CAIRN ENERGY EXPLORATION AND PRODUCTION COMPANY LIMITED

REPORT & FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

Cairn Energy Exploration and Production Company Limited

Directors·
W B B Gammell
J M Brown
M S Thoms
S J Thomson
M J Watts

Secretary.
D A Wood

Auditors
Ernst & Young LLP
Blenheim House
Fountainhall Road
Aberdeen AB15 4DT

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

Registered Office:
50 Lothian Road
Edinburgh EH3 9BY

Registered No:
SC234510

Cairn Energy Exploration and Production Company Limited

Report of the Directors

The Directors submit their Report and Financial Statements for the year ended 31 December 2007

Principal Activities and Business Review
The Company's principal activity is the exploration for oil and gas

In March 2005, pursuant to an asset sale and purchase agreement signed on 31 December 2004, the Company acquired a 15% interest in block GV ONN 97/1 in India where it was exploring for oil and gas

During the year the Company made a loss of $1,351,759 (2006 $511,749) No dividend has been paid or declared in respect of the year ended 31 December 2007 (2006 $nil)

Principal Risks and Uncertainties
The Company is subject to a variety of risks which derive from the nature of the oil and gas exploration business

The Company's future depends significantly upon its success in finding or acquiring and developing oil and gas reserves If the Company is unsuccessful, it would adversely affect the results of its operations and financial condition

The cost of drilling, completing and operating wells is often uncertain As a result, the Company may incur cost overruns or may be required to curtail, delay or cancel drilling operations because of many factors, including unexpected drilling conditions, pressure or irregularities in geological formations, equipment failures or accidents, adverse weather conditions, the need for compliance with environmental regulations, governmental requirements and shortages or delays in the availability of drilling rigs and the delivery of equipment

Post Balance Sheet Events
Subsequent to 31 December 2007 block GV ONN 97/1 has been relinquished

On 30 May 2008 the Company issued a further 1,004,483 ordinary shares of £1 each at par in settlement of a debt due to its immediate holding company

Financial Risk Management Policy
For detail of the Company's financial risk management policy see note 12

Directors
The Directors who held office during the year and subsequently are as follows

W B B Gammell	
J M Brown	(appointed 16 February 2007)
M S Thoms	
S J Thomson	(appointed 3 April 2007)
M J Watts	

Charitable Donations
The Company did not make any charitable contributions in the UK during the year (2006 $nil)

Creditors Payment Policy
It is the Company's payment policy to ensure settlement of suppliers' services in accordance with the terms of the applicable contracts In most circumstances, settlement terms are agreed prior to business taking place

Disclosure of Information to Auditors
The directors of the Company who held office at 31 December 2007 confirm, as far as they are aware, there is no relevant audit information of which the Company's auditors are unaware In making this confirmation, the directors have taken appropriate steps to make themselves aware of the relevant audit information and that the Company's auditors are aware of this information

Cairn Energy Exploration and Production Company Limited

Report of the Directors (continued)

Resolutions

The Company has passed elective resolutions to dispense with the requirements to

Lay accounts before the company's shareholders in annual general meeting

Hold annual general meetings

By Order of the Board

Secretary

50 Lothian Road
Edinburgh EH3 9BY

24 October 2008

Cairn Energy Exploration and Production Company Limited

Directors' Responsibility Statement

The directors are responsible for preparing the Company financial statements in accordance with applicable laws and regulations

UK company law requires the directors to prepare Company financial statements for each financial year Under such law the directors are required to prepare the Company financial statements in accordance with IFRS (as adopted by the EU)

The Company financial statements are required by law and IFRS (as adopted by the EU) to present fairly the financial position and performance of the Company, the Companies Act provides in relation to such financial statements that references in the relevant part of the Companies Act to financial statements giving a true and fair view, are references to their achieving a fair presentation

In preparing the Company financial statements, the directors are required to

- select suitable accounting policies and apply them consistently,
- make judgements and estimates that are reasonable and prudent,
- state whether they have been prepared in accordance with IFRS (as adopted by the EU), and
- prepare the financial statements on the going concern basis unless it is inappropriate to assume that the Company will continue in business

