

NAUTICAL PETROLEUM LIMITED
REPORT & FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2020



COMPANIES HOUSE

22 APR 2021

EDINBURGH MAILBOX

Nautical Petroleum Limited

Directors:

James Smith
Simon Thomson
Paul Mayland

Secretary:

Anne McSherry

Independent Auditors:

PricewaterhouseCoopers LLP
Atria One
144 Morrison Street
Edinburgh
EH3 8EX

Solicitors:

Shepherd and Wedderburn LLP
1 Exchange Crescent
Conference Square
Edinburgh
EH3 8UL

Registered Office:

4th Floor
Wellington House
125 The Strand
London
WC2R 0AP

Registered No:

04362104

Nautical Petroleum Limited

Directors' Report

The Directors of Nautical Petroleum Limited ("the Company") present their Annual Report for the year ended 31 December 2020 together with the audited Financial Statements of the Company for the year.

The operations of Nautical Petroleum Limited and its direct and indirect subsidiaries were impacted by COVID-19 and increased oil price volatility. The Company deferred capital expenditure to preserve liquidity during this period of uncertainty, however production activities on the Company's subsidiary assets in the North Sea continued uninterrupted during 2020.

Subsequent to the balance sheet date, the Company entered into an agreement to sell its interests in its producing assets, Catcher and Kraken; note 6.7 provides further details. The sale is expected to complete in the first half of 2021. As the sales process was not sufficiently advanced at the year end, the assets have not been reclassified as Assets Held-for-Sale at the balance sheet date.

In assessing whether the going concern assumption is appropriate, the Directors considered the Company cash flow forecasts under various scenarios, including the implications of the disposal of its producing assets, identifying risks and mitigants and ensuring the Company has sufficient funding to meet its current commitments as and when they fall due for a period of at least 12 months from the date of approval of the Financial Statements. These forecasts also include scenarios that take account of a prolonged economic downturn as a result of COVID-19 which has led to volatility in oil prices across 2020.

The Directors have a reasonable expectation that the Company will continue in operational existence for a period of at least 12 months from the date of approval of the Financial Statements and have therefore used the going concern basis in preparing the Financial Statements.

Consolidated financial statements are not produced for the Company and its wholly owned subsidiaries (detailed in note 6.4 to the Financial Statements) as provided under the exemption in section 400(1) of the Companies Act 2006.

The Company is a wholly-owned subsidiary of Capricorn Energy Limited. The results of the Company are consolidated into those of the ultimate parent company, Cairn Energy PLC, registered in Scotland, whose principal place of business is at 50 Lothian Road, Edinburgh, EH3 9BY. Copies of Cairn Energy PLC's financial statements are available to the public and may be obtained from the above mentioned address.

Results and Dividend

During the year Nautical Petroleum Limited made a profit of US\$20.0m (2019: profit US\$618.7m). The reduction in profit was due to oil price volatility during the COVID-19 pandemic, although there was no significant impact on production levels.

Dividends of US\$288.0m (2019: US\$269.2m) were declared and distributed in respect of the year ended 31 December 2020 by offset against loans due by the Company's parent undertaking.

Strategic Report

Included in the Strategic Report are the Company's Business Review and principal risks and uncertainties.

Stakeholder engagement

The Company's Section 172 Statement is included in the Strategic Report. The Company is an exploration and production company, whose stakeholders are governments, business partners, peers and contractors. The engagement with the Company's stakeholders is the same as that of the Group. These are discussed on pages 16 to 19 of the Group's annual report which does not form part of this report.

Streamlined Energy and Carbon Reporting ("SECR") Framework

The Company is exempt from the requirement to report in respect of SECR, as Cairn Energy PLC fulfils this requirement on behalf of the Cairn Energy PLC Group.

Accounting Policies

Nautical Petroleum Limited applies accounting policies in line with the Cairn Energy PLC Group accounting policies. Significant accounting policies of the Group are included in the Cairn Energy PLC Group financial statements.

Nautical Petroleum Limited

Directors' Report (continued)

Directors

The directors of the Company who were in office during the year and up to the date of signing the Financial Statements were:

James Smith
Paul Mayland
Simon Thomson
Brita Holstad (resigned 5 February 2020)

The Company maintains qualifying third-party indemnity insurance on behalf of its directors.

Statement of Directors' Responsibilities

The directors are responsible for preparing the Strategic Report, Directors' Report and the Financial Statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the Financial Statements in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006. Under company law the directors must not approve the Financial Statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that year. In preparing these Financial Statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether for the Company, international accounting standards in conformity with the requirements of the Companies Act 2006 have been followed; and
- prepare the Financial Statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and 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.

Disclosure of Information to Auditors

In the case of each director in office at the date the Directors' Report is approved:

- so far as the director is aware, there is no relevant audit information of which the company's auditors are unaware; and
- they have taken all the steps that they ought to have taken as a director in order to make themselves aware of any relevant audit information and to establish that the company's auditors are aware of that information.

The auditors, PricewaterhouseCoopers LLP, have indicated their willingness to continue in office, and a resolution that they be re-appointed will be presented at the annual general meeting.

BY ORDER OF THE BOARD



Anne McSherry
Secretary

50 Lothian Road
Edinburgh EH3 9BY

16 April 2021

Nautical Petroleum Limited

Strategic Report

Results and Dividend

During the year Nautical Petroleum Limited made a profit of US\$20.0m (2019: profit of US\$618.7m). The reduction in profit was due to oil price volatility during the COVID-19 pandemic, although there was no significant impact on production levels. A dividend of US\$288.0m was declared and distributed in respect of the year ended 31 December 2020 and was settled by offset against loans due by the Company's parent company (2019: US\$269.2m).

Business Review

The Company's principal activity is that of oil and gas exploration, development and production in the UK sector of the North Sea (UKCS).

The Company's core competence is within the subsurface, hydrocarbon development and commercial arena of the exploration and production ('E & P') business. The company has built an asset portfolio which will continue to be expanded through 'farming in' to and acquisitions of assets from existing oil and gas companies on the UKCS and with focused licence round applications.

Subsequent to the balance sheet date, the Company entered into an agreement to sell its interests in its producing assets, Catcher and Kraken; note 6.7 provides further details. The sale is expected to complete in the first half of 2021. As the sales process was not sufficiently advanced at the year end, the assets have not been reclassified as Assets Held-for-Sale at the balance sheet date.

After completion of the sale the Company will continue its exploration activities, and will also seek new opportunities within the E and P business sector.

The Company's strategy and business model are linked to those of the Cairn Energy PLC Group ("the Group") during the year and the information that fulfils the requirements of the Strategic Report can be found in the Strategic Report section of the Group's annual report on pages 2 to 69, which does not form part of this report.

Stakeholders and s172 Statement

The directors of the Company consider that they have adhered to the requirements of section 172 of the Companies Act 2006 (the 'Act') and have, in good faith, acted in a way that they consider would be most likely to promote the success of the Company for the benefit of its shareholders and have had regard to and recognised the importance of considering all stakeholders and other matters (as set out in s.172(1) (a-f) of the Act) in its decision making.

Taking into account the relative size of the Company, and its part in the Cairn Energy PLC Group, it is considered reasonable that the decision making is taken by the Group Board of Directors and the Directors of the Company as appropriate. The Group Board of Directors promote full and effective interaction across all levels of the Group to support the delivery of strategic and business objectives within a framework of best corporate governance practice.

The Company is an exploration and production company, with business partners but no employees. The engagement with the Company's stakeholders is the same as that of the Group. These are discussed on pages 16 to 19 of the Group's annual report which does not form part of this report.

Principal Risks and Uncertainties

From the perspective of the Company, the principal risks and uncertainties are integrated with the principal risks of the Group and are not managed separately. Accordingly, the principal risks and uncertainties of the Group which include those of the Company, are discussed in pages 42 to 51 of the Group's annual report which does not form part of this report.

Nautical Petroleum Limited

Strategic Report (continued)

Key Performance Indicators

The key performance indicators of the Company are aligned with those of the Group where these concern activities in the UK sector of the North Sea. These are discussed on pages 30 to 33 of the Group's annual report and do not form part of this report.

BY ORDER OF THE BOARD



Anne McSherry
Secretary

50 Lothian Road
Edinburgh EH3 9BY

16 April 2021

Independent auditors' report to the members of Nautical Petroleum Limited

Report on the audit of the financial statements

Opinion

In our opinion, Nautical Pétroleum Limited's financial statements:

- give a true and fair view of the state of the company's affairs as at 31 December 2020 and of its profit and cash flows for the year then ended;
- have been properly prepared in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements, included within the Report & Financial Statements (the "Annual Report"), which comprise: the balance sheet as at 31 December 2020; the income statement, the statement of comprehensive income, the statement of cash flows, the statement of changes in equity for the year then ended; and the notes to the financial statements, which include a description of the significant accounting policies.

Separate opinion in relation to IFRSs as issued by the IASB

As explained in note 1 to the financial statements, the company, in addition to applying international accounting standards in conformity with the requirements of the Companies Act 2006, has also applied international financial reporting standards (IFRSs) as issued by the International Accounting Standards Board (IASB).

In our opinion, the company financial statements have been properly prepared in accordance with IFRSs as issued by the IASB.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities under ISAs (UK) are further described in the Auditors' responsibilities for the audit of the financial statements section of our report. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We remained independent of the company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, which includes the FRC's Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

Conclusions relating to going concern

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the company's ability to continue as a going concern for a period of at least twelve months from when the financial statements are authorised for issue.

In auditing the financial statements, we have concluded that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate.

However, because not all future events or conditions can be predicted, this conclusion is not a guarantee as to the company's ability to continue as a going concern.

Our responsibilities and the responsibilities of the directors with respect to going concern are described in the relevant sections of this report.

Reporting on other information

The other information comprises all of the information in the Annual Report other than the financial statements and our auditors' report thereon. The directors are responsible for the other information. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except to the extent otherwise explicitly stated in this report, any form of assurance thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we identify an apparent material inconsistency or material misstatement, we are required to perform procedures to conclude whether there is a material misstatement of the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report based on these responsibilities.

With respect to the Strategic Report and Directors' Report, we also considered whether the disclosures required by the UK Companies Act 2006 have been included.

Based on our work undertaken in the course of the audit, the Companies Act 2006 requires us also to report certain opinions and matters as described below.

Independent auditors' report to the members of Nautical Petroleum Limited (continued)

Strategic Report and Directors' Report

In our opinion, based on the work undertaken in the course of the audit, the information given in the Strategic Report and Directors' Report for the year ended 31 December 2020 is consistent with the financial statements and has been prepared in accordance with applicable legal requirements.

In light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we did not identify any material misstatements in the Strategic Report and Directors' Report.

Responsibilities for the financial statements and the audit

Responsibilities of the directors for the financial statements

As explained more fully in the Statement of Directors' Responsibilities the directors are responsible for the preparation of the financial statements in accordance with the applicable framework and for being satisfied that they give a true and fair view. The directors are also responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

Auditors' responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined above, to detect material misstatements in respect of irregularities, including fraud. The extent to which our procedures are capable of detecting irregularities, including fraud, is detailed below.

