lending cost of debt of 6 5%

**Contingent payments**

Contingent payments of $1 0 million at 31 December 2009 relate to the development of the Crawford field with payments triggered in two stages on DBERR approval of the field development plan and first oil

During the year, previously recorded contingent payments relating to the Maureen Area and Crawford fields were derecognised as future payments was no longer deemed probable to the value of $2 7 million This adjustment reduced the carrying value of related intangible assets (refer to Note 13)

## 26 Loans and borrowings

| | Term | Interest rate | 2009 | 2008 |
|---|---|---|---|---|
| | | | $000 | $000 |
| Term loan (Facility "B") | 2013 | LIBOR + 2 5% | **74,349** | 69,046 |
| Revolving credit (Facility "C") | 2016 | LIBOR + 2 5% | **20,000** | 24,309 |
| | | | **94,349** | 93 355 |

Facility "B" is a term loan facility provided by Financial Services North Sea Ltd ("FSNS"), a subsidiary of Mitsubishi Corporation, to Fairfield Betula Limited and Fairfield Fagus Limited The facility is recorded at amortised cost in accordance with IAS 39 repayable from after-tax cash flows, less financing costs 14 days after each quarter end The amortised cost is adjusted at each reporting date to reflect changes in anticipated cash flows Following the full repayment of this facility and the cash collateralization of Facility A discussed below, the provider is entitled to an overriding royalty interest in the future production of Dunlin Area assets ranging between 1% and 2 5% The obligation is determined based on many interrelated assumptions that makes it impractical to disclose the possible effects of changes to these assumptions and other aspects of uncertainty Consequently, it is reasonably possible that outcomes within the next financial year could require a material adjustment to the carrying value of the facility The face value of the loan outstanding at 31 December 2009 was $72 0 million (2008 $72 0 million)

As the facility is payable based on operating cash flows which are variable on, amongst others, the oil price, IAS 1 requires the loan to be classified as a current liability irrespective of the principal repayment dates The facility expires during 2013

Facility C is a revolving $25 million credit facility provided by FSNS to Fairfield Betula Limited The terms of this agreement require this facility to be repaid in full twice a year with a resting period of at least five successive business days The facility expires in 2016

**Decommissioning provisions and guarantees**

Facility "A" is a $273 million decommissioning guarantee facility provided by Guarantee Services North Sea Ltd (a Mitsubishi Corporation subsidiary referred to as "GSNS") to secure the Group's share of the Dunlin Area decommissioning liabilities Facility A, is a guarantee that does not meet the definition of a borrowing under IFRS and consequently is not recorded on the consolidated statement of financial position Facility A incurs a guarantee fee paid quarterly at 3 75% (2008 3 75%)

In the future, the decommissioning letters of credit will be progressively cash collateralised by the Group following the repayment of Facility B with a reduction in the size of the guarantee from GSNS to the letter of credit provider with a corresponding reduction in Facility "A"

The terms of this agreement require this facility to be repaid in full twice a year with a resting period of at least five successive business days The facility expires in 2016

An external review of the Group's decommissioning liabilities was carried out subsequent to the reporting period The impact of this review is set out in Note 34

## 27 Subordinated preference certificates and preference shares

The Group is financed predominantly by debt instruments referred to as investment strips Each investment strip is issued with a nominal value of $10 00 and contains the following two components

- Subordinated preference certificates (SPCs) with an issue price of $9 90, and
- "A" or "B" preference shares with an issue price at $0 10 with nominal value of $0 01 and a share premium of $0 09 Preference shares designated as "A" are held by current or former employees or directors whereas "B" preference shares are issued to institutional holders

### i SPCs

SPCs are valued at amortised cost less directly attributable transaction costs The initial cost allocated to the SPC is determined based on the fair value assigned to the SPC instrument out of the total investment strip SPCs pay an annual coupon of eight percent which is capitalised until the earlier of redemption or the eighth-year anniversary Following the eighth-year anniversary, all outstanding debt attracts an increased coupon interest rate of 14 percent The redemption date has been based on an estimated date of an Initial Public Offering where it is anticipated that the SPC funding will convert into ordinary share capital

The Group concluded that the fair value for 2009 issuances was approximately $9 73 (2008 $9 30) As at 31 December 2009, the estimated conversion date for all SPC instruments was 30 June 2010 (2008 31 December 2011)

| | 2009 Number of shares | 2009 $000 | 2008 Number of shares | 2008 $000 |
|---|---|---|---|---|
| *Initial fair value* | | | | |
| At 1 January | **20,902,008** | **161,115** | 12,861 208 | 86,311 |
| New issues | **10,028,325** | **97,558** | 8,040,800 | 74,804 |
| At 31 December | **30,930,333** | **258,673** | 20,902,008 | 161 115 |
| | | | | |
| *Capitalised interest* | | | | |
| At 1 January | | **41,044** | | 10,705 |
| Capitalised interest for the period | | **50,513** | | 30,109 |
| Unwinding of transaction costs | | **441** | | 230 |
| At 31 December | | **91,998** | | 41,044 |
| | | | | |
| | | **350,671** | | 202,159 |

The increase in carrying value of the SPCs from $202 2 million to $350 7 million is mainly due to the issue of 10,028,325 new shares The interest charge for the period was $50 5 million (2008 $30 1 million) and transaction costs were $441,000 (2008 $230,000) The interest relating to each period is as follows

| | 2009 $000 | 2008 $000 |
|---|---|---|
| 2006/2007 issues discounted at 15% | **18,274** | 15,891 |
| 2008/2009 issues discounted at 10% | **13,845** | 6 184 |
| Impact of redemption date changes | **18,394** | 8,034 |
| Total | **50,513** | 30,109 |

### ii Preference shares

Preference shares hold one vote per share at Board meetings and have an equal right to other ordinary share capital holders to a share of any profit distribution, as if all classes of share constituted one class of share, according to the number of shares held Preference shares will automatically convert to ordinary shares upon the occurrence of the earlier of (a) a listing of the Company's shares and which raises gross proceeds of at least $50 million and (b) when a requisite majority of the preference shareholders requires the Company to so convert

Preference shares are classified as a non-current liability (as opposed to equity) due to a 'down round' protection feature that exists in the terms of the instruments This feature provides a mechanism to adjust the conversion ratio of the preference shares in the event that certain types of shares are issued at a price below the current conversion price (defined under the articles of association as the amount paid to the Company in respect of the allotment and issue of each preference share, including share premium, which is equal to $0 10 per share) Under the mechanism the preference share holder could be compensated for loss in the value of their shares and therefore the risks and rewards of the preference share holders are not aligned to those of a holder of ordinary shares The feature is an embedded derivative and valued in accordance with IAS 39 which has the effect of allocating value between the embedded derivative and the issued preference shares At 31 December 2009, the fair value of this feature is nil (2008 nil)

Authorised preference shares at the end of the reporting period

| | 2009 Number of shares | 2009 $000 | 2008 Number of shares | 2008 $000 |
|---|---|---|---|---|
| A preference shares at nominal value ($0 01 each) | 10,200,800 | 102 | 10,200,800 | 102 |
| B preference shares at nominal value ($0 01 each) | 2,080 000,000 | 20,800 | 2,080,000,000 | 20,800 |
| | **2,090,200,800** | **20,902** | **2,090,200,800** | **20,902** |