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that its financial statements comply with the Companies Act They have a general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and to prevent and detect fraud and other irregularities

The directors confirm that, to the best of their knowledge and belief

- the financial statements have been prepared in accordance with the standards summarised above, give a true and fair view of the assets, liabilities and financial position of the Company's affairs as at 31 December 2007 and of its loss for the year then ended, and
- the Directors Report includes a fair review of the development and performance of the Company's business and a description of the principal risks and uncertainties that it faces

Independent Auditors' Report

To the members of Cairn Energy Exploration and Production Company Limited

We have audited the financial statements of Cairn Energy Exploration and Production Company Limited for the year ended 31 December 2007 which comprise the Income Statement, the Balance Sheet, the Statement of Cash Flows, the Statement of Recognised Income and Expense and the related notes 1 to 17 These financial statements have been prepared under the accounting policies set out therein

This report is made solely to the company's members, as a body, in accordance with Section 235 of the Companies Act 1985 Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditors' report and for no other purpose To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the financial statements in accordance with applicable United Kingdom law and International Financial Reporting Standards (IFRSs) as adopted by the European Union are set out in the Statement of Directors' Responsibilities

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland)

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985 We also report to you whether the information given in the directors' report is consistent with the financial statements

In addition we report to you if, in our opinion, the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed

We read the directors' report and consider the implications for our report if we become aware of any apparent misstatements within it

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements

Opinion

In our opinion

- the financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the company's affairs as at 31 December 2007 and of its loss for the year then ended,
  the financial statements have been properly prepared in accordance with the Companies Act 1985, and
  the information given in the directors' report is consistent with the financial statements

Ernst & Young LLP

Ernst & Young LLP
Registered Auditor
Aberdeen

8
2~~4~~ October 2008

Cairn Energy Exploration and Production Company Limited

Income Statement

For the year ended 31 December 2007

Discontinued operations	Notes	**2007** **$**	2006 $
Administration expenses		**(7,142)**	(2)
Unsuccessful exploration costs		**(1,346,600)**	(504,813)
Operating loss	2	**(1,353,742)**	(504,815)
Finance income	3	**4,379**	
Finance costs	4	**(2,396)**	(6,934)
Profit before tax		**(1,351,759)**	(511,749)
Taxation	5		
Loss for the year attributable to the equity holders	11	**(1,351,759)**	(511,749)

Cairn Energy Exploration and Production Company Limited

Statement of Recognised Income and Expense

For the year ended 31 December 2007

	Notes	**2007** **$**	2006 $
Loss for the year	11	**(1,351,759)**	(511,749)
Total recognised income and expense for the year		**(1,351,759)**	(511,749)

Cairn Energy Exploration and Production Company Limited

Balance Sheet

As at 31 December 2007

	Notes	2007 $	2006 $
Non current assets			
Intangible exploration/appraisal assets	6		754,352
			754,352
Current assets			
Trade and other receivables	7	**81,996**	97,864
Cash and cash equivalents	8	**9,881**	7,714
		91,877	105,578
Total assets		**91,877**	859,930
Current liabilities			
Trade and other payables	9	**1,538,395**	954,689
Total liabilities		**1,538,395**	954,689
Net liabilities		**(1,446,518)**	(94,759)
Equity			
Called up share capital	10	**417,199**	417,199
Retained earnings	11	**(1,863,717)**	(511,958)
Total equity attributable to the equity holders		**(1,446,518)**	(94,759)