Based on our understanding of the company and industry, we identified that the principal risks of non-compliance with laws and regulations related to breaches of UK regulatory principles including tax legislation, and those of the wide variety of jurisdictions in which the investments of the company operate, and we considered the extent to which non-compliance might have a material effect on the financial statements. We also considered those laws and regulations that have a direct impact on the financial statements such as the Companies Act 2006. We evaluated management's incentives and opportunities for fraudulent manipulation of the financial statements (including the risk of override of controls), and determined that the principal risks were related to areas of estimate in the financial statements and posting of inappropriate journal entries in order to improve reported performance. Audit procedures performed included:

- Discussion with management, internal audit, internal and external legal counsel, and individuals outside the finance function, including consideration of known or suspected instances of non-compliance with laws and regulations and fraud.
- Understanding management's controls designed to prevent and detect irregularities.
- Review of Board minutes and Internal Audit reports.
- Challenging assumptions and judgements made by management in its significant accounting estimates, particularly the carrying value of its producing assets, with a focus on any indicators of impairment.
- Identifying and testing journal entries, in particular, any journal entries posted by unexpected users, journals posted at unexpected times, journals reflecting unusual account combinations or journals with descriptions containing key unexpected words.

There are inherent limitations in the audit procedures described above. We are less likely to become aware of instances of non-compliance with laws and regulations that are not closely related to events and transactions reflected in the financial statements. Also, the risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion.

A further description of our responsibilities for the audit of the financial statements is located on the FRC's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditors' report.

Use of this report

This report, including the opinions, has been prepared for and only for the company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Independent auditors' report to the members of Nautical Petroleum Limited (continued)


Other required reporting

Companies Act 2006 exception reporting

Under the Companies Act 2006 we are required to report to you if, in our opinion:

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

We have no exceptions to report arising from this responsibility.



Lindsay Gardiner (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Edinburgh
16 April 2021

Nautical Petroleum Limited

Income Statement

For the year ended 31 December 2020

	Note	2020 US\$m	2019 US\$m
Continuing operations			
Revenue	2.1	394.3	532.3
Cost of sales	2.1	(119.9)	(68.7)
Depletion and amortisation	2.3	(213.5)	(217.6)
Gross profit		60.9	246.0
Pre-award costs		(1.0)	(0.8)
Unsuccessful exploration costs	2.2	(20.1)	(6.1)
Administrative expenses		(0.1)	(0.6)
Impairment of investment in subsidiary	6.4	-	(15.5)
Reversal of impairment of property, plant & equipment - development/producing assets	2.3	-	130.7
Operating profit	4.1	39.7	353.7
Dividends received	6.5	-	279.9
Finance income	4.2	4.2	15.5
Finance costs	4.3	(23.9)	(30.4)
Profit before taxation		20.0	618.7
Taxation			
Tax charge	5.1	-	-
Profit for the year		20.0	618.7

Nautical Petroleum Limited

Statement of Comprehensive Income

For the year ended 31 December 2020

		2020 US\$m	2019 US\$m
Profit for the year		20.0	618.7
Other Comprehensive Income/(Expense)— items that may be recycled to the Income Statement			
Fair value gain/(loss) on hedge options	3.5	52.2	(29.7)
Hedging gain recycled to the Income Statement	2.1	(56.0)	(10.9)
Other Comprehensive Expense for the year		(3.8)	(40.6)
Total Comprehensive Income for the year from continuing operations		16.2	578.1

Nautical Petroleum Limited

Balance Sheet

As at 31 December 2020

	Note	2020 US\$m	2019 US\$m
Non-current assets			
Intangible exploration/appraisal assets	2.2	8.3	21.3
Property, plant & equipment – development/producing assets	2.3	836.1	1,010.6
Investments in subsidiaries	6.4	0.1	0.1
		844.5	1,032.0
Current assets			
Inventory	2.1	12.3	13.8
Cash and cash equivalents	3.1	15.5	120.4
Trade and other receivables	3.4	62.9	76.7
Derivative financial instruments	3.5	0.2	4.1
		90.9	215.0
Total assets		935.4	1,247.0
Current liabilities			
Lease liabilities	3.3	40.9	41.0
Derivative financial instruments	3.5	3.2	1.6
Trade and other payables	3.6	60.3	58.0
Deferred revenue	3.7	4.8	16.9
		109.2	117.5
Non-current liabilities			
Provisions – decommissioning	2.4	151.0	139.8
Lease liabilities	3.3	193.1	234.0
Deferred revenue	3.7	16.9	18.7
		361.0	392.5
Total liabilities		470.2	510.0
Net assets		465.2	737.0
Equity attributable to owners of the parent			
Called-up share capital	6.1	24.9	24.9
Share premium	6.1	93.0	93.0
Hedge reserve	6.1	(3.4)	0.4
Retained earnings		350.7	618.7
Total equity		465.2	737.0

The Financial Statements on pages 9 to 40 were approved by the Board of Directors on 16 April 2021 and signed on its behalf by:



James Smith
Director

Company Registered No: 04362104

Nautical Petroleum Limited

Statement of Cash Flows

For the year ended 31 December 2020

	Note	2020 US\$m	2019 US\$m
Cash flows from operating activities			
Profit before taxation		20.0	618.7
Adjustments for non-cash income and expense and non-operating cash flow:			
Release of deferred revenue	2.1	(13.9)	(17.2)
Unsuccessful exploration costs	2.2	20.1	6.1
Depletion and amortisation	2.1	213.5	217.6
Reversal of impairment of property, plant & equipment - development/producing assets		-	(130.7)
Impairment of investment in subsidiary		-	15.5
Dividends received	6.5	-	(279.9)
Finance income		(4.2)	(15.5)
Finance costs		23.9	30.4
Adjustments for cash flow movements in assets and liabilities:			
Inventory movement		1.5	(5.6)
Trade and other receivables movement	3.4	26.5	(6.2)
Trade and other payables movement	3.6	3.3	4.6
Net cash flows from operating activities		290.7	437.8
Cash flows from investing activities			
Expenditure on intangible exploration/appraisal assets	2.2	(1.6)	(13.0)
Expenditure on property, plant & equipment - development/producing assets	2.3	(32.2)	(24.0)
Interest received		-	0.3
Repayment of loan from parent	3.6	-	(45.9)
Loan to parent		(306.8)	(255.1)
Net cash flows used in investing activities		(340.6)	(337.7)
Cash flows from financing activities			
Other interest and charges		(1.9)	(6.4)
Proceeds from borrowings	3.2	-	20.0
Repayment of borrowings		-	(105.0)
Lease payments	3.3	(57.1)	(56.8)
Lease reimbursements	3.3	4.0	7.0
Net cash flows used in financing activities		(55.0)	(141.2)
Net decrease in cash and cash equivalents		(104.9)	(41.1)
Opening cash and cash equivalents at beginning of year		120.4	161.5
Closing cash and cash equivalents	3.1	15.5	120.4

Nautical Petroleum Limited

Statement of Changes in Equity

For the year ended 31 December 2020

	Equity share capital US\$m	Share premium US\$m	Hedge reserve US\$m	Retained earnings US\$m	Total equity US\$m
At 1 January 2019	24.9	93.0	41.0	269.2	428.1
Profit for the year	-	-	-	618.7	618.7
Fair value on hedge options	-	-	(29.7)	-	(29.7)
Hedging gain recycled to the Income Statement	-	-	(10.9)	-	(10.9)
Total comprehensive income/(expense)	-	-	(40.6)	618.7	578.1
Dividend	-	-	-	(269.2)	(269.2)
At 31 December 2019	24.9	93.0	0.4	618.7	737.0
Profit for the year	-	-	-	20.0	20.0
Fair value on hedge options	-	-	52.2	-	52.2
Hedging gain recycled to the Income Statement	-	-	(56.0)	-	(56.0)
Total comprehensive (expense)/income	-	-	(3.8)	20.0	16.2
Dividends	-	-	-	(288.0)	(288.0)
At 31 December 2020	24.9	93.0	(3.4)	350.7	465.2

Nautical Petroleum Limited

Section 1 – Basis of Preparation

1.1 Significant Accounting Policies

a) Basis of Preparation

The Financial Statements of Nautical Petroleum Limited ("the Company") for the year ended 31 December 2020 were authorised for issue in accordance with a resolution of the Directors on 16 April 2021. The Company is a private limited company incorporated in England and domiciled in the United Kingdom. The registered office is located at 4th Floor, Wellington House, 125 The Strand, London WC2R 0AP. The registered company number is 04362104.

The Company prepares its Financial Statements on a historical cost basis applied consistently throughout the period, unless accounting standards require an alternate measurement basis. Where there are assets and liabilities calculated on a different basis, this fact is disclosed either in the relevant accounting policy or in the notes to the Financial Statements. The Financial Statements have been prepared in accordance with International Accounting Standards in conformity with the requirements of the Companies Act 2006.

The Company's business activities, together with the factors likely to affect its future development, performance and position are set out in the Strategic Report on pages 4 to 5. The financial position of the company, its liquidity position and borrowing facilities are presented in the Financial Statements and supporting notes. In addition, notes 3.9 and 6.2 to the Financial Statements includes the Company's objectives, policies and processes for managing its capital; its financial risk management objectives and details of its financial instruments; and its exposures to credit risk and liquidity risk.

b) Going Concern

The Directors have considered the factors relevant to support a statement of going concern.

In assessing whether the going concern assumption is appropriate, the Directors considered the Company cash flow forecasts under various scenarios, including the implications of the disposal of its producing assets (note 6.7), identifying risks and mitigants and ensuring the Company has sufficient funding to meet its current commitments as and when they fall due for a period of at least 12 months from the date of approval of the Financial Statements. These forecasts also include scenarios that take account of a prolonged economic downturn as a result of COVID-19 which has led to volatility in oil prices across 2020.

The Directors have a reasonable expectation that the Company will continue in operational existence for a period of at least 12 months from the date of approval of the Financial Statements and have therefore used the going concern basis in preparing the Financial Statements.

c) Accounting Standards

The Company prepares its Financial Statements in accordance with applicable IFRS, issued by the International Accounting Standards Board ("IASB") and interpretations issued by the IFRS Interpretations Committee ("IFRS IC") in conformity with the requirements of the Companies Act 2006. The Company's Financial Statements are also consistent with IFRS as issued by the IASB as they apply to accounting periods ended 31 December 2020.

Effective 1 January 2020, the Company has adopted the following standards and amendments to standards:

- Amendments to IAS 1 'Presentation of Financial Statements' and IAS 8 'Accounting Policies'
- Amendments to IFRS 9 'Financial Instruments', IAS 39 'Financial Instruments: Recognition and Measurement' and IFRS 7 'Financial Instruments: Disclosures'
- Revised Conceptual Framework for financial reporting

The adoption of the amendments above has had no material impact on the Company's results or financial statement disclosures.