Preference shares on issue at the end of the reporting period

| | 2009 Number of shares | 2009 $000 | 2008 Number of shares | 2008 $000 |
|---|---|---|---|---|
| A preference shares at nominal value ($0 01 each) | 130,333 | 1 | 102,008 | 1 |
| A preference share premium ($0 09 each) | As above | 227 | As above | 219 |
| | | | | |
| B preference shares at nominal value ($0 01 each) | 30,800,000 | 308 | 20,800,000 | 208 |
| B preference share premium ($0 09 each) | As above | 48,783 | As above | 46,165 |
| | | | | |
| | **30,930,333** | **49,319** | **20,902,008** | **46,593** |

During the year the Company issued 28,325 (2008 40,800) "A" Preference Shares and 10,000,000 (2008 8,000,000) "B" Preference Shares The fair value assigned to "A" and "B" preference shares was $7,699 (2008 $28,000) and $2 7 million (2008 $5 6 million) respectively

**Return of Capital Rights**

In the event of a return on capital on liquidation (except on a purchase by the Company of any shares) or, unless otherwise agreed by a Requisite Majority of Preference Shareholders (see below), the sale of 50% of the investment strips in the Company to a third party or the sale of substantially all of the Group's business and assets (as more fully defined in the Articles of Association and defined as a Liquidation Event), any proceeds from liquidation shall be distributed in the following order of priority

a) SPCs - payment of capital and unpaid yield

b) Preference Shares - payment of the issue price and any unpaid distributions

c) Ordinary Shares - payment of the issue price and any unpaid distributions

d) Any residual amount shall be distributed amongst the holders of Preference and Ordinary Shares according to the number of shares held

During 2009 additional debt was raised via investment strips amounting to $100 3 million (2008 $80 4 million) Of this amount, $97 5 million (2008 $74 8 million) was assigned to the fair value of the SPCs and $2 8 million (2008 $5 6 million) to the value of preference shares

## 28 Issued capital and reserves

Authorised and fully paid issued capital is as follows

| | 2009 Number of shares | 2009 $000 | 2008 Number of shares | 2008 $000 |
|---|---|---|---|---|
| Founder ordinary shares ($0 01 each) | | | | |
| Authorised | 230,000,000 | 2,300 | 230,000,000 | 2,300 |
| Allotted, called-up and fully paid | 2,300,090 | 23 | 2,300,090 | 23 |
| "A" ordinary shares ($0 01 each) | | | | |
| Authorised | 311,730,800 | 3 117 | 311 730,800 | 3,117 |
| Allotted, called-up and fully paid | - | - | - | - |
| "B" ordinary shares ($0 01 each) | | | | |
| Authorised | 2,080,000,000 | 20,800 | 2,080,000,000 | 20,800 |
| Allotted called-up and fully paid | - | - | - | - |

Reconciliation of movements in equity

| 2009 | Founder shares | Cash flow hedge reserve | Foreign currency translation reserve | Retained deficit | Total equity |
|---|---|---|---|---|---|
| | $000 | $000 | $000 | $000 | $000 |
| At January 2009 | 221 | 62 664 | (12,831) | (71,379) | **(21,325)** |
| Derivative change in value | - | (40,609) | - | - | **(40,609)** |
| Share- based payment | - | - | - | 2,200 | **2,200** |
| Foreign currency | - | - | 4,933 | - | **4,933** |
| Total loss for the period | - | - | - | (64,053) | **(64,053)** |
| | 221 | 22,055 | (7,898) | (133,232) | **(118,854)** |

| 2008 | Founder shares | Cash flow hedge reserve | Foreign currency translation reserve | Retained deficit | Total equity |
|---|---|---|---|---|---|
| | $000 | $000 | $000 | $000 | $000 |
| At January 2008 | 221 | - | (615) | (49 754) | **(50,148)** |
| Derivative change in value | - | 62,664 | - | - | **62,664** |
| Share- based payment | - | - | - | 1,469 | **1,469** |
| Foreign currency | - | - | (12,216) | - | **(12,216)** |
| Total loss for the period | - | - | - | (23,094) | **(23,094)** |
| | 221 | 62,664 | (12,831) | (71,379) | - **(21,325)** |

**Share capital**

Share capital includes the total net proceeds (both nominal value and share premium) on issue of the Company's equity share capital, comprising $0 01 Founder Shares

**Cash flow hedge reserve**

Cash flow hedge reserve comprises the effective portion of the cumulative net change (net of tax) in the fair value of cash flow hedging instruments related to hedged transactions that have not yet occurred

**Foreign currency translation reserve**

The foreign currency translation reserve comprises all foreign currency differences arising from the translation of the financial statements of subsidiary companies which have a different presentation currency to the Group

## 29 Capital management

The primary objective of the Group's capital management is to ensure financial stability, manage financial risks and secure the Group's short-term and long-term need of capital The Group's defines its capital as equity, comprising of shares, SPCs and reserves

The Group manages its capital structure and makes adjustments to it, in light of changes in economic conditions To maintain or adjust the capital structure, the Group calls on cash from its investors in the form of investment strips

The Group manages its short-term capital requirements by producing monthly cash flow forecasts and management accounts and making capital structure adjustments as considered necessary Management of the medium to long-term capital requirements of the Group is monitored by the Board by way of the Annual Budget and 3 year forecast

Through the Subscription and Shareholders' Agreement, the Group's Investors and Founders have committed to provide capital of up to $404 8m by the issuance of Founder Shares, Preference Shares and SPCs of which $300 million was subscribed at the year end (2008 $201 2 million) The $404 8m is made up of an original $201 2m of investment strips and a further $203 6 million (2008 $203 6 million) which was agreed on 12 March 2008 At 31 December 2009 the total of agreed undrawn borrowing facilities was $108 5 million (2008 - $173 5 million) Since the balance sheet date, a further $10 million of capital was subscribed following a capital call notice issued on 12 April 2010

## 30 Share-based payments

### Senior executive and employee share option plan

The Board may grant share options to employees and Directors in accordance with The Fairfield Energy Limited Management Share Option Scheme ("Scheme") The exercise price is set out in the Scheme and varies on the level of capital that Investors have subscribed to in the form of Preference Shares and SPCs in accordance with the Subscription and Shareholders' Agreement ("SSA")

Options granted have standard vesting conditions with twenty percent vesting on the grant date and on each of the following four annual anniversaries a further twenty percent is vested The options have no performance conditions In the event of a liquidation (or similar event), any options which have not yet vested will automatically vest in full and may be exercised immediately prior to (and conditional upon) the occurrence of that event A listing of the Company, unless otherwise determined by the Board, does not accelerate the vesting of the options If any option holder leaves the Company, vested options must be exercised within three months unless employments ceases through death or ill health In these instances, all options vest immediately with an expiry date of 12 months from the grant date The total number of ordinary share options that can be issued cannot exceed 15% of the issued preference shares at any time All options granted are equity-settled

### Expense and movements during the year

The expense arising from equity-settled share based payments during the year was $1,976,000 (2008 $1,395,000) The expense arising from cash-based settlements totalled $224,000 (2008 $74,000)