Signed on behalf of the Board on 24 October 2008

Director

Cairn Energy Exploration and Production Company Limited

Statement of Cash Flows

For the year ended 31 December 2007

	Note	2007 $	2006 $
Cash flows used in operating activities			
Loss for year		**(1,351,759)**	(511,749)
Unsuccessful exploration costs		**1,346,600**	504,813
Finance income		**(4,379)**	
Finance costs		**2,396**	6,934
Trade and other payables movement		**(27,564)**	
Waiver of inter group debt			2
Net cash used in operating activities		**(34,706)**	
Cash flows used in investing activities			
Expenditure on exploration/appraisal assets		**(559,400)**	(469,788)
Interest received		**257**	
Net cash used in investing activities		**(559,143)**	(469,788)
Cash flows from financing activities			
Interest paid		**(1,315)**	
Bank charges		**(1,081)**	(535)
Proceeds from group borrowings		**598,412**	478,107
Net cash flows from financing activities		**596,016**	477,572
Net increase in cash and cash equivalents		**2,167**	7,784
Opening cash and cash equivalents at beginning of year		**7,714**	(70)
Closing cash and cash equivalents	8	**9,881**	7,714

1 Accounting Policies

a) Basis of preparation

The Company prepares its accounts on a historical cost basis Where there are assets and liabilities calculated on a different basis, this fact is disclosed in the relevant accounting policy The Company's ultimate holding company, Cairn Energy PLC, has confirmed it will make available sufficient funds to allow the Company to pay its liabilities as they fall due for the next twelve months Hence these accounts have been prepared on a going concern basis

b) Accounting standards

The Company prepares its accounts in accordance with applicable International Financial Reporting Standards (IFRS) as adopted by the EU

Relevant new standards and interpretations issued by the IASB, but not yet effective and not applied in these financial statements are as follows

Title	Change to accounting policy	Date of adoption by Cairn	Impact on initial application
Effective date from 1 January 2009			
Revised IAS 1 'Presentation of Financial Statements'	No changes to current accounting policy	1 Jan 2009	Presentation and disclosure requirements for certain items in the Income Statement

No other IFRS as issued by the IASB which are not yet effective are expected to have an impact on the Company's financial statements

During the year, the Company adopted IFRIC 8 'Scope of IFRS 2', amendment to IFRS 2 'Share based payment' Vesting Conditions and Cancellations", amendment to IAS 1 'Presentation of Financial Statements – Capital Disclosures', and IFRS 7 'Financial Instruments Disclosures', amendment to IAS 32 'Financial Instruments Disclosure and Presentation'

c) Presentational currency

The functional and presentational currency of Cairn Energy Exploration and Production Company Limited is US Dollars ("$") The Company's policy on foreign currencies is detailed in note 1(h)

d) Joint Ventures

The Company participates in an unincorporated Joint Venture which involves the joint control of assets used in the Company's oil and gas exploration activities The Company accounts for its share of assets, liabilities, income and expenditure of Joint Ventures in which the Company holds an interest, classified in the appropriate Balance Sheet and Income Statement headings The Company's principal licence interest is a jointly controlled asset

The company has an interest in the following unincorporated joint venture

	Working interest
GV ONN 97/1	15 0%

Subsequent to 31 December 2007 this block has been relinquished

e) Other income

Interest income is recognised using the effective interest method on an accruals basis and is recognised within 'Finance Income' in the Income Statement

1 Accounting Policies (continued)

f) Oil and gas intangible exploration/appraisal assets and property, plant & equipment development/producing assets

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

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

Exploration expenditure incurred in the process of determining exploration targets is capitalised initially within exploration/appraisal assets and subsequently allocated to drilling activities Exploration/appraisal drilling costs are initially 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

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

All costs incurred after the technical feasibility and commercial viability of producing hydrocarbons has been demonstrated 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

Net proceeds from any disposal of an exploration asset are initially credited against the previously capitalised costs Any surplus proceeds are credited to the Income Statement Net proceeds from any disposal of development/producing assets are credited against the 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 exceed or are less than the appropriate portion of the net capitalised costs of the asset

Depletion

The Company depletes separately, where applicable, any significant components within development/producing assets, such as fields, processing facilities and pipelines which are significant in relation to the total cost of a development/producing asset