There are no new standards or amendments, issued by the IASB and endorsed by the EU, that have yet to be adopted by the Company that will materially impact the Company's Financial Statements.

d) Investments

The Company's investments in subsidiaries are carried at cost less provisions resulting from impairment. In testing for impairment the carrying value of the investment is compared to its recoverable amount, being its fair value less costs of disposal. The fair value includes the discounted future net cash flows of oil and gas assets held by the subsidiary, using estimated cash flow projections over the licence period. For exploration assets, estimated discounted cash flows are risk-weighted for future exploration success.

Discounted future net cash flows are calculated using an estimated short-term oil price based on the forward curve and long-term oil price of US\$55/bbl unescalated (2019: long-term oil price of US\$65/bbl escalated at 2.0%), escalation for costs of 0.5% (2019: 2.0%) and a discount rate of 10% (2019: 10%). Full details on the assumptions used for valuing oil and gas assets can be found in section 2.

Nautical Petroleum Limited

Section 1 – Basis of Preparation

1.1 Significant Accounting Policies (continued)

e) Joint Arrangements

The Company is a partner (joint operator) in oil and gas exploration, development and production licences which are unincorporated joint arrangements. All of the Company's current interests in these arrangements are determined to be joint operations. The Company's principal licence interests are below:

Asset Name	Licence	Block(s)	Operator	Interest (%)
Kraken	P1077	9/2b	Enquest Heather Ltd (70.5%)	29.5
Catcher	P1430	28/9a	Premier Oil UK Ltd (50%)	20
Agar-Plaintain*	P1763	9/9d, 9/14a	Apache Beryl Ltd (50%)	25
Laverda	P2070	28/4a	Premier Oil UK Ltd (54%)	20
Chimera*	P2312	3/16a, 3/17a	Nautical Petroleum Limited	45
		22/11b, 22/12b, 22/16b,	Nautical Petroleum Limited	
Woodstock	P2379	22/17c		50
65Jaws	P2380	22/12d	Shell U.K. Limited (50%)	50
Manhattan	P2381	22/13c, 22/18d	Nautical Petroleum Limited	100
Bonneville	P2453	28/9c	Premier Oil UK Ltd (50%)	20
Laverda Template	P2454	28/9d	Premier Oil UK Ltd (54%)	20
Mane	P2466	3/16b, 3/21a, 3/22a	No Operator	100
		13/10, 13/3, 13/4, 13/5, 13/8,		
East Orkney Basin	P2468	13/9, 14/1, 14/6, 6/28, 6/29	No Operator	50
Cougar Rapide	P2550	28/9f	Premier Oil UK Ltd	20

* licence has been relinquished in 2021

Costs incurred relating to an interest in a joint operation other than costs relating to production are capitalised in accordance with the Company's accounting policies for oil and gas assets as appropriate (notes 2.2 and 2.3). All the Company's intangible exploration/appraisal assets and property, plant & equipment – development/producing assets relate to interests in joint operations.

The Company's working capital balances relating to joint operations are included in trade and other receivables (note 3.4) and trade and other payables (note 3.6). Any share of finance income or costs generated or incurred by the joint operation is included within the appropriate income statement account.

f) Foreign Currencies

These Financial Statements continue to be presented in US dollars (US\$), the functional currency of the Company.

The Company translates foreign currency transactions into the functional currency at the rate of exchange prevailing at the transaction date (or an approximation thereof where not materially different). Monetary assets and liabilities denominated in foreign currency are translated into the functional currency at the rate of exchange prevailing at the balance sheet date. Exchange differences arising are taken to the Income Statement except for those incurred on borrowings specifically allocable to development projects, which are capitalised as part of the cost of the asset, though there were none in either the current or preceding year.

Nautical Petroleum Limited

Section 2 – Oil and Gas Assets and Operations

Significant accounting judgements in this section:

Impairment testing of oil and gas assets

The Company has reviewed its long-term economic assumptions, focussing on the forecast impact a move from hydrocarbons towards renewable sources of energy will have on demand for oil and gas and associated prices, concluding that peak oil demand will be followed by structurally lower prices. At the year end, the Company revised its oil price assumptions reducing its long-term oil price assumption from US\$65/bbl to US\$55/bbl and removing future escalation of prices. Updated production profile estimates, reflecting this change in assumption, have led to downward reserve revisions and combined with lower forecast prices have reduced the fair value less cost of disposal of producing asset cash-generating units. As the reduction in the oil price assumption is an indicator that impairment may exist impairment tests were performed. No impairment was recorded.

Key estimates and assumptions in this section:

Estimation of hydrocarbon reserves and long-term oil price assumption

Oil and gas reserve volumes and related production profiles are estimated based on an internal process manual which follows industry best practice. This represents the Company's best estimate of reserves as at the reporting date. The Reserves and Resources Reporting Committee of the ultimate parent undertaking, which provides oversight, advice and guidance while providing senior level review, reports to the Cairn Energy PLC Group's Audit Committee before ultimately requesting approval of annual reserve volumes by the Board. The directors of the Company adopt the same reserve volumes as approved by the ultimate parent.

Third-party audits of the Company's reserves and resources are conducted annually.

A change in reserve volumes could impact depletion and decommissioning charges, impairment testing, release of deferred revenue and related deferred tax assets and liabilities.

The Company reduced its long-term oil price assumption from US\$65/bbl to US\$55/bbl flat also removing future price escalation which it believes reflects long-term market conditions. The Company's short-term assumption remains linked to the forward curve but has been shortened from three to two years.

Impairment testing of intangible exploration/appraisal assets and property, plant & equipment – development/producing assets

Where it is identified that there is an indicator of impairment, or an indicator identified that a prior year impairment may have reversed or decreased, on an intangible exploration/appraisal asset or a development/producing asset, an impairment test is conducted in accordance with the Company's accounting policies. The test compares either the carrying value of the asset or the carrying value of the cash-generating unit ("CGU") containing the asset, to the recoverable amount of that asset or CGU.

The recoverable amount of an asset represents its fair value less costs of disposal. This is based on either a verifiable third-party arm's length transaction from which a fair value can be obtained or, where there is no such transaction, the fair value less costs of disposal of an asset is calculated using a discounted post-tax cash flow model over the field life of the asset. The Company does not believe that the value in use of the asset would materially exceed its fair value less cost of disposal.

The key assumptions used in the Company's discounted cash flow models reflect past experience and take account of external factors. These assumptions include:

- Short/medium-term oil price based on a six-month average forward curve for two years from the balance sheet date (2019: three-month average forward curve for three years from the balance sheet date);
- Long-term oil price of US\$55/bbl unescalated (2019: US\$65/bbl escalated at 2.0%);
- Reserve estimates of discovered resource (2P and 2C) based on P50 reserve estimates;
- Production profiles based on internal estimates including assumptions on performance of assets;
- Cost profiles for the development and operating costs supplied by the operators and escalated at 0.5% (2019: 2.0%) per annum; and
- Post-tax discount rates of 10% (2019: 10%).

Decommissioning estimates

Provisions for decommissioning are based on the latest estimates provided by operators, subject to review by the Company and adjusted where deemed necessary. Costs provided to date are an estimate of the cost that would be incurred to remove and decommission facilities that existed at the year end and to plug and abandon development wells drilled to that date. Costs are escalated at 0.5% per annum (2019: 2.0%) and discounted at risk-free rates between 0.0% and 0.7% (2019: 2.0%).

Nautical Petroleum Limited

Section 2 – Oil and Gas Assets and Operations

2.1 Gross Profit: Revenue and Cost of Sales

Accounting policies

Revenue

Revenue from oil sales represents the Company's share of sales, on a liftings basis, from its producing interests in the UK North Sea, at the point in time where ownership of the oil or gas has been passed to the buyer. This occurs either when the customer takes delivery of a cargo of oil from the FPSO or at the contracted delivery point whichever is determined to be the point in time that the consideration due becomes unconditional and only the passage of time is required before payment is due. Revenue is measured using the Brent (or estimated Brent) oil price plus or minus the applicable discount based on the quality of the oil. Revenue from the sale of gas is recorded based on the volume of gas accepted each day by customers at the delivery point.

Commodity price hedging

The Company may hedge oil production for the Company's assets in line with hedging policies approved by the Board. Where a hedging instrument has been formally designated as a hedge for hedge accounting, changes in the intrinsic value of the hedged item and the time value of the option are recognised within Other Comprehensive Income (where the hedge is effective) based on fair value and are reclassified to the Income Statement when the hedged production itself affects profit or loss. Hedge effectiveness is assessed on a prospective basis at commencement and throughout the life of the option. Any hedge ineffectiveness identified is immediately charged to the Income Statement.

A change in the fair value of an option that is either not designated as a hedging instrument for hedge accounting or does not qualify for hedge accounting is recognised in the Income Statement.

Cost of sales and inventory

Production costs include the Company's share of costs incurred by the joint operation in extracting oil and gas. Also included are marketing and transportation costs and loss-of-production insurance costs payable over the year. Adjustments for overlift (where liftings taken by the Company exceed its working interest share), underlift (where liftings taken by the Company are less than its working interest share) and movements in inventory are included in cost of sales. Oil inventory is measured at market value in accordance with established industry practice.

Variable lease charges represent lease payments made on leases over and above the fixed lease commitment. Variable lease costs are charged directly to the Income Statement.

	Year ended 31 December 2020 US\$m	Year ended 31 December 2019 US\$m
Oil sales	323.7	501.6
Gas sales	0.8	2.6
Gain on hedge options designated for hedge accounting	56.0	10.9
Loss on hedge options not designated for hedge accounting	(0.1)	-
Release of deferred revenue (see note 3.7)	13.9	17.2
Revenue from oil and gas sales	394.3	532.3
Production costs	(75.9)	(68.1)
Oil inventory and underlift adjustment	(16.6)	20.6
Variable lease charges	(27.4)	(21.2)
Cost of sales	(119.9)	(68.7)
Depletion and amortisation (see note 2.3)	(213.5)	(217.6)
Gross profit	60.9	246.0

Revenue

The Company receives revenue from its two producing assets in the UK North Sea, Kraken and Catcher. On Kraken, where only oil is sold, the Company took a full lifting of crude on a scheduled basis to reflect the Company's working interest until a change in the marketing of Kraken crude during the second half of 2020 which results in the Company now receiving its working interest percentage share of each lifting of crude. This now aligns with Catcher where the Company receives its working interest share of each lifting of crude and its working interest share of Catcher gas sales. Payment terms are within 30 days.

Net sales volumes during the year averaged ~21,000 boepd (2019: ~21,400 boepd) for the two assets combined, realising an average sales price of US\$42.23/boe (2019: US\$64.52/boe).

COVID-19 contributed to pricing volatility during 2020 but had no significant impact on production levels.

Nautical Petroleum Limited

Section 2 – Oil and Gas Assets and Operations

2.1 Gross Profit: Revenue and Cost of Sales (continued)

Commodity price hedging

During 2020, the Company realised gains on hedge options designated for hedge accounting of US\$56.0m (2019: US\$10.9m) as the oil price fell below the floor on several hedge contracts. Hedging gains and/or losses on hedge options designated for hedge accounting are recycled to the Income Statement from Other Comprehensive Income when the option matures. Details on the Company's hedging position at 31 December 2020 can be found in note 3.5.