A reconciliation of the options on issue is set out in the table below

| | 2009 | 2009 | 2008 | 2008 |
|---|---|---|---|---|
| | Number of shares | Option value ($/share) | Number of shares | Option value ($/share) |
| Outstanding at 1 January | | | | |
| Exercise price $5 00 | 1,408,700 | - | 825,000 | - |
| Exercise price $12 00 | 589,500 | - | 75,000 | - |
| Granted during the year | | | | |
| February 2008 - Exercise price $5 00 | - | - | 108,900 | 8 87 |
| December 2008 - Exercise price $5 00 | - | - | 474,800 | 1 41 |
| December 2008 - Exercise price $12 00 | - | - | 514,500 | 1 03 |
| July 2009 - Exercise price $5 00 | 914,450 | 1 73 | - | - |
| July 2009 - Exercise price $12 00 | 1,034,850 | 1 21 | - | - |
| Outstanding at 31 December | 3,947,500 | - | 1,998,200 | - |
| Exercisable at 31 December | 1,444,140 | - | 654,640 | - |

The Group is an unlisted entity and consequently does not have a recognised market price for its ordinary shares or historic share price volatility data which can readily be determined for use within option pricing models An independent actuary has measured the fair value of the options using a binomial pricing model taking into account the terms and conditions upon which the instruments were issued The maximum term of the options granted is ten years

The weighted average remaining contractual life of options granted during the year was 9 5 years (2008 9 2 years) The weighted average fair value of options granted during the year was $1 45 (2008 $1 97)

The following table lists the inputs to the models used for the plan for the year ended 31 December

| | 2009 | 2008 |
|---|---|---|
| Implied equity value ($) | 3 16 | 2 50 |
| Share return volatility (%) | 100 | 100 |
| Dividend yield (%) | - | - |
| Comparable group share volatility (%) | 45 to 79 | 50 to 65 |
| Risk-free interest rate (%) | 2 6 | 1 6 to 3 1 |
| Expected life of share options (years) | 3 to 3 5 | 3 to 3 5 |

The expected life of share options is based on current expectations and is not necessarily indicative of exercise patterns that may occur

## 31 Pensions and other post-retirement benefits

The Group contracts out to recognised personal pension schemes which are defined contribution schemes The expense charged to the Income Statement for the period amounted to

| | 2009 $000 | 2008 $000 |
|---|---|---|
| Pension costs expensed to the income statement | 1,201 | 1,203 |

## 32 Related party disclosures

### a) Equity interests

The financial statements include the financial statements of the Group and the subsidiaries listed in the following table

| Name | Country of Incorporation | % Equity Interest 2009 | 2008 |
|---|---|---|---|
| Fairfield Energy Limited | England | 100% | 100% |
| Fairfield Energy Holdings Limited | England | 100% | 100% |
| Fairfield Acer Limited | England | 100% | 100% |
| Fairfield Betula Limited | England | 100% | 100% |
| Fairfield Cedrus Limited | England | 100% | 100% |
| Fairfield Fagus Limited | England | 100% | 100% |

### b) Transactions with related parties

Apart from transactions relating to SPCs, preference shares and key management personnel compensation, there were no transactions with related parties during the year ended 31 December 2009

### c) The ultimate parent

Fairfield Energy Limited is the ultimate parent entity within the Group Company financial statements follow the Consolidated financial statements on pages 43 to 53

### d) Entity with significant influence over the Group

At 31 December 2009 by virtue of a 36% (2008 36%) shareholding, the only entity with significant influence was Warburg Pincus LLC

### e) Joint venture in which the Group is a venturer

Joint venture relationships are disclosed in Note 16

### i Compensation of key management personnel

IAS 24 defines key management personnel as those persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any director (whether executive or otherwise) of that entity The key management personnel of the Group is considered to be the directors Key management compensation is listed in the following table

| | 2009<br>$000 | 2008<br>$000 |
|---|---|---|
| Short-term benefits | 722 | 876 |
| Post-employment benefits | 67 | 63 |
| Termination benefits | - | - |
| Share-based payments | 619 | 261 |
| Total | 1,408 | 1,200 |

Mark Francis McAllister is the only director accruing pension benefits under the defined contribution plan

### ii Directors' interests in the Senior Executive Plan

All staff and employees are members of the same Share Option Scheme Refer to Note 30 for additional information

For the year ended 31 December 2009, the highest paid Director was Mark Francis McAllister with a total remuneration of $463,000 (2008 - $483,000)

## 33 Commitments, contingencies and guarantees

### Capital and other commitments

At 31 December 2009, the Group was party to gross capital and other commitments of $25 9 million (2008 $25 5m) These commitments include both capital and operating contractual obligations

### Contingencies

The Group does not have any contingent liabilities other than the contingent liabilities recorded in the Group's statement of financial position as described in Note 25 as at 31 December 2009 In 2008, the Group had a commitment to pay approximately £3 1 million upon first oil production from the Maureen Field However, in 2009 this field was deemed a dry well and subsequently impaired As a result it is improbable that this commitment will be payable by the Group

### Guarantees

At 31 December 2009 the Group had the following guarantees

a) A letter of credit with Esso Exploration and Production UK Limited to safeguard them as co-owners of Sullom Voe Terminal, in the event that the Group overlifts from the terminal and is subsequently unable to repay the resulting value of the oil This is recorded as cash on hand

b) A letter of credit provided to secure the Group's decommissioning liabilities with the Dunlin area fields (refer to Note 25)

The above-listed guarantees were also in place at 31 December 2008

## 34 Events after the reporting period

During the first half of 2010, the Company entered into its annual review of its decommissioning liabilities in accordance with the decommissioning cost provision deed (DCPD) held with the former owners of the Dunlin Area Assets The review involves an independent expert evaluating the present value of its future decommissioning costs associated with the Dunlin Area which forms the basis of the level of security Fairfield is required to hold in respect of the future remediation costs The preliminary findings of the expert indicate a present cost of the future works of $510 million, in line with the estimate assumed for the decommissioning liabilities recorded on the Group's Statement of Financial Position (refer to Note 25) Although this review is not expected to be finalised until the end of June 2010, the Company signed an agreement to make available additional security of $77 million in 2010 in order to provide certainty over the cash security required The security will be cash collateralised from additional debt facilities At 31 December 2009, the Company has a letter of credit facility of $273 million in place to cover its future decommissioning costs (refer to Note 26)

On 12 April 2010, a further capital call to subordinated preference certificate and preference share holders was completed giving rise to the subscription of an additional $10 0 million

The Group repaid $18 6 million on 14 January 2010 and $2 3 million on 14 April 2010 of its term loan Facility B

# Statement of directors' responsibilities for the Company financial statements

The Directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable United Kingdom law and those International Financial Reporting Standards (IFRSs) as adopted by the European Union

The Directors are required to prepare financial statements for each financial year which present fairly the financial position, financial performance and cash flows of the Company for that period In preparing those financial statements, the Directors are required to

- Select suitable accounting policies and then apply them consistently,
- Present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information,
- Provide additional disclosures when compliance with the specific requirements in IFRSs is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance, and
- State that the Company has complied with IFRSs, subject to any material departures disclosed and explained in the financial statements

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 2006 They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities

The Directors confirm that they have complied with these requirements and, having a reasonable expectation that the Company have adequate resources to continue in operational existence for the foreseeable future, will continue to adopt the going concern basis in preparing the accounts

