

Desire Petroleum

'Desire' or 'The Company'

Preliminary Results

Desire Petroleum plc (AIM:DES) the exploration company focusing on the North Falkland Basin, is pleased to announce its Preliminary Results for the year ended 31 December 2009.

Operational Highlights

- Secured Ocean Guardian rig for drilling campaign that commenced in February 2010
- Reduced costs by subcontracting rig to Rockhopper Exploration and BHP Billiton
- Successful completion of Liz 14/19-1 well culminating in gas discovery
- Drilling expected to resume in Q3 2010

Financial Highlights

- Raised c.£60m via Placing and Open Offer to fund drilling campaign
- Loss for the year was \$3.77 million
- Current cash at hand \$88 million

Commenting on the results Stephen Phipps, Chairman of Desire said:

“It has been an exciting year for Desire and the Company has made much progress in the period. Further detailed analysis on the Liz well is currently being carried out and we look forward to updating shareholders on the results when the analysis is completed within the next couple of months. We remain upbeat about the resource potential within the North Falkland Basin and look forward to recommencing drilling later this year.”

For further information please contact:

**Desire Petroleum plc** 020 7436 0423  
Stephen Phipps, Chairman  
Dr Ian Duncan, Chief Executive Officer

**Seymour Pierce Limited** 020 7107 8000  
Jonathan Wright

**Buchanan Communications** 020 7466 5000  
Tim Thompson  
Ben Romney  
Chris McMahon

## Chairman's Statement

Dear Shareholder,

The period since the last report and accounts has been an eventful one for Desire, culminating in a gas discovery on the Liz 14/19-1 well, the drilling of which was completed in early April 2010. Indeed in the short period beginning September last year, Desire has secured the services of the Ocean Guardian drilling rig, raised circa £ 60 million in a Placing and subsequent Open Offer to shareholders and successfully completed the first well to have been drilled in the North Falkland Basin for twelve years.

In my statement to you some twelve months ago I suggested then that Desire's biggest challenge in 2009 was to secure a "suitable rig at a suitable price from as close to the North Falkland Basin as possible". The softening in rig rates and greater rig availability as a result of the global recession enabled us to achieve our first two goals, if not the third. A suitable rig, the Ocean Guardian, was secured at a suitable price from Diamond Offshore Drilling (UK) Ltd in September 2009. However, the Ocean Guardian was located in the North Sea some 8,000 miles and 70 towing days distance from the Falklands. In the event the offer of a fixed mobilisation and demobilisation charge persuaded your Board to take the opportunity of using the Ocean Guardian drilling unit.

Having waited and watched both rig availability and rig rates move against us for some years your Board believed, and still believes, that Desire should try and drill as many wells as possible using the Ocean Guardian. To this end Desire undertook a successful Placing of 60 million shares at 70p per share in October 2009 and a subsequent 1 for 10 Open Offer to all shareholders at 70p which was completed in January 2010. The two share issues raised circa £ 60 million post expenses adding to our existing \$ 40 million cash balance.

In addition Rockhopper Exploration has subcontracted the rig to drill its two prospects, Sea Lion and Ernest, in the North Falkland Basin and BHP Billiton has subcontracted the rig to drill the Toroa prospect in the East Falkland Basin. The net effect of this is a sharing of the mobilisation/demobilisation costs to the benefit of all parties.

In conjunction with Desire's money raising, Senergy (GB) Ltd were commissioned to write a Competent Persons Report on Desire's top ten prospects, namely, Liz, Ann, Alpha, Dawn, Jacinta, Beth, Ninky, Rachel, Helen and Pam. Their key conclusions are as follows; that the mean, net to Desire, unrisks prospective recoverable resources in those ten prospects is over 3 billion barrels; that the mean, gross, unrisks prospective recoverable resources in those ten prospects is over 4.6 billion barrels; and that the mean, gross, unrisks prospect size ranges from 122 million barrels recoverable (Ninky) to 1,631 million barrels recoverable (Alpha). The results of this report have further endorsed our view of the prospectivity of the North Falkland Basin. For those shareholders wishing for more details the Senergy (GB) Ltd report can be viewed on our website: [www.desireplc.co.uk](http://www.desireplc.co.uk).