Cost of sales and inventory

Inventory of oil held at the year end is recorded at a market value of US\$12.3m (2019: US\$13.8m). Underlift adjustments on Kraken production volumes of US\$15.1m at 31 December 2019 fully unwound during 2020 following the change in the marketing of the crude. There is now no overlift or underlift adjustment on either Catcher or Kraken. The total inventory and underlift decrease in the year was US\$16.6m (2019: increase of US\$20.6m).

Variable lease costs on the Kraken FPSO of US\$15.0m (2019: US\$6.1m) and on the Catcher FPSO of US\$12.4m (2019: US\$15.1m) are charged to the Income Statement. Details on leases can be found in note 3.3.

2.2 Intangible Exploration/Appraisal Assets

Accounting policy

The Company follows a successful-efforts based accounting policy for oil and gas assets. Costs incurred prior to obtaining the legal rights to explore an area are expensed immediately to the Income Statement as pre-award costs.

Expenditure incurred on the acquisition of a licence interest is initially capitalised on a licence-by-licence basis. Costs are held, undepleted, within intangible exploration/appraisal assets until such time as the exploration phase on the licence area is complete or commercial reserves have been discovered and a field development plan approved.

Exploration expenditure incurred in the process of determining oil and gas exploration targets is capitalised initially within intangible exploration/appraisal assets and subsequently allocated to drilling activities. Costs are recognised following a cost accumulation model where any contingent future costs on recognition of an asset are recognised only when incurred. This includes where the Company has entered into a 'farm-in' agreement to either acquire or part-dispose of an exploration interest.

A farm-in is an agreement in which a party agrees to acquire from one or more of the existing licencees, an interest in an exploration licence, for a consideration which may consist of the performance of a specified work obligation on behalf of the existing licencees. This obligation may be subject to a monetary cap. Refund of full or partial costs incurred to date may also be included in a farm-in agreement. Where the Company has part-disposed of an exploration licence interest through a farm-in arrangement, a 'farm-down', the contingent consideration payable by the third party on the Company's behalf is not recognised in the Financial Statements. The future economic benefit which the Company will receive as a result of the farm-down will be dependent upon future success of any exploration drilling.

Exploration/appraisal drilling costs are capitalised on a well-by-well basis until the success or otherwise of the well has been established. The success or failure of each exploration/appraisal effort is judged on a well-by-well basis. Drilling costs are written off on completion of a well unless the results indicate that hydrocarbon reserves exist and there is a reasonable prospect that these reserves are commercial and work to confirm the commercial viability of such hydrocarbons is intended to be carried out in the foreseeable future. Where results of exploration drilling indicate the presence of hydrocarbons which are ultimately not considered commercially viable, all related costs are written off to the Income Statement.

Following appraisal of successful exploration wells, if commercial reserves are established and technical feasibility for extraction demonstrated and approved in a field development plan, then the related capitalised intangible exploration/appraisal costs are transferred into a single field cost centre within property, plant & equipment – development/producing assets, after testing for impairment (see below).

Proceeds from the disposal or farm-down of part or all of an exploration/appraisal asset are credited initially to that interest with any excess being credited to the Income Statement.

Impairment

Intangible exploration/appraisal assets are reviewed regularly for indicators of impairment and tested for impairment where such indicators exist. An indicator that one of the Company's assets may be impaired is most likely to be one of the following:

- There are no further plans to conduct exploration activities in the area;
- Exploration drilling in the area has failed to discover commercial reserve volumes;
- Changes in the oil price or other market conditions indicate that discoveries may no longer be commercial; or
- Development proposals for appraisal assets in the pre-development stage indicate that it is unlikely that the carrying value of the exploration/appraisal asset will be recovered in full.

Nautical Petroleum Limited

Section 2 – Oil and Gas Assets and Operations

2.2 Intangible Exploration/Appraisal Assets (continued)

Impairment (continued)

In such circumstances the intangible exploration/appraisal asset is allocated to any property, plant & equipment – development/producing assets within the same CGU and tested for impairment. Any impairment arising is recognised in the Income Statement for the year. Where there are no development assets within the CGU, the excess of the carrying amount of the exploration/appraisal asset over its recoverable amount is charged immediately to the Income Statement.

	UK Total US\$m
Cost	
At 1 January 2019	44.2
Additions	4.3
Unsuccessful exploration costs	(6.1)
Transfer to development/producing assets	(18.1)
At 31 December 2019	24.3
Additions	8.6
Unsuccessful exploration costs	(20.1)
Disposals	(1.5)
At 31 December 2020	11.3
Impairment	
At 1 January 2019, 31 December 2019 and 31 December 2020	3.0
Net book value	
At 31 December 2018	41.2
At 31 December 2019	21.3
At 31 December 2020	8.3

All additions to exploration/appraisal assets have been funded through cash and working capital.

UK

Additions in the year include the acquisition and subsequent costs on the non-operated licence P2380 containing the Jaws prospect. A 50% interest in this licence was obtained through a swap for a 50% interest in the licence P2379 containing the Diadem prospect. During the year US\$4.3m and US\$2.5m were incurred on the Jaws and Diadem prospects respectively with remaining additions of US\$1.8m incurred across the rest of the UK portfolio of licences.

US\$20.1m was charged to the Income Statement as unsuccessful costs in the year, including US\$19.4m on the Agar-Plantain licence which was relinquished early in 2021 after concluding that the discovery was not commercially viable in a lower oil-price environment.

Costs capitalised at 31 December 2020 of US\$8.3m include the above mentioned Jaws and Diadem prospects and US\$1.5m on the Manhattan and East Orkney licences.

In 2019, well cost additions were US\$3.2m as the Company completed the Chimera exploration well, agreeing a farm-down prior to drilling reducing the Company's capital exposure. The well was ultimately unsuccessful. Other exploration additions of US\$1.1m in 2019 related to ongoing portfolio management. Additions relating to drilling in 2019 included US\$2.5m of rig costs incurred under short-term lease contracts.

Impairment review

At the year end, the Company reviewed its remaining intangible exploration/appraisal assets for indicators of impairment. No indicators of impairment were identified.

Nautical Petroleum Limited

Section 2 – Oil and Gas Assets and Operations

2.3 Property, Plant & Equipment – Development/Producing Assets

Accounting policy

Costs

All costs incurred after the technical feasibility and commercial viability of producing hydrocarbons has been demonstrated and a development plan approved, are capitalised within development/producing assets on a field-by-field basis. Subsequent expenditure is capitalised only where it either enhances the economic benefits of the development/producing asset or replaces part of the existing development/producing asset. Any remaining costs associated with the part replaced are expensed.

Costs of borrowings relating to the ongoing construction of development/producing assets and facilities are capitalised during the development phase of the project. Capitalisation ceases once the asset is ready to commence production.

Net proceeds from any disposal, part-disposal or farm-down of development/producing assets are credited against the appropriate portion of previously capitalised cost. A gain or loss on disposal of a development/producing asset is recognised in the Income Statement to the extent that the net proceeds, measured at fair value, exceed or are less than the appropriate portion of the net capitalised costs.

Depletion and amortisation

Depletion is charged on a unit-of-production basis, based on proved and probable reserves on a field-by-field basis. Fields within a single development area may be combined for depletion purposes. Where production commences prior to completion of the development, costs to be depleted include the costs-to-complete of the facility required to extract the volume of reserves recorded. Amortisation charged on right-of-use leased assets is also charged on a unit-of-production basis, based on proved and probable reserves.

Impairment

Development/producing assets are reviewed for indicators of impairment at the balance sheet date. Indicators of impairment for the Company's development assets include:

- Downward revisions of reserve estimates;
- Increases in cost estimates for development projects; or
- A decrease in the oil price or other negative changes in market conditions.

Impairment tests are carried out on each development/producing asset at the balance sheet date where an indicator of impairment is identified. The test compares the carrying value of an asset to its recoverable amount based on the higher of its fair value less costs of disposal or value in use. Where the fair value less costs of disposal supports the carrying value of the asset, no value-in-use calculation is performed.

If it is not possible to calculate the fair value less costs of disposal of an individual asset, the fair value less costs of disposal is calculated for the CGU containing the asset and tested against the carrying value of the assets and liabilities in the CGU for impairment. Where an asset can be tested independently for impairment, this test is performed prior to the inclusion of the asset into a CGU for further impairment tests.

If the carrying amount of the asset or CGU exceeds its recoverable amount, an impairment charge is made.

Where there has been a charge for impairment in an earlier period that charge will be reversed in a later period where there has been a change in circumstances to the extent that the recoverable amount is higher than the net book value at the time. In reversing impairment losses, the carrying amount of the asset will be increased to the lower of its original carrying value or the carrying value that would have been determined (net of depletion) had no impairment loss been recognised in prior years.

Decommissioning

At the end of the producing life of a field, costs are incurred in plugging and abandoning wells, removing subsea installations and decommissioning production facilities. The company recognises the full discounted cost of decommissioning as an asset and liability when the obligation to rectify environmental damage arises. The decommissioning asset is included within property, plant & equipment – development/producing assets with the cost of the related installation. The liability is included within provisions.

Revisions to the estimated costs of decommissioning which alter the level of the provisions required are also reflected in adjustments to the decommissioning asset. The amortisation of the asset is calculated on a unit-of-production basis based on proved and probable reserves. The amortisation of the asset is included in the depletion charge in the Income Statement and the unwinding of discount of the provision is included within finance costs.

Nautical Petroleum Limited

Section 2 – Oil and Gas Assets and Operations

2.3 Property, Plant & Equipment – Development/Producing Assets (continued)

	UK US\$m	UK Right-of-use leased assets US\$m	Total US\$m
Cost			
At 1 January 2019	1,077.4	313.4	1,390.8
Additions	16.4	-	16.4
Increase in decommissioning asset	10.7	2.9	13.6
Transfer from exploration/appraisal assets	18.1	-	18.1
At 31 December 2019	1,122.6	316.3	1,438.9
Additions	35.6	-	35.6
Increase in decommissioning asset	3.4	-	3.4
At 31 December 2020	1,161.6	316.3	1,477.9
Depletion, amortisation and impairment			
At 1 January 2019	319.7	21.7	341.4
Depletion and amortisation charges	161.1	56.5	217.6
Reversal of impairment	(130.7)	-	(130.7)
At 31 December 2019	350.1	78.2	428.3
Depletion and amortisation charges	164.5	49.0	213.5
At 31 December 2020	514.6	127.2	641.8
Net book value			
At 31 December 2018 ¹	757.7	144.2	901.9
At 31 December 2019	772.5	238.1	1,010.6
At 31 December 2020	647.0	189.1	836.1

¹ The 2018 net book value excludes the IFRS 16 opening balance adjustment of US\$147.5m recorded on 1 January 2019.

The Company's UK producing assets contain two cash generating units; the Kraken development area, including the Worcester satellite field, and the Greater Catcher and Laverda development areas which form a single unit.