Having made the requisite enquiries, so far as the directors are aware, there is no relevant audit information (as defined by Section 418(3) of the Companies Act 2006) of which the Company's auditors are unaware, and the directors have taken all the steps they ought to have taken to make themselves aware of any relevant audit information and to establish that the Company's auditors are aware of that information

Mark McAllister
Chief Executive Officer
Date 4 June 2010

# Independent auditor's report

**TO THE MEMBERS OF FAIRFIELD ENERGY LIMITED**

We have audited the parent company financial statements of Fairfield Energy Limited for the year ended 31 December 2009 which comprise the Company Income Statement, the Company Statement of Comprehensive Income, Company Statement of Financial Position, the Company Statement of Changes in Equity, the Company Statement of Cash Flows and the related notes 1 to 18 The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006 Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed

**Respective responsibilities of directors and auditors**

As explained more fully in the Directors' Responsibilities Statement set out on page 41, the directors are responsible for the preparation of the parent company financial statements and for being satisfied that they give a true and fair view Our responsibility is to audit the parent company financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland) Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors

**Scope of the audit of the financial statements**

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error This includes an assessment of whether the accounting policies are appropriate to the parent company's circumstances and have been consistently applied and adequately disclosed, the reasonableness of significant accounting estimates made by the directors, and the overall presentation of the financial statements

**Opinion on financial statements**

In our opinion the parent company financial statements

- Give a true and fair view of the state of the Company's affairs as at 31 December 2009 and of its loss for the year then ended,
- Have been properly prepared in accordance with IFRSs as adopted by the European Union, and
- Have been prepared in accordance with the requirements of the Companies Act 2006

**Opinion on other matters prescribed by the Companies Act 2006**

In our opinion the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the parent company financial statements

**Matters on which we are required to report by exception**

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion

- Adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us, or
- The parent company financial statements are not in agreement with the accounting records and returns, or
- Certain disclosures of directors' remuneration specified by law are not made, or
- We have not received all the information and explanations we require for our audit

**Other matter**

We have reported separately on the Group financial statements of Fairfield Energy Limited for the year ended 31 December 2009

Ken Williamson (Senior statutory auditor)
for and on behalf of Ernst &Young LLP, Statutory Auditor
London
4 JUNE 2010

# Company income statement

for the year ended 31 December

| | Notes | 2009 $000 | 2008 $000 |
|---|---|---|---|
| Revenue | | - | - |
| Cost of sales | | - | (5) |
| **Gross (loss)** | | - | (5) |
| Administrative expenses | | (25,523) | (21,385) |
| Other operating income | 4i | 22,067 | 16,301 |
| **Operating (loss)** | | (3,456) | (5,089) |
| Finance income | 4iii | 8,845 | 1,060 |
| Finance costs | 4iv | (50,981) | (56,363) |
| **(Loss) from operations before tax** | | (45,592) | (60,392) |
| Income tax expense | 5 | - | - |
| **(Loss) after tax** | | (45,592) | (60,392) |

# Company statement of comprehensive income

for the year ended 31 December

| | Notes | 2009 $000 | 2008 $000 |
|---|---|---|---|
| **(Loss) for the period** | | (45,592) | (60,392) |
| Other comprehensive income | | - | - |
| Other comprehensive income, net of tax | | - | - |
| **Total comprehensive income** | | (45,592) | (60,392) |

# Company statement of financial position

as at 31 December

| | Notes | 2009<br>$000 | 2008<br>$000 |
|---|---|---|---|
| **Non-current assets** | | | |
| Property, plant and equipment | 6 | 891 | 1,277 |
| Intangible assets | 7 | 827 | 125 |
| Investments | 8 | 8,743 | 8,743 |
| Intercompany loans | 9 | 254,243 | 148,742 |
| | | **264,704** | **158,887** |
| **Current assets** | | | |
| Trade and other receivables | 9 | 8,882 | 4,803 |
| Prepayments and accrued income | | 575 | 430 |
| Cash and short-term deposits | 10 | 5,542 | 14,393 |
| | | **14,999** | **19,626** |
| ***Total assets*** | | **279,703** | **178,513** |
| **Non-current liabilities** | | | |
| Subordinated preference certificates | 13 | 350,671 | 202,159 |
| Preference shares | 13 | 49,319 | 46,593 |
| | | **399,990** | **248,752** |
| **Current liabilities** | | | |
| Trade and other payables | 11 | 2,469 | 9,608 |
| Deferred income and accruals | | 2,363 | 1,905 |
| Provisions | 12 | 1,000 | 975 |
| | | **5,832** | **12,488** |
| **Total liabilities** | | **405,822** | **261,240** |
| **NET (LIABILITIES)** | | **(126,119)** | **(82,727)** |
| **Equity** | | | |
| Founder shares | 14 | 23 | 23 |
| Founder share premium | 14 | 198 | 198 |
| Retained deficit | 14 | (126,340) | (82,948) |
| **TOTAL EQUITY** | | **(126,119)** | **(82,727)** |

Mark McAllister
Chief Executive Officer
Date 4 June 2010

# Company statement of changes in equity

for the year ended 31 December

| | Notes | Founder shares $000 | Founder share premium $000 | Retained deficit $000 | Total $000 |
|---|---|---|---|---|---|
| **At 1 January 2009** | | 23 | 198 | (82,948) | **(82,727)** |
| Total comprehensive income | | - | - | (45,592) | **(45,592)** |
| Transactions with owners, recorded directly in equity | | | | | |
| Share-based payment transactions | 14 | - | - | 2,200 | **2,200** |
| **Balance at 31 December 2009** | **14** | **23** | **198** | **(126,340)** | **(126,119)** |

for the year ended 31 December

| | Notes | Founder shares $000 | Founder share premium $000 | Retained deficit $000 | Total $000 |
|---|---|---|---|---|---|
| **At 1 January 2008** | | 23 | 198 | (24,025) | **(23,804)** |
| Total comprehensive income | | - | - | (60,392) | **(60,392)** |
| Transactions with owners, recorded directly in equity | | | | | |
| Share-based payment transactions | 14 | - | - | 1,469 | **1,469** |
| **Balance at 31 December 2008** | **14** | **23** | **198** | **(82,948)** | **(82,727)** |

# Company statement of cash flows

for the year ended 31 December

| | Notes | 2009 $000 | 2008 $000 |
|---|---|---|---|
| **Operating activities** | | | |
| (Loss) / Profit before tax | | (45,592) | (60,392) |
| *Adjustments for* | | | |
| Depreciation and amortisation | 4ii | 745 | 766 |
| Discount unwind | | 25 | - |
| Share-based payments | | 2,200 | 1,469 |
| SPC interest expense | 4iv | 50,954 | 30,339 |
| Net finance costs | | (76) | 19,285 |
| *Working capital adjustments* | | | |
| (Increase) / decrease in trade and other receivables | | (4,125) | 11,804 |
| (Increase) / decrease in prepayments and accrued income | | (145) | - |
| Increase / (decrease) in trade and other payables | | (6,637) | 6,629 |
| **Net cash inflow from operating activities** | | **(2,651)** | **9,900** |
| **Investing activities** | | | |
| Interest received | | 78 | 1,040 |
| Expenditure on property, plant and equipment | | (304) | (944) |
| Expenditure on intangible assets | | (757) | (74) |
| Increase in intercompany receivables | | (105,501) | (96,373) |
| **Net cash outflow from investing activities** | | **(106,484)** | **(96,351)** |
| **Financing activities** | | | |
| Proceeds from issue of preference shares | | 2,726 | 5,604 |
| Proceeds from issue of SPCs | | 97,558 | 74,804 |
| **Net cash inflow from financing activities** | | **100,284** | **80,408** |
| **Increase in cash and cash equivalents** | | **(8,851)** | **(6,043)** |
| Net foreign exchange difference | | - | - |
| Cash and cash equivalents at beginning of the period | | 14,393 | 20,436 |
| **Cash and cash equivalents at the end of the period** | 10 | **5,542** | **14,393** |