The Company depletes expenditure on property, plant & equipment development/producing assets on a unit of production basis, based on proved and probable reserves on a field by field basis In certain circumstances, fields within a single development area may be combined for depletion purposes

Impairment

Exploration/appraisal assets are reviewed regularly for indicators of impairment and costs are written off where circumstances indicate that the carrying value might not be recoverable In such circumstances the exploration asset is allocated to development/producing assets within the same geographic segment and tested for impairment Any such impairment arising is recognised in the Income Statement for the period Where there are no development/producing assets within a geographic segment, the exploration/appraisal costs are charged immediately to the Income Statement

Impairment reviews on development/producing assets are carried out on each cash generating unit identified in accordance with IAS 36 "Impairment of Assets" The Company's cash generating units are those assets which generate largely independent cash flows and are normally, but not always, single development areas

1 Accounting Policies (continued)

f) **Oil and gas intangible exploration/appraisal assets and property, plant & equipment development/producing assets (continued)**

Impairment (continued)

At each reporting date, where there are indicators of impairment, the net book value of the cash generating unit is compared with the associated expected discounted future net cash flows If the net book value is higher, then the difference is written off to the Income Statement as impairment Discounted future net cash flows for IAS 36 purposes are calculated using an estimated oil price of $60/bbl (2006 $30/bbl) or the appropriate gas price as dictated by the relevant gas sales contract, escalation for prices and costs of 3% and a discount rate of 10% (2006 3% and 10% respectively) Forecast production profiles are determined on an asset by asset basis, using appropriate petroleum engineering techniques

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 discounted future net cash flows are 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 periods

g) **Financial instruments**

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another

Financial assets are categorised as financial assets held at fair value through profit or loss, held to maturity investments, loans and receivables and available for sale financial assets The Company holds financial assets which are classified as loans and receivables

Financial liabilities generally substantiate claims for repayment in cash or another financial asset Financial liabilities are categorised as either fair value through profit or loss or held at amortised cost All of the Company's financial liabilities are held at amortised cost

Financial instruments are generally recognised as soon as the Company becomes party to the contractual regulations of the financial instrument

Loans and other receivables

Trade receivables, loans and other receivables that have fixed or determinable payment that are not quoted on an active market are classified as 'loans and receivables' Loans and receivables are measured at amortised cost using the effective interest method less any impairment Trade and other receivables are recognised when invoiced Interest income is recognised by applying the effective interest rate, except for short term receivables where the recognition of interest would be immaterial

The carrying amounts of loans and other receivables are tested at each reporting date to determine whether there is objective material evidence of impairment, for example overdue trade debt Any impairment losses are recognised through the use of an allowance account When a trade receivable is uncollectible, it is written off against the allowance account Subsequent recoveries of amounts previously written off are credited against the allowance account Changes in the carrying amount of the allowance account are recognised in the Income Statement or Balance Sheet in accordance with where the original receivable was recognised

Cash and cash equivalents

Cash and cash equivalents comprise cash at bank and short term deposits with an original maturity of three months or less

For the purpose of the Statement of Cash Flows, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts

Trade payables and other non derivative financial liabilities

Trade payables and other creditors are non-interest bearing and are measured at cost

1 Accounting Policies (continued)

g) Financial instruments (continued)

Borrowing costs

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

h) Foreign currencies

Cairn translates foreign currency transactions into the functional currency, $, at the rate of exchange prevailing at the transaction date 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

i) Equity

Equity instruments issued by the Company are recorded at the proceeds received, net of direct issue costs, allocated between share capital and share premium

j) Taxation

The tax expense represents the sum of current tax and deferred tax

The current tax is based on taxable profit/ (loss) for the year Taxable profit/(loss) differs from net profit/(loss) 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 The Company's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the Balance Sheet date

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/ (loss)

Deferred income 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 Ventures 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 income tax 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