Additions of US\$35.6m consist of Kraken costs of US\$18.2m, including drilling costs of the Worcester well, and Catcher spend of US\$17.4m, where the Varadero infill well and subsea installation were completed in the year. Drilling of the Catcher North and Laverda development wells have been delayed due to COVID-19 uncertainties. The current year additions were funded through cash and working capital and include US\$10.4m of costs under short-term lease contracts.

The increase in the decommissioning asset in the current year of US\$3.4m (2019: US\$10.7m) relates to changes in estimates for both Kraken and Catcher.

The 2019 additions relating to the Kraken producing asset of US\$12.1m included the completion of the final sub-surface drill centre, DC-4. Remaining 2019 additions of US\$4.3m were incurred on the Catcher producing asset.

Combined depletion and amortisation charges for the year of US\$213.5m (2019: US\$217.6m) were charged to the Income Statement based on production during the year and total reserves over the life of the asset.

Nautical Petroleum Limited

Section 2 – Oil and Gas Assets and Operations

2.3 Property, Plant & Equipment – Development/Producing Assets (continued)

Impairment review

At 31 December 2020, following a reduction in the Company's long-term oil price assumption, impairment tests were conducted on the Company's UK producing assets at the balance sheet date. No impairment was identified.

During 2019, production performance on Kraken improved significantly and in addition the Operator conducted more regular well testing to improve reservoir monitoring. Consequently the Company revised production profile estimates upward reflecting this improvement while also incorporating new volumes associated with the Worcester satellite field, subsequently developed in 2020. The changes to the production profile resulting from improved performance is an indicator that prior year impairment charges may no longer exist or may have decreased. The resultant impairment test indicated that a full reversal of prior year impairment charges should be recorded. The reversal was capped to US\$130.7m, being the brought forward impairment adjusted for the depletion that would have been charged had no impairment been recorded.

Sensitivity analysis on the Company's impairment tests can be found in note 2.6.

Proposed Sale of Catcher and Kraken Producing Assets

On 8 March 2021, the Company entered into a sales agreement to dispose of its entire interests in the Catcher and Kraken producing assets (note 6.7). As the sales process was not sufficiently advanced at the year end, the assets have not been reclassified as Assets Held-for-Sale at the balance sheet date.

2.4 Provisions - Decommissioning

	Development/ Producing assets US\$m	Total US\$m
At 1 January 2019	117.8	117.8
Foreign exchange	5.8	5.8
Unwinding of discount (note 4.3)	2.6	2.6
Provided in the year	13.6	13.6
At 31 December 2019	139.8	139.8
Foreign exchange	4.9	4.9
Unwinding of discount (note 4.3)	2.9	2.9
Provided in the year	3.4	3.4
At 31 December 2020	151.0	151.0

The decommissioning provisions at 31 December 2020 represent the present value of decommissioning costs related to the Kraken and Catcher development/producing assets. Amounts provided during the year of US\$3.4m reflect additional decommissioning costs for the wells drilled in the year. Provisions during 2019 related to revised decommissioning estimates for Kraken.

The provisions are based on operator cost estimates, subject to internal review and amendment where considered necessary and are calculated using assumptions based on existing technology and the current economic environment, discount rate of 0.0% and 0.7% per annum for Catcher and Kraken respectively (2019: 2.0%). The rates are based on the UK risk-free rate to the maturity of the respective decommissioning liability. The reasonableness of these assumptions is reviewed at each reporting date.

The decommissioning provisions represent management's best estimate of the obligation arising based on work undertaken at the balance sheet date. Actual decommissioning costs will depend upon the prevailing market conditions for the work required at the relevant time. The decommissioning of the Company's development/producing assets is forecast to occur between 2026 and 2036.

On completion of the sale of the Kraken and Catcher producing assets (note 6.7), the responsibility for carrying out the decommissioning of these assets will cease to be a liability for the Company as it will fall to the purchaser.

Nautical Petroleum Limited

Section 2 – Oil and Gas Assets and Operations

2.5 Capital Commitments

	At 31 December 2020 US\$m	At 31 December 2019 US\$m
Oil and gas expenditure:		
Intangible exploration/appraisal assets	25.9	40.4
Property, plant & equipment – development/producing assets	7.9	63.7
Contracted for	33.8	104.1

Capital commitments represent the Company's share of obligations in relation to its interests in joint operations. These commitments include the Company's share of the capital commitments of the joint operations themselves.

The capital commitments for intangible exploration/appraisal assets includes the Jaws exploration well planned for Q2 2021.

The capital commitments for property, plant & equipment – development/producing assets predominantly relates to Catcher and includes its planned satellite developments and 4D seismic acquisition.

As at 31 December 2020, the company had the following commitments relating to short-term leases and leases yet to commence. These amounts are also included in the total of capital commitments shown above.

	Development/ Producing assets US\$m	Total US\$m
Lease commitments at 31 December 2020	6.0	6.0
Lease commitments at 31 December 2019	10.6	10.6

Commitments relating to the Kraken and Catcher FPSO lease obligations which are operating rather than capital commitments are disclosed in note 3.3.

Nautical Petroleum Limited

Section 2 – Oil and Gas Assets and Operations

2.6 Impairment Testing Sensitivity Analysis

At 31 December 2020, impairment tests were conducted on the Company's producing asset cash generating units. No impairment was recorded.

The Company has run sensitivities on its long-term oil price assumption of US\$55/bbl, using alternate long-term price assumptions of US\$50/bbl and long-term prices based on the IEA's World Economic Outlook 2020 Sustainable Development Scenario ('WEO-2020'). These are considered to be reasonably possible long-term changes for the purposes of sensitivity analysis. The impact on the carrying value of development/producing assets is shown below.

Reduction in long-term oil price assumption to:	WEO-2020 US\$m	US\$50/bbl US\$m
Reduction in carrying value of development/producing assets	46.4	57.9

The oil price at the end of the Company's short-term, forward-curve based assumption period was US\$48/bbl and the impact of using this price as a long-term assumption does not materially differ from the US\$50/bbl sensitivity shown above.

The Company's proved and probable and contingent reserve estimates are based on P50 probabilities. P10 and P90 estimates are also produced but would not provide a reasonable estimate to be used in calculating the fair value of the Company's assets.

The valuations of Catcher and Kraken used in the year end impairment test have not been updated to reflect the combined value of the assets in the sales agreement entered with Waldorf Production Limited (note 6.7). However, the sales value agreed would not indicate any impairment of the producing assets.

Nautical Petroleum Limited

Section 3 – Working Capital, Financial Instruments and Long-term Liabilities

3.1 Cash and Cash Equivalents

	At 31 December 2020 US\$m	At 31 December 2019 US\$m
Cash and cash equivalents	15.5	120.4

3.2 Loans and Borrowings

The Company is a party in the Cairn Energy PLC Group's Reserve-Based Lending ('RBL') facility which was undrawn at 31 December 2020.

Reconciliation of opening and closing liability to cash flow movements:	Year ended 31 December 2020 US\$m	Year ended 31 December 2019 US\$m
Opening liability	-	85.0
Loan advances disclosed in the Cash Flow Statement: Advances in the year	-	20.0
Loan repayments disclosed in the Cash Flow Statement: Repayments in the year	-	(105.0)
Other movements in the Cash Flow Statement: Debt arrangement fees paid	-	0.8
Non-cash movements Amortisation of debt arrangement fees	-	(0.8)
Closing liability	-	-
Amounts due greater than one year	-	-
	-	-

No loan funding was drawn during 2020 (2019: US\$20.0m) by the Company and the RBL facility was undrawn at 31 December 2020 and 31 December 2019.

Debt arrangement fees paid in 2019 represent amounts paid by Capricorn Energy Limited, the Company's parent undertaking in 2018 for the extension of the RBL which were recharged to the Company as loan funding was drawn down during 2019.

Interest on debt drawn is charged at the appropriate LIBOR for the currency drawn plus an applicable margin. The facility remains subject to biannual redeterminations, has a market standard suite of covenants and is cross-guaranteed by all Group companies party to the facility. Any debt drawn is repayable in line with the amortisation of bank commitments over the period from 1 July 2022 to the extended final maturity date of 31 December 2025.

Total commitments under the facility are US\$575.0m. An accordion feature permits additional future commitments of up to US\$425.0m. The maximum available drawdown at 31 December 2020 was US\$107.0m available to several Group companies. The facility can also be used for general corporate purposes and may also be used to issue letters of credit and performance guarantees for the Cairn Energy PLC Group of up to US\$250.0m. Details of guarantees granted under this facility can be found in note 6.3.

Nautical Petroleum Limited

Section 3 – Working Capital, Financial Instruments and Long-term Liabilities

3.3 Lease Liabilities

Accounting policy

Lease liabilities are measured and recorded on commencement of the asset being brought in to use. Measurement is based on the lower of fair value of the asset or the net present value of fixed lease commitments under the contract. Lease payments made in excess of the fixed instalments are charged direct to the Income Statement as variable lease costs.

Lease payments are allocated between capital and interest based on the rate implicit in the lease agreement. Where this is not practical to determine, the Company's incremental borrowing rate is used.

Where there are changes subsequent to initial recognition, adjustments are made to both the lease liability and the capitalised asset. The interest rate used where the rate implicit in the lease is not determinable is updated at the date of the remeasurement.

No lease liability is recognised for leases where the period over which the right-of-use of an asset is obtained is forecast to be less than 12 months. Leases for low value items are not recorded as a liability but are charged as appropriate when the benefit is obtained.

Reconciliation of opening and closing liabilities to cash flow movements:	Year ended 31 December 2020 US\$m	Year ended 31 December 2019 US\$m
Opening lease liabilities	275.0	312.9
Leases commenced and revisions to leases in year:		
Revisions to lease liabilities	-	-
	-	-
Lease payments disclosed in the Cash Flow Statement as financing cash flows:		
Total lease payments	(84.5)	(78.0)
Variable lease payments (note 2.1)	27.4	21.2
	(57.1)	(56.8)
Other movements in the Cash Flow Statement:		
Reimbursements received from lessors	4.0	7.0
Non-cash movements		
Reimbursements due transferred from other receivables	(1.0)	(3.0)
Lease interest charges	13.1	14.9
	12.1	11.9
Closing liabilities	234.0	275.0
Amounts due less than one year:		
Tangible development/producing assets - right-of-use assets	40.9	41.0
Amounts due greater than one year:		
Tangible development/producing assets - right-of-use assets	193.1	234.0
Total lease liabilities	234.0	275.0

Variable lease costs are disclosed in note 2.1. Amortisation charges on right-of-use assets relating to property, plant & equipment - development/producing assets are disclosed in note 2.3. Costs relating to short-term leases and leases of low value assets, relating to exploration and development activities are disclosed in notes 2.2 and 2.3 where material. There are no further material short-term leases or charges for leases of low-value assets. The maturity analysis for lease liabilities is disclosed in note 3.8. The carrying value of right-of-use development/producing assets at 31 December 2020 is US\$189.1m (2019: US\$238.1m) (see note 2.3).