## Notes to the Company financial statements

### 1 Significant accounting policies

**a) Reporting entity**
Fairfield Energy Limited is principally engaged in administering the Group's activities in the appraisal, development and production of hydrocarbon accumulations The financial statements for the year ended 31 December were authorised for issue in accordance with a resolution of the directors on 29 April 2010 The Company is a limited company incorporated and domiciled in England and Wales The registered office is located at Ash House, Staines, Middlesex, United Kingdom

**b) Basis of preparation**
The financial statements of the Company for the year ended 31 December 2009 have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union (EU) and as applied in accordance with the provisions of the Companies Act 2006 The accounting policies adopted are consistent with those applied in the financial statements for the year ended 31 December 2008 Certain reclassifications of prior year disclosures have been made to increase comparability and understandability of the financial statements These are set out in Note 3

**c) Statement of compliance**
The financial statements of the Company have been prepared in accordance with International Financial Reporting Standards (IFRS) and adopted by the EU

**d) Basis of measurement**
The financial statements have been prepared under the historical cost convention except for certain financial assets and liabilities that have been measured at fair value

**e) Presentation and functional currencies**
The financial statements are presented in United States dollars, which is also the Company's functional currency The financial statements are rounded to the nearest thousand ($000) unless stated otherwise

**f) Foreign currency translation**
Transactions in foreign currencies are initially recorded by the Company in US dollars at the spot exchange rate Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency spot rate of exchange ruling at the reporting date

**g) Property, plant and equipment**
Plant and equipment is stated at cost, net of accumulated depreciation and any provisions for impairment, if any Depreciation is calculated on a straight-line basis over the estimated useful life of the asset as follows

| | |
|---|---|
| IT equipment | 3 years |
| Furniture and fittings | 3 years |
| Software | 3 years |

**g) Intangible assets**
Intangible assets are measured on initial recognition at cost and carried net of accumulated depreciation Gains or losses arising from de-recognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in the income statement when the asset is derecognised Depreciation is calculated on a straight-line basis over an estimated useful life of 3 years

**h) Investments**
Investments are initially recognised at the cost of acquisition and carried net of accumulated depreciation and any provisions for impairment. The assets are amortised based on units of production

**i) Trade and other receivables**
Trade and other receivables, including receivables from related parties, are initially recognised at fair value and subsequently measured at amortised cost less an allowance for uncollectable amounts Collectability and impairment are assessed on a regular basis Subsequent recoveries of amounts previously written off are credited against other expenses in the income statement

**j) Provisions and contingencies**
Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects, where appropriate, the risks specific to the liability Where discounting is used, the increase in the provision due to the passage of time is recognised as a finance cost

A contingent liability is disclosed where the existence of an obligation will only be confirmed by future events or where the amount of the obligation cannot be measured reliably except where the contingent liability results as part of a business combination

**k) Subordinated Preference Certificates (SPC) and convertible preference shares**
The Company issues financial instruments referred to as investment strips These instruments are required to be accounted for as financial liabilities under IAS 39 Each investment strip contains two components SPCs and "A" or "B" preference shares The SPCs are measured at amortised cost The difference between the net proceeds and amortised cost equate to the preference share value Refer to Note 12 for further detail

**l) Share-based payment transactions**

Employees (including senior executives) and Directors of the Group receive remuneration in the form of share-based payment transactions, whereby employees render services as consideration for equity instruments ('equity-settled transactions')

*Equity settled transactions*

The cost of equity settled transactions with employees and Directors are measured by reference to the fair value at the date at which they are granted and are recognised as an expense over the vesting period, which ends on the date on which the relevant holders become fully entitled to the award Fair value is determined by an independent external valuer using an appropriate pricing model In valuing equity-settled transactions, no account is taken of any vesting conditions, other than conditions linked to the price of the shares of the Company (market conditions)

No expense is recognised for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition, which are treated as vesting irrespective of whether or not the market condition is satisfied, provided that all other performance conditions are satisfied

Forfeiture as defined in IFRS 2 and the specific conditions of the Group's share based payments refers to the failure to satisfy vesting conditions other than market conditions The fair values determined by the independent valuer do not make any advance allowance for employees leaving service before the vesting date and forfeiting their options However, where employees leave before vesting, the expenses in the relevant period reflect the actual experience of leavers before vesting

At each balance sheet date before vesting, the cumulative expense is calculated, representing the extent to which the vesting period has expired and the management's best estimate of the achievement or otherwise of non-market conditions number of equity instruments that will ultimately vest or in the case of an instrument subject to a market condition, be treated as vesting as described above The movement in cumulative expense since the previous balance sheet date is recognised in the income statement, with a corresponding entry in equity

**m) Financial instruments**
*Loans and other receivables*
Trade receivables, loans and other receivables that have fixed or determinable payments that are not quoted on an active market are classified as loans and receivables Loans and receivables are measured at amortised cost using the effective interest method less any impairment Trade and other receivables are recognised when invoiced

*Bank deposits*
Bank deposits with an original maturity of over three months are held as a separate category of current asset and presented on the face of the statement of financial position

*Cash and cash equivalents*
Cash and short-term deposits in the statement of financial position comprise cash at bank and on hand, restricted cash holdings (cash held in joint ventures and escrow accounts) and short-term deposits with an original maturity of three months or less

*Trade payables and other non derivative financial liabilities*
Trade payables and other creditors are non-interest bearing and are measured at cost.

**n) Deferred Income tax**

*Deferred income tax*
Deferred income tax is recognised on temporary differences arising between the tax base of assets and liabilities and their carrying amounts in the consolidated financial statements

A deferred income tax liability is not recognised if a temporary difference arises on initial recognition of an asset or liability in a transaction (other than a business combination), that at the time of the transaction, affects neither, accounting nor taxable profit or loss

Deferred income tax assets are recognised to the extent that it is probable that future income tax profit will be available against which the temporary differences can be utilised

Deferred income tax is provided on temporary differences arising on investments in subsidiaries, jointly controlled entities and associates, except where the timing of the temporary difference can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future

Deferred tax assets and liabilities are measured based on tax rates and laws enacted or substantively enacted at the statement of financial position date Deferred tax liabilities may be offset against deferred tax assets within the same tax entity and tax jurisdiction Measurement of deferred tax liabilities and assets reflect the tax consequences expected to arise from the manner in which the asset or liability is recovered or settled

**o) Pension and other post-employment benefits**

The Company operates a defined contribution pension scheme Amounts payable to the pension plan are charged to the income statement in the same period in which the services have been rendered by the employees

## 2 Critical accounting judgements

**a) Critical judgements in applying the Company's accounting policies**

**i SPCs and preference shares**

SPCs and preference shares are funding instruments sourced from private equity The value of these instruments is based on estimated future cash flows and are impacted by the expected conversion date As at the balance sheet date, the Company has made the judgment that conversion will occur on the expected Initial Public Offering date, May 2010