However, notwithstanding the potential positives we see from our own geophysical work and from Senergy (GB) Ltd's independent report in to our prospects, only by drilling wells will we truly be able to unlock the potential of the North Falkland Basin. Our first well, the Liz 14/19-1 well was spudded on 22nd February 2010 with a target depth of 3,500 metres. After drilling to a depth of 3,667 metres the well was plugged and abandoned as a gas discovery, with 17 metres of net hydrocarbon pay between 2961 and 3031 metres within a zone of over-pressured, predominantly sandstone, reservoir. In addition dry gas was recovered from a deeper interval below 3,400 metres, good oil shows were encountered in the Liz fan and oil shows were encountered in the Beth fan. In each case though, reservoir quality was poor, and further detailed work will be undertaken to assess the results. A more detailed appraisal of the Liz well results will be included in the Annual Report and Accounts.

The Liz well proved to be complex yet it was highly encouraging. Hydrocarbons have been found in at least two separate intervals, the geological model for the basin has been confirmed and at least two petroleum systems have been found to be present, with hydrocarbon shows recorded over a wide interval. It was the first well to be drilled in a multi-

well campaign by Desire and, after more detailed technical work has been carried out, Desire will decide which play type is to be drilled next. The Ocean Guardian is now subcontracted to Rockhopper Exploration and BHP for three wells and Desire expects to resume drilling sometime in the third quarter of 2010.

The results for the year ended 31 December 2009 have been prepared under International Financial Reporting Standards (IFRS). The loss for the year was \$3,768,000.

Administrative expenses at \$1,103,000 were lower than last year, due to a combination of the strengthening of the US dollar, and lower underlying costs. The majority of administrative expenses are incurred in pounds sterling, so exchange rate movements will influence the dollar presentation. The translated pound equivalent charge for the year of £708,000 compares with £789,000 in 2008.

The non-cash charge for share-based payments at \$82,000 is lower than the 2008 level, as the economic cost of share-based compensation plans is now largely expensed.

The majority of the Company's funds have long been held in US dollars, to match expected expenditure on future exploration programmes. The Company's US dollar balances increased from \$ 39 million to \$47 million during the year, of which \$25 million is held in escrow accounts. With the Ocean Guardian drilling rig having in the event been mobilised from, and being operated out of, the UK, a significant element of the 2010 exploration programme will now be incurred in Pounds Sterling.

As a result of the share placing in November 2009, the Company's Sterling balances increased from £1.5 million to £ 41 million. The exchange loss for the year of \$2,731,000 arises on these Sterling balances, and follows a weakening of the pound against the dollar between the share placing date and the year-end.

Investment income of \$148,000 is significantly lower than the corresponding period, with both US dollar and Sterling interest rates at historically low levels.

Finally, it remains for me to thank my colleagues and our two main contractors, AGR who run our drilling operations, and Senegy (GB) Ltd, who provide us with our geoscience support, for their excellent work over the last year. Together we look forward to resuming drilling in the North Falkland Basin later this year.

Yours sincerely,

Stephen L Phipps

## **Report of the Directors**

The directors present their report to the audited financial statements for the year ended 31 December 2009.

### **Principal activities**

The principal activity of the Group for the year continued to be that of oil and gas exploration.

### **Business review**

The Company is required by the Companies Act to set out in this report a fair review of the business of the Group during the financial year ended 31 December 2009 and of the position of the Group at the end of the year and a description of the principal risks and uncertainties facing the Group. The information that fulfils the requirements of the business review can be found within the Chairman's Statement and Technical Review. These include details of expected future developments in the business of the Group. The Directors do not believe that there are any significant key performance indicators that are relevant to the Group at present.

### **Dividends**

The Directors do not recommend payment of a dividend (2008-\$nil).

### **Share capital**

On 27 April 2009, options were exercised over 1,195,600 shares and these were subsequently allotted. The option exercises raised \$375,480.

On 10 November 2009, the Company issued 60,000,000 shares under a placing at a subscription price of 70 pence per share. In this respect the Company raised \$66.5 million, net of costs.

Following the year end, on 12 January 2010, the Company issued 28,971,544 shares under an open offer at a subscription price of 70 pence per share, raising \$32.7 million, net of costs.

On 2 February 2010, options were exercised over 7,203,583 shares, and these were subsequently allotted, raising \$3,746,677.

### **Directors and their interests**

On the 4 February 2009, Mr D L Clifton resigned as a Director.

The interests of the Directors who served at the end of the year in the ordinary shares of the Company are shown within the Report of the Remuneration and Nomination Committees section of this announcement.

Mr A G Windham and Mr S L Phipps retire by rotation at the Annual General Meeting and, being eligible, offer themselves for re-election.

Details of the Directors' interests in contracts with the Group are set out in note 23 to the accounts.