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Section 3 – Working Capital, Financial Instruments and Long-term Liabilities

3.4 Trade and Other Receivables

Accounting Policy

Trade receivables represent amounts due from the sale of oil and gas from the Company's UK producing assets. Other receivables primarily represent recharges to joint operations. Joint operation receivables are receivables that relate to the Company's interest in its oil and gas joint arrangements, including the Company's participating interest share of the other receivables of the joint arrangements themselves.

Trade receivables, other receivables and joint operation receivables, which are financial assets, are measured initially at fair value and subsequently recorded at amortised cost.

A loss allowance is recognised, where material, for expected credit losses on all financial assets held at the balance sheet date. Expected credit losses are the difference between the contractual cash flows due to the Company, and the discounted actual cash flows that are expected to be received. Where there has been no significant increase in credit risk since initial recognition, the loss allowance is equal to 12-month expected credit losses. Where the increase in credit risk is considered significant, lifetime credit losses are provided. For trade receivables a lifetime credit loss is recognised on initial recognition where material.

	At 31 December 2020 US\$m	At 31 December 2019 US\$m
Trade receivables	16.1	22.2
Amounts receivable from group companies	31.4	10.2
Other receivables	2.3	5.7
Accrued income – underlift (see note 2.1)	-	15.1
Joint operation receivables	13.1	23.5
	62.9	76.7

Trade receivables are measured at amortised cost. Revenue is recognised at the point in time where title passes to the customer and payment becomes unconditional.

Where material the Company has assessed the recoverability of trade and other receivables and no loss allowance is recognised for expected credit losses on all financial assets held at the balance sheet date.

Reconciliation of opening and closing receivables to operating cash flow movements:	Year ended 31 December 2020 US\$m	Year ended 31 December 2019 US\$m
Opening trade and other receivables	76.7	62.3
Closing trade and other receivables	(62.9)	(76.7)
Decrease/(Increase) in trade and other receivables	13.8	(14.4)
(Decrease)/Increase in joint operation receivables relating to investing activities	(10.2)	0.3
(Decrease) in prepayments and other receivables relating to other non-operating activities	(0.3)	(1.1)
Increase/(Decrease) in amounts receivable from group companies	23.1	(9.4)
Foreign exchange	0.1	18.4
Trade and other receivables movement recorded in operating cash flows	26.5	(6.2)

The movements in joint operation receivables relating to investing activities, relate to the Company's share of the receivables of joint operations in respect of exploration, appraisal and development activities. Movements relating to production activities are included in amounts through operating cash flows.

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Section 3 – Working Capital, Financial Instruments and Long-term Liabilities

3.5 Derivative Financial Instruments

	At 31 December 2020 US\$m	At 31 December 2019 US\$m
Current assets		
Financial assets – hedge options maturing within one year	0.2	4.1
Current liabilities		
Financial liabilities – hedge options maturing within one year	(3.2)	(1.6)
	(3.0)	2.5

The Company currently has an active commodity price hedging programme in place to protect debt capacity and support committed capital programmes. Mark-to-market gains and losses on oil price hedge options are recorded as financial assets and financial liabilities as appropriate at 31 December 2020.

At 31 December 2020 the Company had hedged ~1.0m barrels of 2021 forecast Kraken and Catcher oil production, using three-way collar and swap structures. ~0.5m barrels of production have been hedged through three-way collars, with a weighted average ceiling, floor and sub-floor prices of US\$55.00/bbl, US\$48.27/bbl and US\$35.00/bbl respectively (all prices quoted relate to dated Brent). ~0.5m barrels of production have been hedged through swap options with a weighted average strike price of US\$45.20/bbl. At 31 December 2020, no production forecast beyond 31 December 2021 had been hedged.

The three-way collars and swaps have been designated as hedges for hedge accounting. Hedge effectiveness is assessed at commencement of the option and prospectively thereafter. At the year end, the closing Brent oil price was US\$50.49/bbl (2019: US\$66.00/bbl). Fair value movements on the cost of the option are recorded in the Statement of Comprehensive Income in the year, with fair value losses of US\$3.8m being offset by fair value gains on options that matured in the year of US\$56.0m. The gain on matured options has been recycled to the Income Statement. In 2019 fair value losses of US\$40.6m were offset by fair value gains of US\$10.9m on options that matured in the year. The gain on matured options was recycled to the Income Statement.

	At 31 December 2020	At 31 December 2019
Hedge options outstanding at the year end		
Volume of oil production hedged	1.0mmbbls	2.8mmbbls
Weighted average sub-floor price of options	US\$35.00	-
Weighted average floor price of options	US\$48.27	US\$62.09
Weighted average ceiling price of options	US\$55.00	US\$74.89
Weighted average strike price of swaps	US\$45.20	US\$61.85
Maturity dates	January 2021 - December 2021	January 2020 - December 2020
Effects of hedge accounting on financial position and profit for the year		
	US\$m	US\$m
Financial assets	0.2	4.1
Financial liabilities	(3.2)	(1.6)
Accruals and other payables – accrued option costs	(0.5)	(2.1)
Fair value gain/(loss) on hedge options recorded in Other Comprehensive Income	52.2	(29.7)
Hedging gain recycled to Income Statement	(56.0)	(10.9)
Hedging gain recorded in Income Statement within revenue (note 2.1)	56.0	10.9

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Section 3 – Working Capital, Financial Instruments and Long-term Liabilities

3.5 Derivative Financial Instruments (continued)

Sensitivity analysis

Sensitivity analysis has been performed on equity movements that would arise from changes in the year end oil price forward curve and the resulting impact on the fair value of open hedge options at the year end. The sensitivity analysis considers only the impact on line items directly relating to hedge accounting (being financial assets and liabilities and fair value gains through Other Comprehensive Income) and not the impact of the change of other balance sheet items where valuation is based on the year end oil price, such as inventory.

Increase/(decrease) in equity	At 31 December 2020 US\$m	At 31 December 2019 US\$m
Change in oil price forward curve		
Decrease of 10%	8.8	12.4
Decrease of 20%	4.2	26.6
Increase of 10%	(4.3)	(12.6)
Increase of 20%	(9.2)	(25.5)

3.6 Trade and Other Payables

Accounting policy

Trade and other payables are non-interest bearing, with the exception of certain inter-group loans, and are measured at fair value initially then amortised cost subsequently.

Joint operation payables are payables that relate to the Company's interest in its oil and gas joint arrangements, including the Company's participating interest share of the trade and other payables of the joint arrangements themselves. Where the Company is operator of the joint operation, joint operation payables also include amounts that the Company will settle to third parties on behalf of joint operation partners. The amount to be recovered from partners for their share of such liabilities are included within joint operation receivables.

	At 31 December 2020 US\$m	At 31 December 2019 US\$m
Trade payables	8.7	-
Other taxation and social security	-	0.1
Amounts payable to group companies	7.6	7.2
Accruals and other payables	15.6	10.5
Joint operation payables	28.4	40.2
	60.3	58.0

Joint operation payables include US\$0.9m (2019: US\$4.2m), US\$5.1m (2019: US\$5.5m) and US\$22.4m (2019: US\$30.5m) relating to exploration/appraisal assets, development/producing assets and production costs respectively.

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Section 3 – Working Capital, Financial Instruments and Long-term Liabilities

3.6 Trade and Other Payables (continued)

Reconciliation of opening and closing payables to operating cash flow movements:	Year ended 31 December 2020 US\$m	Year ended 31 December 2019 US\$m
Opening trade and other payables	(58.0)	(386.0)
Closing trade and other payables	60.3	58.0
Increase/(Decrease) in trade and other payables	2.3	(328.0)
Decrease in joint operation payables relating to investing activities	3.8	12.9
(Increase)/Decrease in trade payables relating to investing activities	(3.1)	1.1
Decrease in accruals and other payables relating to non-operating activities	1.6	1.1
(Increase)/Decrease in amounts payable to group companies	(0.4)	319.7
Foreign exchange	(0.9)	(2.2)
Trade and other payables movement recorded in operating cash flows	3.3	4.6

Movements above for investing activities relate to exploration, appraisal and development activities through the Company's joint operations. Movements relating to production activities are included in amounts through operating cash flows. The movement in trade and other payables recorded in the Cash Flow Statement through operating cash flows primarily arise on production activities in the UK North Sea. The reduction in amounts payable to group companies in 2019 of US\$319.7m represented US\$279.9m of dividends from subsidiaries which were settled by offset against existing balances due, cash settlements on intercompany balances of US\$45.9m, and an offsetting amount of intercompany interest payable of US\$6.1m.

3.7 Deferred Revenue

Accounting policy

Deferred revenue, arising from a streaming agreement, is treated as cash received in advance of future oil sales. Revenue is recorded at the fair value of the consideration received and is amortised to the Income Statement on a unit-of-production basis, based on expected future volumes to which the stream provider is entitled.

FlowStream deferred revenue	Note	2020 US\$m	2019 US\$m
At 1 January		35.6	52.8
Released during the year	2.1	(13.9)	(17.2)
At 31 December		21.7	35.6
Amounts expected to be released within one year		4.8	16.9
Amounts expected to be released after one year		16.9	18.7
		21.7	35.6

Deferred revenue relates to the stream agreement with FlowStream entered into in 2017. A step-down in the percentage of Kraken crude sales attributable to FlowStream, triggered during 2020, has reduced the amounts that fall payable within 12 months from the balance sheet date.

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Section 3 – Working Capital, Financial Instruments and Long-term Liabilities

3.8 Financial Instruments

Set out below is the comparison by category of carrying amounts and fair values of all the Company's financial instruments that are carried in the Financial Statements.

Financial assets	At 31 December 2020 US\$m	At 31 December 2019 US\$m
Carrying amount and fair value		
<i>Financial assets at amortised cost</i>		
Cash and cash equivalents	15.5	120.4
Trade receivables	16.1	22.2
Amounts receivable from group companies	31.4	10.2
Other receivables	2.3	5.7
Joint operation receivables	13.1	23.5
Accrued underlift	-	15.1
<i>Derivative financial instruments</i>		
Financial assets – hedge options	0.2	4.1
	78.6	201.2

Due to the short-term nature of financial assets held at amortised cost, their carrying amount is considered to be the same as the fair value. There are no material impairments of financial assets held on the balance sheet at either 31 December 2019 or 2020.

All the Company's financial assets are expected to mature within one year. (2019: all less than one year).

Financial liabilities	At 31 December 2020 US\$m	At 31 December 2019 US\$m
Carrying amount and fair value		
<i>Financial liabilities at amortised cost</i>		
Trade payables	8.7	-
Joint operation payables	28.4	40.2
Amounts payable to group companies	7.6	7.2
Accruals and other payables	15.6	10.5
Lease liabilities/Finance lease liability	234.0	275.0
<i>Derivative financial instruments</i>		
Financial liabilities – hedge options	3.2	1.6
	297.5	334.5

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Section 3 – Working Capital, Financial Instruments and Long-term Liabilities

3.8 Financial Instruments (continued)

The fair value of financial assets and liabilities, other than the hedge options, has been calculated by discounting the expected future cash flows at prevailing interest rates.