## 3 Reclassifications

### i Reclassifications

The Company has made certain reclassifications to the presentation set out within in its 2008 financial statements to assist users of its financial statements Significant reclassifications are described below

*Company Income Statement*

- Foreign exchange gains and losses – Realised and unrealised foreign exchange gains and losses have been reclassified from administrative expenses to either finance income or finance costs This reclassification has been made to help users of the accounts to better understand changes to administrative expenses by removing fluctuations caused only by foreign exchange The impacts of these changes are disclosed in notes 4iv and 4v, and
- Intracompany revenues generated from the recharging of labour costs have been eliminated against the appropriate line items within administrative expense The impact of this change was to reduce other income and reduce administrative costs by $2 3 million

*Company Statement of Financial Position*

- Prepayments and accrued income, and deferred income and accruals – The Company has disaggregated these current assets and current liabilities from trade and other receivables and trade and other payables respectively, to be consistent with the presentation of the Group Statement of Financial Position The impact of these changes on the Company financial statements can be identified on the face of the Statement of Financial Position and within notes 9 and 11

*Company Statement of Cash Flows*

- Grouping of similar items – The number of line items on the Statement of Cash Flows has been reduced by grouping similar items together This principle has been applied to finance income and finance cost items and depreciation and amortisation

### ii Other presentation changes

Certain presentational changes have been made to assist users of the financial statements These changes include

- The Company accounts of Fairfield Energy Limited have been presented separately following the consolidated financial statements to simplify the presentation of the accounts, and
- A Statement of Comprehensive Income has been prepared in accordance with to the revised International Accounting Standard IAS 1 The presentation of this statement impacts the presentation of the statement of changes in equity The impacts of these changes can be seen on the face of the respective financial statements

## 4. Other income / expenses

### i Other operating income

| | 2009 | 2008 |
|---|---|---|
| | $000 | $000 |
| Joint venture recoveries | 15,348 | 9,729 |
| Other income | 6,719 | 6,572 |
| **Total other operating income** | **22,067** | 16,301 |

### ii Depreciation, depletion and amortisation

| | 2009 | 2008 |
|---|---|---|
| | $000 | $000 |
| Included in administrative expenses | | |
| Amortisation of intangible assets | 55 | 42 |
| Depreciation of property, plant and equipment | 690 | 724 |
| **Total depreciation, depletion and amortisation** | **745** | 766 |

### iii Finance income

| | 2009 | 2008 |
|---|---|---|
| | $000 | $000 |
| Interest income | 78 | 1 060 |
| Foreign exchange gains | 8,767 | - |
| **Total finance income** | **8,845** | 1,060 |

### iv Finance costs

| | 2009 | 2008 |
|---|---|---|
| | $000 | $000 |
| Interest on loans and other finance costs | 2 | 14 |
| Interest on SPCs (See Note 26) | 50,954 | 30 339 |
| Discount unwinding | 25 | 72 |
| Amortisation of SPC transaction costs (Note 26) | - | - |
| Foreign exchange losses | - | 25,938 |
| **Total finance costs** | **50,981** | 56,363 |

### v Auditors' remuneration

Fees payable to the Company's auditors for the audit of the Company's financial statements were $318,423 (2008 $527,615) Remuneration receivable by the Company's auditors for the supply of other services to the Company is not presented in the Company financial statements as this information is provided in the consolidated financial statements

**vi Employee benefits expense**

| | 2009 $000 | 2008 $000 |
|---|---|---|
| Wages and salaries | 6,781 | 7,191 |
| Bonuses | 1,013 | 1,110 |
| Social security costs | 1,079 | 1,007 |
| Pension costs | 1,201 | 1,203 |
| Insurance (medical and life) | 2 | 167 |
| Share-based payments | 1,582 | 1,469 |
| | 11,658 | 12,147 |
| **Average number of employees** | | |
| Directors | 2 | 2 |
| Finance and administration | 19 | 13 |
| Technical | 28 | 27 |
| | 49 | 42 |

Additional information regarding the remuneration of key management is set out in Note 32vi

## 5 Income tax

The major components of income tax expense for the years ended 31 December 2009 and 2008 are

### i Income statement

There was no income tax charge for the years ended 31 December 2009 and 2008

### ii Statement of comprehensive income

There were no deferred tax items charged directly or credited within equity for the years ended 31 December 2009 and 2008

A reconciliation between tax expense and the product of accounting profit multiplied by the UK standard income tax rate for the year ended 31 December 2009 is as follows

| | 2009 $000 | 2008 $000 |
|---|---|---|
| Accounting loss before income tax | (45,592) | (60,392) |
| Accounting loss multiplied by the UK standard rate of corporation tax of 28% (Group) | (12,767) | (17,212) |
| Expenditure not deductible for tax purposes | 14,297 | 8,816 |
| Non-taxable income | (1,800) | - |
| Benefit of previously unrecognised temporary differences | (950) | - |
| Temporary differences not recognised | 710 | 553 |
| Losses carried forward not recognised | - | 7,774 |
| Group relief for no consideration | 510 | 69 |
| | - | - |

The Company has tax losses of $17 9 million (2008 $35 8 million) which arose in the UK and available indefinitely for offset against future taxable profits of the Company Deferred tax assets have not been recognised in respect of these losses as they are not expected to offset taxable profits in the Company in the foreseeable future The above has been adjusted for amounts relating to share based payments

## 6 Property, plant and equipment

Property, plant and equipment held by the Company is disclosed in Note 12 of the consolidated financial statements

## 7 Intangible assets

| | Website costs $000 | Software $000 | Total $000 |
|---|---|---|---|
| **Year ended 31 December 2009** | | | |
| Net carrying amount at 1 January 2009 | 125 | - | 125 |
| Additions | - | 757 | 757 |
| Amortisation and impairment charge | (55) | - | (55) |
| **Carrying amount at 31 December 2009** | 70 | 757 | 827 |
| **At 31 December 2009** | | | |
| Historical cost | 167 | 757 | 924 |
| Accumulated amortisation | (97) | - | (97) |
| Net carrying amount | 70 | 757 | 827 |
| **Year ended 31 December 2008** | | | |
| Net carrying amount at 1 January 2008 | 93 | - | 93 |
| Additions | 74 | - | 74 |
| Amortisation and impairment charge | (42) | - | (42) |
| **Carrying amount at 31 December 2008** | 125 | - | 125 |
| **At 31 December 2008** | | | |
| Historical cost | 167 | - | 167 |
| Accumulated amortisation | (42) | - | (42) |
| Net carrying amount | 125 | - | 125 |

## 8 Investments

| | 2009 $000 | 2008 $000 |
|---|---|---|
| Investments in subsidiaries | 8,743 | 8,743 |
| Carrying amount at 31 December | 8,743 | 8,743 |

Investments in which the Company holds 20% or more of the nominal value of any class of share capital are as follows

| Name of subsidiary | Holding | % of voting rights and shares held | Nature of business |
|---|---|---|---|
| Fairfield Energy Holdings Limited | Ordinary shares | 100% | Holding company |
| Fairfield Acer Limited | Ordinary shares | 100% | Oil and gas exploration |
| Fairfield Betula Limited | Ordinary shares | 100% | Oil and gas exploration |
| Fairfield Cedrus Limited | Ordinary shares | 100% | Oil and gas exploration |
| Fairfield Fagus Limited | Ordinary shares | 100% | Oil and gas exploration |