Deferred income tax assets are recognised for all deductible temporary differences, carry forward of unused tax assets and unused tax losses, to the extent that it is probable that taxable profits will be available against which the deductible temporary differences, carry forward of unused tax assets and unused tax losses can be utilised, except where the deferred income tax asset relating to the deductible temporary timing difference arises from the 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 In respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in Joint Ventures, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profits will be available against which the temporary differences can be utilised

The carrying amount of deferred income tax assets are reviewed at each Balance Sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the deferred income tax asset to be utilised

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the periods in which the asset is realised or the liability is settled, based on tax rates and laws enacted or substantively enacted at the Balance Sheet date

Deferred tax assets and liabilities are only offset where they arise within the same tax jurisdiction and the Company intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously

Cairn Energy Exploration and Production Company Limited

1 Accounting Policies (continued)

k) Key estimations and assumptions

The Company has used estimates and assumptions in arriving at certain figures within the financial statements The resulting accounting estimates may not equate with the actual results which will only be known in time Those areas believed to be key areas of estimation are noted below, with further details of the assumptions used listed at the relevant note

Item	**Refer to:**
Impairment testing	1(f)

2 Operating Loss

Auditors' remuneration

The Company's auditors' remuneration of $6,300 (2006 $6,000) has been borne by the ultimate holding company Cairn Energy PLC

The Company has a policy in place for the award of non audit work to the auditors which, in certain circumstances, requires Audit Committee approval Auditors' remuneration for other services is disclosed in the financial statements of Cairn Energy PLC, the ultimate parent undertaking

3 Finance Income

	2007 **$**	2006 $
Bank interest	**257**	
Realised exchange gain	**4,122**	
	4,379	

4 Finance Costs

	2007 **$**	2006 $
Loan interest payable	**1,315**	
Bank charges	**1,081**	535
Realised exchange loss		6,399
	2,396	6,934

5 Taxation

A reconciliation of the income tax expense applicable to the profit or loss before income tax at the applicable tax rate, to the income tax expense at the Company's effective tax rate, is as follows

	2007	2006
	$	$
Loss before taxation	**(1,351,759)**	(511,749)
Tax at the UK corporation tax rate of 30% (2006 30%)	**(405,528)**	(153,525)
Effects of		
Deferred tax not recognised	**368,259**	153,524
Impact of deferred tax rate change to 28%	**37,269**	
Non taxable income / non deductible expenses		1
Tax expense		

There is a deferred tax asset of $521,783 as at 31 December 2007 (2006 $153,524) in relation to fixed asset timing differences, pre trading expenditure and tax losses This asset has not been recognised as there is insufficient evidence that it will reverse in the foreseeable future This asset will be recoverable if the company generates sufficient taxable income in the future

6 Intangible Exploration/Appraisal Assets

	South Asia	**Total**
	$	**$**
Cost and net book value		
At 1 January 2006	496,591	**496,591**
Additions	762,574	**762,574**
Unsuccessful exploration costs	(504,813)	**(504,813)**
At 1 January 2007	754,352	**754,352**
Additions	592,248	**592,248**
Unsuccessful exploration costs	(1,346,600)	**(1,346,600)**
At 31 December 2007		
Net book value at 31 December 2007		
Net book value at 31 December 2006	754,352	754,352

Cairn Energy Exploration and Production Company Limited

Notes to the Accounts (continued)

For the year ended 31 December 2007

7 Trade and Other Receivables

	2007	2006
	$	$
Amounts owed by Group companies		1,473
Joint Venture debtors and prepayments	**81,996**	96,391
	81,996	97,864

All trade and other receivables at 31 December 2007 and 2006 are current and unimpaired

8 Cash and Cash Equivalents

	At 1 January 2007	Cash flow	Exchange movements	**At 31 December 2007**
	$	$	$	**$**
Cash at bank	7,714	2,167		**9,881**
Cash and cash equivalents	**7,714**	**2,167**		**9,881**

	At 1 January 2006	Cash flow	Exchange movements	At 31 December 2006
	$	$	$	$
Cash at bank		7,714		7,714
Bank overdraft	(70)	70		
Cash and cash equivalents	(70)	7,784		7,714