Maturity analysis

The expected financial maturity of the Company's financial liabilities at 31 December 2020 is as follows:

	< 1 year US\$m	1-2 years US\$m	2-5 years US\$m	>5 years US\$m
<i>Financial liabilities at amortised cost</i>				
Trade payables	8.7	-	-	-
Joint operation payables	28.4	-	-	-
Amounts payable to group companies	7.6	-	-	-
Accruals and other payables	15.6	-	-	-
Lease liabilities	40.9	41.1	89.6	62.4
Financial liabilities – hedge options	3.2	-	-	-
	104.4	41.1	89.6	62.4

The expected financial maturity of the Company's financial liabilities at 31 December 2019 is as follows:

	< 1 year US\$m	1-2 years US\$m	2-5 years US\$m	>5 years US\$m
<i>Financial liabilities at amortised cost</i>				
Amounts payable to group companies	7.2	-	-	-
Joint operation payables	40.2	-	-	-
Accruals and other payables	10.5	-	-	-
Lease liabilities	41.0	40.9	123.0	70.1
Financial liabilities – hedge options	1.6	-	-	-
	100.5	40.9	123.0	70.1

Fair value

The Company holds hedge options which are held at fair value determined by models which have observable inputs.

The Company held the following financial instruments measured at fair value:

	At 31 December 2020 US\$m	At 31 December 2019 US\$m
Assets measured at fair value – Level 2		
<i>Derivative financial instruments</i>		
Financial assets – hedge options	0.2	4.1
Liabilities measured at fair value – Level 2		
<i>Derivative financial instruments</i>		
Financial liabilities – hedge options	(3.2)	(1.6)
	3.0	2.5

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Section 3 – Working Capital, Financial Instruments and Long-term Liabilities

3.9 Financial Risk Management: Objectives and Policies

The main risks arising from the Company's financial instruments are commodity price risk, liquidity risk, credit risk and foreign currency risk. The Board of Cairn Energy PLC, through the Treasury Sub-Committee, reviews and agrees policies for managing each of these risks and these are summarised below.

Cairn Energy PLC's Treasury function and Executive Team as appropriate are responsible for managing these risks, in accordance with the policies set by the Board. Management of these risks is carried out by monitoring of cash flows, investment and funding requirements using a variety of techniques. These potential exposures are managed while ensuring that the Company has adequate liquidity at all times in order to meet its immediate cash requirements. There are no significant concentrations of risks unless otherwise stated. The Company does not enter into or trade financial instruments, including derivatives, for speculative purposes.

The primary financial assets and liabilities comprise cash, short and medium-term deposits, money market liquidity funds, intra-group loans and other receivables and financial liabilities held at amortised cost. The strategy has been to finance operations through a mixture of retained profits, bank borrowings and other production related streaming agreements. Other alternatives such as equity issues and other forms of non-investment-grade debt finance are reviewed by the Board, when appropriate.

Commodity price risk

Commodity price risk arises principally from the Company's North Sea production, which could adversely affect revenue and debt availability due to changes in commodity prices.

The Company measures commodity price risk through an analysis of the potential impact of changing commodity prices. Based on this analysis and considering materiality and the potential business impact, the Company may choose to hedge.

Linked to production in the UK North Sea, the Company continued to hedge during 2020 in order to protect debt capacity and support committed capital programmes. Details of current hedging arrangements, together with oil price sensitivity analysis, can be found in note 3.5.

Transacted derivatives are designated, where possible, in cash flow hedge relationships to minimise accounting income statement volatility. The Company is required to assess the likely effectiveness of any proposed cash flow hedging relationship and demonstrate that the hedging relationship is expected to be highly effective prior to entering into a hedging instrument and at subsequent reporting dates.

Liquidity risk

The Company closely monitors and manages its liquidity risk using both short and long-term cash flow projections, supplemented by debt and equity financing plans and active portfolio management. Cash forecasts are regularly produced and sensitivities run for different scenarios including, but not limited to, changes in asset production profiles and cost schedules.

The operations of the Company have been impacted by COVID-19 and increased oil price volatility throughout 2020. The Company has deferred capital expenditure to preserve liquidity during this period of uncertainty. The Company runs various sensitivities on its liquidity position throughout the year. This includes scenarios forecasting a prolonged economic downturn as a result of COVID-19 and further volatility in oil prices.

Details of the Company's debt facilities can be found in note 3.2. The Company as part of the Cairn Energy PLC Group is subject to quarterly forecast liquidity tests as part of the RBL facility agreement. The Company has complied with the liquidity requirements of this test at all times during the year.

The Company currently has surplus cash that is invested in a combination of money market liquidity funds and term deposits with a number of international and UK financial institutions, ensuring sufficient liquidity to enable the Company to meet its short and medium-term expenditure requirements.

Credit risk

Credit risk arises from cash and cash equivalents, investments with banks and financial institutions, trade receivables and joint operation receivables.

Customers and joint operation partners are subject to a risk assessment using publicly available information and credit reference agencies, with follow-up due diligence and monitoring if required.

Investment credit risk for investments with banks and other financial institutions is managed by the Group Treasury function in accordance with the Board-approved policies of Cairn Energy PLC. These policies limit counterparty exposure, maturity, collateral and take account of published ratings, market measures and other market information. The limits are set to minimise the concentration of risks and therefore mitigate the risk of financial loss through counterparty failure.

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Section 3 – Working Capital, Financial Instruments and Long-term Liabilities

3.9 Financial Risk Management: Objectives and Policies (continued)

Credit risk (continued)

It is the Company's policy to invest with banks or other financial institutions that firstly offer the greatest degree of security and, secondly the most competitive interest rates. Repayment of principal is the overriding priority and this is achieved by diversification and shorter maturities to provide flexibility. The Board continually re-assesses the Company's policy and updates as required.

At the year end the Company does not have any significant concentrations of bad debt risk. The maximum credit risk exposure relating to financial assets is represented by the carrying value as at the balance sheet date.

Foreign currency risk

The Company manages exposures that arise from non-functional currency receipts and payments by matching receipts and payments in the same currency and actively managing the residual net position.

Where residual net exposures do exist and they are considered significant, the Company may from time to time opt to use derivative financial instruments to minimise exposure to fluctuations in foreign exchange and interest rates.

The following table demonstrates the sensitivity to movements in the US\$:GBP exchange rate, with all other variables held constant, on the Company's monetary assets and liabilities. These are considered to be reasonably possible changes for the purposes of sensitivity analysis. The Company's exposure to foreign currency changes for all other currencies is not material.

	At 31 December 2020		At 31 December 2019	
	Effect on loss before tax US\$m	Effect on equity US\$m	Effect on loss before tax US\$m	Effect on equity US\$m
10% increase in GBP to US\$	(18.7)	(18.7)	(16.3)	(16.3)
10% decrease in GBP to US\$	18.7	18.7	16.3	16.3

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Section 4 – Income Statement Analysis

4.1 Operating Profit

The Company's auditors' remuneration for 2020 was US\$42,047 (2019: US\$37,035). The Company had additional timewriting audit services provided by the auditors of US\$42,506 (2019 US\$83,840). Auditors' remuneration for other services for the Cairn Energy PLC Group is disclosed in the financial statements of the ultimate parent undertaking.

The Company has a policy in place for the award of non-audit work to the auditors which requires Audit Committee approval. No such costs were incurred by the Company during the year (2019: US\$nil).

Remuneration of key management personnel

The directors of the Company are also directors of other companies in the Cairn Energy PLC Group. The directors received remuneration for the year as shown in note 6.5 which was paid by other companies in the Group. The directors do not believe that it is practicable to apportion this amount between their services as directors of the Company and their services as directors of Cairn Energy PLC and fellow subsidiary companies. There are no agreements between the Company and the Board of Directors.

Employees

The Company has no employees (2019: none).

4.2 Finance Income

	Year ended 31 December 2020 US\$m	Year ended 31 December 2019 US\$m
Bank and other interest receivable	-	0.5
Interest receivable from group companies	4.2	4.7
Exchange gain	-	10.3
	4.2	15.5

4.3 Finance Costs

	Year ended 31 December 2020 US\$m	Year ended 31 December 2019 US\$m
Loan interest and facility fee amortisation	-	3.5
Interest payable to group companies	0.3	6.1
Other finance charges	1.9	3.3
Unwinding of discount - provisions	2.9	2.6
Lease interest	13.1	14.9
Exchange loss	5.7	-
	23.9	30.4

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Section 5 – Taxation

Significant accounting judgements in this section:

Deferred taxation

At each reporting date, the Company reviews unused tax losses and allowances to assess whether it is probable that taxable profits will be available against which the Company can utilise these losses and allowances and whether or not a deferred tax asset should be recognised.

At 31 December 2019 and 2020, the Company concluded that no deferred tax asset should be recognised. Impairment tests performed on its producing assets at both balance sheet dates determined that assets were held at or close to their recoverable value. No deferred tax asset can therefore be recognised as it is unlikely that there will be further profits available against which a deferred tax asset could be recovered.

Key estimates and assumptions in this section:

In determining whether future taxable profits are available to recognise deferred tax assets, the Company uses the same economic models that are used for impairment testing. The key assumptions are therefore consistent with those detailed in section 2.

Accounting policy

The total tax charge or credit represents the sum of current tax and deferred tax.

The current tax charge is based on the taxable profit for the year. Taxable profit differs from net profit as reported in the Income Statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. Where there are uncertain tax positions, the Company assesses whether it is probable that the position adopted in tax filings will be accepted by the relevant tax authority, with the results of this assessment determining the accounting that follows. If it is not considered probable that the income tax filing position will be accepted by the tax authority, the uncertainty is reflected within the carrying amount of the applicable tax asset or liability by using either the most likely amount or an expected value of the tax treatment, depending on which method is considered to better predict the resolution of the uncertainty, based on the underlying facts and circumstances.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the Financial Statements and the corresponding tax bases used in the computation of taxable profit or loss.

Deferred tax assets are recognised for deductible temporary differences that exist only where it is probable that taxable profits will be generated against which the carrying value of the deferred tax asset can be recovered.

Deferred tax liabilities are recognised for all taxable temporary differences except in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint operations where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

A deferred tax asset or liability is not recognised if a temporary difference arises on initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss. However, where the recognition of an asset is associated with an interest in a joint operation, which applies to all the Company's intangible exploration/appraisal asset and property, plant & equipment – development/producing asset additions, and the Company is not able to control the timing of the reversal of the temporary difference or the temporary difference is expected to reverse in the foreseeable future, a deferred tax asset or liability shall be recognised.

Current and deferred tax is calculated using tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

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Section 5 – Taxation

5.1 Tax Charge on Profit for the Year

Factors affecting tax charge for the year

A reconciliation of the income tax charge applicable to the profit before income tax to the UK statutory rate of income tax is as follows:

	Year ended 31 December 2020 US\$m	Year ended 31 December 2019 US\$m
Profit before taxation from continuing operations	20.0	618.7
Profit before tax multiplied by the UK statutory rate of corporation tax of 19% (2019: 19%)	3.8	117.6
Effect of:		
Special tax rates and reliefs applying to oil and gas activities	(16.4)	61.9
Impact on deferred tax of adjustments in respect of prior years	(2.0)	(3.3)
Temporary differences not recognised	16.1	(121.1)
Permanent items (non-taxable)/non-deductible	(0.9)	(51.9)
Tax losses (claimed from)/ surrendered to other group companies	(0.6)	(3.2)
Total tax charge on profit from continuing operations	-	-

The reconciliation shown above has been based on the average UK statutory rate of corporation tax for 2020 of 19% (2019: 19%).