All subsidiaries are incorporated and operating in the UK The Company accounts for its investments in subsidiaries using the cost model

## 9. Trade and other receivables

| | 2009 | 2008 |
|---|---|---|
| Current | $000 | $000 |
| Trade and other receivables | 8,694 | 4,480 |
| VAT receivable | 188 | 323 |
| | 8,882 | 4,803 |
| | | |
| Non-current | | |
| Loans receivable from inter-group entities | 254,243 | 148,742 |
| | 254,243 | 148,742 |

## 10. Cash and short-term deposits

| | 2009 $000 | 2008 $000 |
|---|---|---|
| Cash at bank and in hand | 5,542 | 14 393 |
| | 5,542 | 14,393 |

## 11 Trade and other payables

| | 2009 $000 | 2008 $000 |
|---|---|---|
| Trade payables | 2,036 | 9,296 |
| Other payables | 433 | 312 |
| | 2,469 | 9,608 |

## 12 Provisions

| | 2009 $000 | 2008 $000 |
|---|---|---|
| Net carrying amount at 1 January | 975 | 902 |
| New or increased provisions | - | - |
| Unwinding of discount | 25 | 73 |
| | 1,000 | 975 |

**Deferred payments**

An earn out payment of $1 million is payable to the former owner of the Crawford Field upon attaining a certain level of oil production, upon the sale of the field or when a certain level of oil reserves are booked on a proved and probable basis

## 13 Subordinated preference certificates and preference shares

The Subordinated preference certificates and preference shares of the Company match those disclosed under the Group accounts See Note 27 on page 36 of the consolidated financial statements for further details

## 14 Issued capital and reserves

Authorised and fully paid issued capital is as follows

| | 2009 Number of shares | 2009 $000 | 2008 Number of shares | 2008 $000 |
|---|---|---|---|---|
| Founder ordinary shares ($0 01 each) | | | | |
| Authorised | 230,000,000 | 2,300 | 230,000,000 | 2,300 |
| Allotted, called-up and fully paid | 2,300,090 | 23 | 2,300,090 | 23 |

Reconciliation of movements in equity

| 2009 | Founder shares $000 | Retained deficit $000 | Total equity $000 |
|---|---|---|---|
| At January 2009 | 221 | (82,948) | (82,727) |
| Share- based payment | - | 2,200 | 2,200 |
| Total loss for the period | - | (45 592) | (45,592) |
| | 221 | (126,340) | (126,119) |

| 2008 | Founder shares $000 | Retained deficit $000 | Total equity $000 |
|---|---|---|---|
| At January 2008 | 221 | (24,025) | (23,804) |
| Share- based payment | - | 1,469 | 1,469 |
| Total loss for the period | - | (60,392) | (60,392) |
| | 221 | (82,948) | (82,727) |

Share-based payments of the Company match those disclosed under the Group accounts See Note 30 on page 38 of the consolidated financial statements for further details

## 15 Financial assets and liabilities

### a) Fair value of financial assets and liabilities

Management believes that for all financial assets and liabilities, other than the SPCs, that the carrying amount of the assets and liabilities equates their fair value Set out below is a comparison by category of carrying amounts and fair values of all of the Company's financial instruments that are carried in the financial statements

| | Carrying Amount | | Fair Value | |
|---|---|---|---|---|
| | 2009 | 2008 | 2009 | 2008 |
| | $000 | $000 | $000 | $000 |
| *Financial liabilities* | | | | |
| Trade and other payables | 2,469 | 9,608 | 2,469 | 9,608 |
| Deferred income and accruals | 2,361 | 1,905 | 2,361 | 1,905 |
| Provisions (current) | 1,000 | 975 | 1 000 | 975 |
| SPCs | 350,671 | 202,159 | 353,212 | 220,200 |
| Preference shares | 49,319 | 46,593 | 244,350 | 129,592 |
| | | | | |
| *Financial assets* | | | | |
| Trade and other receivables | 3,886 | 4 803 | 3,886 | 4 803 |
| Prepayments and accrued income | 575 | 430 | 575 | 430 |
| Cash and short-term deposits | 5 542 | 14,393 | 5,542 | 14,393 |

### b) Credit risk

The Company's income principally comes in the form of recharges to joint venture partners Credit risk associated with this relationship is managed within the framework of the Joint Operating Agreements by committing to spending on projects when the funds from all operators are already in place

The Company may have significant cash balances arising from capital calls and its operating activities at any particular time Cash is maintained on deposit with the Royal Bank of Scotland

The Company's maximum exposure to credit risk is limited to the carrying value of financial assets as disclosed in Note 15(a)

### c) Currency exposure

i *Exposure to currency risk*

The Company's statement of financial position and income statement are affected by movements in USD/GBP exchange rates Currency exposure arises from sales or purchases in currencies other than functional currency At present, the Company has not engaged in hedging transactions to eliminate exposure to these risks The Company's exposure to foreign currency is as follows

| | 2009 | 2008 |
|---|---|---|
| | £000 | £000 |
| Cash and short-term deposits | **4,513** | 14,211 |
| Trade receivables | **4,168** | 677 |
| Trade payables | **(2,786)** | (284) |
| Net exposure | **5,895** | 14,604 |

The following significant exchange rates applied during the year

| | Average rate 2009 | 2008 | Reporting date spot rate 2009 | 2008 |
|---|---|---|---|---|
| USD GBP | 0 6391 | 0 5367 | 0 6198 | 0 6919 |

ii *Sensitivity analysis*

The following table demonstrates the sensitivity to a reasonably possible change in the Sterling exchange rate, with all other variables held constant, of the Company's profit before tax (due to movement in the foreign exchange component of costs)

| | Increase / decrease in £ US$ rate | Increase / (decrease) on lost before tax $000 |
|---|---|---|
| 2009 | +10% | (951) |
| | -10% | 951 |
| 2008 | +10% | (2,356) |
| | -10% | 2,356 |

***Methods and assumptions***

Sensitivity analysis was performed by applying a percentage increase/decrease to components of profit and loss which were denominated in currency other than functional currency The 10% level of change was considered to be realistic based upon the rates exhibited over the period

### d) Interest rate risk management

Financial instruments exposed to interest rate risk include loan facilities B and C (linked to LIBOR) and cash held on deposit (interest bearing accounts at market rates) SPCs, have a fixed annual rate of interest of 8% for the first 7 years and 14% thereafter and therefore are not affected by external changes in interest rates

The Company's exposure to interest rate risk and sensitivity analysis on a change of 100 basis points in interest rates on balances of which interest is charged at 31 December 2009 is set out below

| Interest rate risk exposures 31 December 2009 | Floating interest rate $000 | Fixed interest rate $000 | Total $000 | Sensitivity Analysis Profit and Loss 100 Bp increase $000 | 100 bp decrease $000 | Equity 100 bp increase $000 | 100 bp decrease $000 |
|---|---|---|---|---|---|---|---|
| Financial assets | | | | | | | |
| Cash | 5,542 | - | 5,542 | (55) | 55 | - | - |
| **Net financial assets/(liabilities)** | **5,542** | **-** | **5,542** | | | | |

| Interest rate risk exposures 31 December 2008 | Notes | Floating interest rate $000 | Fixed interest rate $000 | Total $000 | Sensitivity Analysis Profit and Loss 100 bp increase | 100bp decrease | Equity 100bp increase | 100 bp decrease |
|---|---|---|---|---|---|---|---|---|
| Financial assets | | | | | | | | |
| Cash | | 14,393 | - | 14,393 | (144) | 144 | - | - |
| **Net financial assets/(liabilities)** | | **14,393** | **-** | **14,393** | | | | |