9 Trade and Other Payables

	2007	2006
	$	$
Amounts owed to Group companies	**1,121,939**	525,000
Joint Venture creditors and accruals	**416,456**	398,003
Other creditors and accruals		31,686
	1,538,395	954,689

10 Share Capital

	£1 Ordinary Number
Authorised ordinary shares	
At 31 December 2006 and 2007	**5,100,000**

	£1 Ordinary Number	£1 Ordinary $
Allotted, issued and fully paid ordinary shares		
At 1 January 2006	1	2
Issued during the year	213,554	417,197
At 31 Decemeber 2006	213,555	417,199
At 31 December 2007	**213,555**	**417,199**

On 28 June 2006 and 20 December 2006 the Company issued 23,215 and 190,339 fully paid ordinary shares of £1 each at par to Cairn Energy PLC and Capricorn Energy Limited respectively in settlement of inter company balances

On 30 May 2008 the Company issued a further 1,004,483 ordinary shares of £1 each at par in settlement of a debt due to its immediate holding company

11 Equity

	Equity share capital $	Retained earnings $	**Total $**
At 1 January 2006	2	(209)	**(207)**
Shares issued	417,197		**417,197**
Loss for year		(511,749)	**(511,749)**
At 1 January 2007	417,199	(511,958)	**(94,759)**
Loss for year		(1,351,759)	**(1,351,759)**
At 31 December 2007	**417,199**	**(1,863,717)**	**(1,446,518)**

12 Financial Risk Management Objectives and Policies

The Company's primary financial instruments comprise bank loans, cash and short and medium term deposits The Company's strategy has been to finance its operations through a mixture of retained profits and bank borrowings Other alternatives such as equity finance and project finance are reviewed by the Board, when appropriate, to fund substantial acquisitions or oil and gas projects

The Company's treasury function is responsible for managing investment and funding requirements including banking and cash flow monitoring It must also recognise and manage interest and foreign exchange exposure whilst ensuring that the Company has adequate liquidity at all times in order to meet its immediate cash requirements

The Company may from time to time opt to use derivative financial instruments to minimise its exposure to fluctuations in foreign exchange rates, interest rates and movements in oil and gas prices Derivative financial instruments have not been used throughout 2006 or 2007 It is, and has been throughout the year under review, the Company's policy that no trading in derivative financial instruments shall be undertaken

The main risks arising from the Company's financial instruments are liquidity risk, interest rate risk, foreign currency risk and credit risk The Board reviews and agrees policies for managing each of these risks and these are summarised below

Liquidity risk

The Company, through its immediate holding company Capricorn Energy Limited, has access to the available cash balances of the Capricorn Oil Limited Group ('Group') As at 31 December 2007 there were no credit facilities in place Subsequently, Capricorn Oil Limited has access, if so required, to the Cairn Energy PLC £30 million revolving credit facility to fund working capital This facility was signed on 28 March 2008 and expires on 31 January 2013 This facility is jointly provided by The Royal Bank of Scotland PLC and Bank of Scotland PLC Interest is charged at floating rates determined by LIBOR plus an applicable margin

In addition the Company has access to the Capricorn Oil Limited facilities to cover the issue of bank guarantees As at 31 December 2007 there were $35m of facilities in place of which $28 8m was unutilised In 2006 the Company had access to Cairn Energy PLC Group facilities of $45m, of which $28 9m was unutilised Fixed rates of interest apply to these

The Group currently has surplus cash which it has placed on short and medium term deposit, ensuring sufficient liquidity to enable the Group to meet its short/medium term expenditure requirements

Interest rate risk

Surplus funds are placed on short/medium term deposit at floating rates It is the Company's policy to deposit funds with banks or other financial institutions that offer the most competitive interest rate at time of issue

Short/medium term borrowing arrangements are available at floating rates The treasury function may from time to time opt to manage a proportion of the interest costs on this debt by using derivative financial instruments such as interest rate swaps At this time, however, there is no requirement for such instruments as there is no debt drawn