The UK main rate of corporation tax is currently 19% (2019: 19%). In the Spring Budget 2020, the UK Government announced that from 1 April 2020 the corporation tax rate would remain at 19% (rather than reducing to 17%, as previously enacted). This new law was substantively enacted on 17 March 2020. Deferred taxes at the balance sheet date have been measured using these enacted tax rates and reflected in these financial statements. The applicable UK statutory tax rate applying to North Sea oil and gas activities is 40% (2019: 40%).

The effect of special tax rates and reliefs applying to oil and gas activities of US\$(16.4)m (2019: US\$61.9m) comprises US\$(8.0)m (2019: US\$65.7m) in respect of differences between the average UK statutory rate and the special rates applying to oil and gas activities in the UK and US\$(8.4)m (2019: US\$(3.8)m) in respect of the UK ring fence expenditure supplement ("RFES") claimed in the year.

The effect of temporary differences not recognised of US\$16.1m (2019: US\$(121.1)m) relates predominantly to the movement of the unrecognised deferred tax asset on UK decommissioning liabilities.

5.2 Deferred Tax Assets and Liabilities

Reconciliation of movement in deferred tax assets/(liabilities):

	Temporary difference in respect of non- current assets US\$m	Losses US\$m	Other temporary differences US\$m	Total US\$m
Deferred tax assets/(liabilities)				
At 1 January 2019	(243.6)	243.6	-	-
Deferred tax (charge)/credit through the Income Statement	(53.8)	(11.6)	65.4	-
At 31 December 2019	(297.4)	232.0	65.4	-
Deferred tax credit/(charge) through the Income Statement	57.0	(45.1)	(11.9)	-
At 31 December 2020	(240.4)	186.9	53.5	-

Recognised deferred tax assets

No deferred tax asset has been recognised at the Balance Sheet date on non-Ring Fence trading losses of US\$3.7m (2019: US\$3.7m); non trade loan relationship deficits of US\$nil (2019: US\$0.9m); on other ring fence temporary differences of US\$151.0m (2019: US\$116.0m) relating to decommissioning liabilities; or on activated investment allowances of US\$43.7m (2019 US\$nil) as it is not deemed probable that future profits will be available to recover the value of the asset given the detrimental change in market conditions continuing to impact the oil and gas industry.

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Section 6 – Capital Structure and Other Disclosures

6.1 Issued Capital and Reserves

Called-up share capital

Allotted, issued and fully paid ordinary shares	Number 20p ordinary '000	20p ordinary US\$m
At 1 January 2019, 31 December 2019 and 31 December 2020	92,023	24.9

Share premium

	2020 US\$m	2019 US\$m
At 1 January 2019, 31 December 2019 and 31 December 2020	93.0	93.0

Hedge reserve

The hedge reserve at 31 December 2020 of US\$(3.4)m (2019 US\$0.4m) has arisen on commodity price hedging, see note 3.5 for full details. The hedge reserve is used to recognise the effective portion of gains or losses on the derivatives that are designated for, and qualify as, cash flow hedges.

6.2 Capital Management

The objective of the Company's capital management structure is to ensure that there remains sufficient liquidity within the Company to carry out committed work programme requirements. The Company monitors the long-term cash flow requirements of the business in order to assess the requirement for changes to the capital structure to meet that objective and to maintain flexibility. The Company, as part of the Cairn Energy PLC Group, is subject to quarterly forecast liquidity tests as part of the RBL facility. The Company has complied with the capital requirements of this test at all times during the year.

The Company manages the capital structure and makes adjustments to it in light of changes to economic conditions. No significant changes were made in the objectives, policies or processes during the year ended 31 December 2020.

Capital and net debt, including lease liabilities, was as follows:

	At 31 December 2020 US\$m	At 31 December 2019 US\$m
Continuing operations		
Amounts payable to group companies	7.6	7.2
Lease liabilities	234.0	275.0
Less cash and cash equivalents	(15.5)	(120.4)
Net debt	226.1	161.8
Equity	465.2	737.0
Capital and net funds less payables	691.3	898.8
Gearing ratio	32.7%	18.0%

Nautical Petroleum Limited

Section 6 – Capital Structure and Other Disclosures

6.3 Guarantees

Details of the Company's RBL facility can be found in note 3.2. On entering into the facility the Company granted cross-guarantees to each of the lenders.

6.4 Investments in Subsidiaries

Accounting policy

The Company's investments in subsidiaries are carried at cost less provisions resulting from impairment. In testing for impairment the carrying value of the investment is compared to its recoverable amount, being its fair value less costs of disposal. The fair value includes the discounted future net cash flows of oil and gas assets held by the subsidiary, using estimated cash flow projections over the licence period. For exploration assets, estimated discounted cash flows are risk-weighted for future exploration success.

Discounted future net cash flows are calculated using an estimated short-term oil price based on the forward curve and long-term oil price of US\$55/bbl unescalated (2019: long-term oil price of US\$65/bbl escalated at 2.0%), escalation for costs of 0.5% (2019: 2.0%) and a discount rate of 10% (2019: 10%). Full details on the assumptions used for valuing oil and gas assets can be found in section 2.

	Subsidiary undertakings US\$m	Total US\$m
Cost		
At 1 January 2019, 31 December 2019 and 31 December 2020	21.7	21.7
Impairment		
At 1 January 2019	6.1	6.1
Impairment charge	15.5	15.5
At 31 December 2019 and 31 December 2020	21.6	21.6
Net book value		
At 31 December 2018	15.6	15.6
At 31 December 2019	0.1	0.1
At 31 December 2020	0.1	0.1

At the year end, investments in subsidiaries were reviewed for indicators of impairment. No such indicators were noted.

As at 31 December 2019 the Company's investments in Alba Resources Limited and Nautical Holdings Limited were impaired to reflect the fair value of their underlying assets. Charges of US\$5.8m and US\$9.7m relating to these respective companies were made to the Income Statement in 2019.

During 2020 liquidation of the Company's two Italian subsidiaries, Nautical Italia SRL and Transunion Petroleum Italia SRL was completed. As the investments in these two subsidiaries had been previously impaired down to the fair value of their assets, there was no gain or loss on their disposal on liquidation.

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6.4 Investments in Subsidiaries (continued)

The Company's subsidiaries as at the balance sheet date are set out below. The Company holds 100% of the voting rights and beneficial interests in the ordinary shares of the following companies:

Direct holdings	Business	Country of incorporation	Country of operation	Registered office address
Agora Oil and Gas (UK) Limited	Exploration	Scotland	UK	50 Lothian Road, Edinburgh, EH3 9BY
Alba Resources Limited*	Exploration	Scotland	UK	50 Lothian Road, Edinburgh, EH3 9BY
Nautical Holdings Limited	Holding company	England	UK	Wellington House 4th Floor, 125 The Strand, London, WC2R 0AP
Indirect holdings	Business	Country of incorporation	Country of operation	Registered office address
Nautical Petroleum AG ^	Production	Switzerland	UK	Baarerstrasse 8, 6300 Zug, Switzerland
UAH Limited	Holding company	England	UK	Wellington House 4th Floor, 125 The Strand, London, WC2R 0AP

* Company is in the process of liquidation at the balance sheet date

^ Company was in the process of liquidation at the year end and the liquidation completed in February 2021

6.5 Related Party Transactions

The Company's subsidiaries are listed in note 6.4. The following table provides the Company's balances which are outstanding with group companies at the balance sheet date:

	At 31 December 2020 US\$m	At 31 December 2019 US\$m
Amounts payable to subsidiary undertakings	(7.6)	(7.2)
Amounts receivable from parent companies	31.4	10.2
	23.8	3.0

The amounts outstanding are unsecured and repayable on demand and will be settled in cash. Interest, where charged, is at market rates. No guarantees have been given.

The following table provides the Company's transactions with group companies recorded in the profit for the year:

	Year ended 31 December 2020 US\$m	Year ended 31 December 2019 US\$m
Amounts invoiced by group companies	9.3	6.6
Amounts invoiced to group companies	52.3	5.3

Directors' remuneration

The remuneration of the Directors of the Company is set out below.

	Year ended 31 December 2020 US\$m	Year ended 31 December 2019 US\$m
Emoluments	3.4	3.5
Share-based payments	0.6	-
	4.0	3.5

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6.5 Related Party Transactions (continued)

Pension contributions were made on behalf of Directors in 2020 of US\$0.2m (2019: US\$0.2m).

389,169 LTIP share awards to Directors vested during 2020 (2019: none). Share-based payments shown above represent the market value at the vesting date of these awards.

Other transactions

During the year the Company did not make any purchases in the ordinary course of business from an entity under common control (2019: US\$nil).

Dividends

Dividends of US\$288.0m were declared and distributed by the Company in respect of the year ended 31 December 2020 and was settled by offset against loans due by the Company's parent company, Capricorn Energy Limited (2019: US\$269.2m).

During 2019 the Company received dividends of US\$279.9m from various subsidiaries as follows: Nautical Holdings Limited US\$125.2m, UAH Limited US\$41.6m and Alba Resources Limited US\$6.2m, all of which were settled by assignation of inter-company receivables. An additional distribution was recorded in the 2019 Income Statement of US\$106.9m from Agora Oil and Gas (UK) Limited which was settled by forgiving a debt to that company by the Company.

6.6 Ultimate Parent Company

The Company is a wholly-owned subsidiary of Capricorn Energy Limited and of its ultimate parent, Cairn Energy PLC. The results of the Company are consolidated into Cairn Energy PLC, registered in Scotland, whose principal place of business is at 50 Lothian Road, Edinburgh, EH3 9BY.

Copies of Cairn Energy PLC's financial statements are available to the public and may be obtained from the above mentioned address.

6.7 Event after the Balance Sheet Date

Sale of the Company's interests in the Catcher and Kraken Producing Assets

On 8 March 2021, the Company entered into an agreement that will result in the sale of its interests in the UK Catcher and Kraken producing assets to Waldorf Production Limited for a cash consideration of US\$460m plus additional contingent consideration dependent principally on oil prices from 2021 to the end of 2025. The consideration is subject to adjustments for working capital and other customary interim period adjustments from the economic effective date of 1 January 2020. As at 31 December 2020, the interim period and working capital adjustments were approximately US\$144m. On completion of the deal, derecognition of deferred tax assets, currently offsetting deferred tax liabilities, is expected to result in a loss after tax, which at the year-end was forecast to be approximately US\$140m.

The transaction is conditional upon, inter alia, the release of guarantees by the Company in favour of the OGA and FPSO contractors and OGA confirmation that its power to revoke licences will not be exercised on the change of control of the interests. The disposal is a Class 1 transaction for the Cairn Energy PLC Group and subject to Cairn Energy PLC shareholder approval.