### e) Liquidity risk management

The Company currently relies on drawing capital from its shareholders and investors to manage its funding requirements The annual budget is the basis for forecasting capital requirements and capital is called on the basis of it as adjusted for changes indicated in monthly and quarterly management reports Liquidity risk is managed by ensuring capital calls are issued well in advance to meet payment of expenses as they arise Capital calls require Shareholders and Investors to subscribe in US dollars to the issuance of additional Preference Shares and SPCs Until utilised, capital drawn down is held on short term deposits and on the current account

The following are the contractual maturities of financial liabilities, including estimated interest payments and excluding the impact of netting agreements

| 31 December 2009 | Carrying Amount $000s | Contractual cash flows $000s | 6mth or less $000s | 6-12 months $000s | 1-2 years $000s | 2-5 years $000s | More than 5 years $000s |
|---|---|---|---|---|---|---|---|
| **Non-derivative financial liabilities** | | | | | | | |
| Trade and other payables | 2,469 | (2,469) | (2,469) | - | - | - | - |
| Provisions | 1,000 | (1,000) | - | (1,000) | - | - | - |
| Subordinated preference certificates | 350,671 | (364,614) | - | - | - | - | (364,614) |
| Preference shares | 49,319 | (49,319) | - | - | - | - | (49,319) |
| | 403,459 | (417,402) | (2,469) | (1,000) | - | - | (413,933) |

| 31 December 2008 $000s | Carrying Amount | Contractual cash flows | 6mth or less | 6-12 months | 1-2 years | 2-5 years | More than 5 years |
|---|---|---|---|---|---|---|---|
| **Non-derivative financial liabilities** | | | | | | | |
| Trade and other payables | 9,608 | (9,608) | (9,608) | - | - | - | - |
| Provisions | 975 | (975) | - | (975) | - | - | - |
| Subordinated preference certificates | 202,159 | (293,086) | - | - | - | - | (293,086) |
| Preference shares | 46,593 | (46,593) | - | - | - | - | (46,593) |
| | 259,335 | (350,262) | (9,608) | (975) | - | - | (339,679) |

## 16. Related party disclosures

### a) Equity interests

The Company financial statements include the financial statements of the subsidiaries listed in the following table

| Name | Country of Incorporation | % Equity Interest 2009 | 2008 |
|---|---|---|---|
| Fairfield Energy Holdings Limited | England | 100% | 100% |
| Fairfield Acer Limited | England | 100% | 100% |
| Fairfield Betula Limited | England | 100% | 100% |
| Fairfield Cedrus Limited | England | 100% | 100% |
| Fairfield Fagus Limited | England | 100% | 100% |

Transactions entered into during the year ended and as at 31 December 2009 are as follows

| | Recoveries and other income to related parties* $000 | Trade receivables owed by related parties | Loans owed by related parties $000 |
|---|---|---|---|
| **2009** | | | |
| Transactions with subsidiaries | 15,348 | 5 213 | 254,243 |
| Transactions with joint ventures | 6,719 | 3,669 | - |
| **2008** | | | |
| Transactions with subsidiaries | 9,729 | - | 148,742 |
| Transactions with joint ventures | 6,475 | - | - |

### b) Entity with significant influence over the Company

At 31 December 2009 by virtue of a 36% (2008 36%) shareholding of the Company, the only entity with significant influence was Warburg Pincus LLC

### c) Terms and conditions of transactions with related parties in the wholly owned Group

Sales and purchases of goods and services between related parties are made at normal market prices and on terms equivalent to those that prevail in arm's length transactions Outstanding balances with entities other than subsidiaries are unsecured, interest free and cash settlement is expected within 30 days of invoice Terms and conditions for transactions with subsidiaries are the same, with the exception that balances are placed on intercompany accounts with no specified credit period Intercompany loans are not expected to be repaid in the immediate future The Company has not benefited from any guarantees for any related party receivables or payables and has not recognised any bad debts or made any provision for doubtful debts relating to amounts owed by related parties

## 17 Commitments, contingencies and guarantees

### Capital and other commitments

At 31 December 2009, the Company was party to gross capital and other commitments of $13 9 million (2008 $16 5 million) These commitments include both capital and operating contractual obligations

### Contingencies and guarantees

The Company, as parent company to the Group, may enter into contracts on behalf of its subsidiaries where better terms can be obtained

## 18 Events after the reporting date

Events subsequent to the reporting date are disclosed in Note 34 of the Consolidated Financial Statements

# Glossary of terms

| | |
|---|---|
| **$** | United States Dollar |
| **AGM** | Annual general meeting |
| **Appraisal well** | Drilled to follow up a discovery and evaluate its commercial potential |
| **bbl** | Barrel |
| **Board** | The Board of Directors of Fairfield Energy Limited |
| **boe** | Barrels of oil equivalent |
| **boepd** | Barrels of oil equivalent per day |
| **bopd** | Barrels of oil per day |
| **BS** | Brent System |
| **CGU** | Cash-generating unit |
| **Combined Code** | The Combined Code dated June 2006 appended to the Listing Rules |
| **Companies Act** | The Companies Act 2006 (as amended) and/or the Companies Act 2006 (as amended), as appropriate |
| **The Company** | Fairfield Energy Limited |
| **DECC** | Department of Energy and Climate Change |
| **Development well** | Drilled to recover hydrocarbons |
| **Dunlin Area** | Dunlin area assets include references to the Dunlin, Dunlin South West, Skye/Block 6, Osprey and Merlin fields The first three fields are held in the subsidiary Fairfield Betula The remainder are held in Fairfield Fagus On occasion, Darwin (also known as North West Hutton), may be included in the definition of the Dunlin Area |
| **E&E** | Exploration and evaluation |
| **EIR** | Effective interest rate |
| **FDP** | Field development plan |
| **Group** | The Company and its subsidiaries |
| **HS&E** | Health safety and environment |
| **IAS** | International Accounting Standard |
| **IFRS** | International Financial Reporting Standard(s) |
| **JV** | Joint venture |
| **LIBOR** | London Inter-Bank Offered Rate |
| **LTI** | Lost Time Injury |
| **M** | Million |
| **PRT** | Petroleum revenue tax |
| **SPC(s)** | Subordinated preference certificate(s) |
| **SVT** | Sullom Voe Terminal |

# Company information

**Registered No 5562373**

**Directors**
Christopher Alan Wright
Mark Francis McAllister
Simon William Caines Eyers *
Peter Kagan *
David Krieger *
David L Pearce *
Jeff van Steenbergen *
Frederick Matthew Thomas Ponsonby * (resigned 31/7/09)
Andrew Paterson *
* denotes Non-Executive Directors

**Secretary**
Iain MacDonald

**Auditors**
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**Bankers**
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**Solicitors**
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