Foreign currency risk

The Company manages exposures that arise from receipt of revenues in foreign currencies, by matching receipts and payments in the same currency, and actively managing the residual net position

In order to minimise the Company's exposure to foreign currency fluctuations, currency assets are matched with currency liabilities by borrowing or entering into foreign exchange contracts in the applicable currency if deemed appropriate The loan facilities allow loans denominated in US Dollars, Sterling, Euro or such other currency as may be agreed between the lenders and Company from time to time

No forward foreign exchange contracts were entered into during 2007 (2006 $nil) There were no outstanding foreign exchange contracts at the start of the year or at the end of the year

12 Financial Risk Management Objectives and Policies (continued)

Credit risk

With respect to deposit and other treasury arrangements, as a general rule the Board will only approve a bank or financial institution that has a Moody's rating for long term deposits of A and above

The Board will continue to assess the Company's strategies for managing credit risks At the year end the Company does not have any significant concentrations of bad debt risk and overall the exposure to bad debts is not considered to be significant

Capital Management

The Company manages its capital structure and makes adjustments to it, in light of changes to economic conditions To maintain or adjust the capital structure, the Company may adjust the dividend payment to the parent, return capital, issue new shares for cash, repay debt or other such restructuring activities as appropriate

No changes were made in the objectives, policies or processes during the period ended 31 December 2007

As at 31 December 2007 capital and net debt were made up as follows

	2007	2006
	£	
Amounts owed to Group companies	**1,121,939**	525,000
Joint Venture creditors and accruals	**416,456**	398,003
Other creditors and accruals		31,686
Less cash and short term deposits	**(9,881)**	(7,714)
Net Debt	**1,528,514**	946,975
Equity	**(1,446,518)**	(94,759)
Capital and net debt	**81,996**	852,216
Gearing ratio	**1864%**	111%

13 Financial Instruments

The Company calculates the fair value of assets and liabilities by reference to amounts considered to be receivable or payable on the Balance Sheet date

The Company's financial assets, together with their fair values are as follows

Financial assets

	Carrying amount		**Fair value**	
	2007	2006	**2007**	2006
	$	$	**$**	$
Cash and cash equivalents	**9,881**	7,714	**9,881**	7,714
	9,881	7,714	**9,881**	7,714

The Company has no financial liabilities

13 Financial Instruments (continued)

The following table sets out the carrying amount, by maturity, of the Company's financial instruments that are exposed to interest rate risk

At 31 December 2007	Less than one year $	Total $
Floating rate		
Cash assets	9,881	9,881
	9,881	9,881

At 31 December 2006	Less than one year $	Total $
Floating rate		
Cash assets	7,714	7,714
	7,714	7,714

14 Capital Commitments

Oil and gas expenditure	**2007 $**	2006 $
Intangible exploration/appraisal assets	**828,526**	1,458,497
Contracted for	**828,526**	1,458,497

The above capital commitments represent the Company's share of obligations in relation to its interests in Joint Ventures As all Company joint ventures are jointly controlled assets, these commitments also represent the Company's share of the capital commitments of the Joint Ventures themselves

15 Related Party Transactions

The following table provides the total amount of transactions which have been entered into with Group companies

	2007 $	2006 $
Transactions		
Waiver of inter company balance		2
Balances at 31 December		
Amounts owed by Group companies		1,473
Amounts owed to Group companies	**(1,121,939)**	(525,000)
	(1,121,939)	(523,527)

Remuneration of key management personnel
No remuneration was paid to directors, who are the key management personnel of the Company, for services to this Company during the year (2006 $nil)

16 Ultimate Parent Company

The Company is a subsidiary of Capricorn Energy Limited The Company's ultimate holding company is 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

17 Post Balance Sheet Events

Subsequent to 31 December 2007 block GV ONN 97/1 has been relinquished

On 30 May 2008 the Company issued a further 1,004,483 ordinary shares of £1 each at par in settlement of a debt due to its immediate holding company