## Special business – Annual General Meeting resolutions

Items 5 and 6 of the Notice of the forthcoming Annual General Meeting contain resolutions which renew and extend existing authorisations for a further year. The Directors believe that they should have the authorities proposed under items 5 and 6 in order to take advantage of business opportunities as they arise, thus maintaining a desirable degree of flexibility.

- 5 Under the Companies Act 2006, the Directors are prohibited from allotting securities of the Company without prior authorisation from shareholders to do so. The effect of this resolution is to give the Directors authority until the 2011 Annual General Meeting to allot relevant securities up to an aggregate nominal amount of £325,891.
- 6 The Companies Act 2006 also provides that, unless shareholders otherwise consent, all new equity securities to be offered for cash must first be offered to existing shareholders in proportion to their individual holdings. The effect of this resolution is to give the Directors authority, until the 2011 Annual General Meeting, to allot equity securities for cash, other than to existing shareholders, up to a limited aggregate nominal amount of £162,946.

## Substantial shareholdings

As at 10 March 2010 the Company had been notified of the following holdings of 3% or more of its issued share capital:

	Number of ordinary shares	%
Phipps & Company Limited	33,532,633	10.29
Barclayshare Nominees Limited	21,531,162	6.61
TD Warehouse Nominees (Europe) Limited	18,810,763	5.77
HSDL Nominees Limited	10,856,979	3.33
LR Nominees Limited	10,328,998	3.17

## Corporate governance

The Combined Code Principles of Good Governance and Code of Best Practice is not mandatory for companies traded on the Alternative Investment Market of the London Stock Exchange. However, the Directors are committed to applying the requirements of the Code where they are considered appropriate. This statement explains how the Group has applied the principles of the Code throughout the year. The Board meets regularly throughout the year and is responsible for the overall Group strategy, acquisition and divestment policy, approval of major capital expenditure and consideration of significant financing matters. It reviews the strategic direction of individual trading companies, their annual budgets, their progress toward achievement of these budgets and their capital expenditure programmes.

## Status of non-executive directors

None of the non-executive directors would be deemed independent under the Combined Code. However, the non-executive directors have considerable experience in the Oil & Gas sector which the Company draws upon on a regular basis. In addition, the non-executive directors are sufficiently independent of management so as to be able to exercise independent judgment and bring an objective viewpoint and, thereby, protect and promote the interests of shareholders.

## **Going concern**

It is the opinion of the Board that both the Group and the Company have adequate resources to continue in operational existence for the foreseeable future, being twelve months from the date of approval of the financial statements. For this reason, the Board has adopted the going concern basis in preparation of the financial statements.

## **Qualifying third party indemnity provisions**

The Company's articles of association contain qualifying indemnity provisions under which each director shall be entitled to be indemnified by the Company in respect of certain liabilities which may attach to him in his capacity as a director of the Company. These provisions were in force throughout the year and remain in force at the date of this report.

## **Audit Committee**

The Audit Committee was chaired by Mr E Wisniewski and included Mr A G Windham and Mr R Lyons as members throughout the year. Mr D L Clifton resigned from the Committee on 4 February 2009.

The Committee convenes twice a year and its terms of reference include the review of the Annual and Interim Accounts, accounting policies of the Company and its subsidiaries, internal management and financial controls, and the planning, scope and results of the Auditor's programme. UHY Hacker Young Manchester LLP attend the meetings at the request of the Committee.

Following approval of this Annual Report, Clive Maudsley of auditors UHY Hacker Young Manchester LLP will have acted as audit engagement partner to the Group for five years. The Audit Committee have reviewed this situation in accordance with APB Ethical Standard 3 (Revised) 'Long Association with The Audit Engagement' and consider that, at this time of substantial change in the business, and in the interests of audit quality, Clive Maudsley should remain as audit engagement partner for a further period not exceeding two years. This has been proposed to UHY Hacker Young Manchester LLP and they have agreed to this proposal.

## **Remuneration Committee and Nomination Committee**

The Remuneration Committee is chaired by Mr A G Windham and included Mr E Wisniewski and Mr R Lyons as members throughout the year. Mr D L Clifton resigned from the Committee on 4 February 2009.

The Nomination Committee was chaired by Mr R Lyons from 4 February 2009 and included Mr E Wisniewski and Mr A G Windham as members throughout the year. Mr D L Clifton resigned from the Committee on 4 February 2009 and was chairman up to that date.

The Committees' responsibilities include the consideration and approval of the terms of service, nomination, remuneration and benefits of the Company's Directors.

The Board, as a whole, determines the remuneration of the non-executive Directors (with Directors absenting themselves from discussions regarding their own remuneration as appropriate).

## **Internal control**

The Board, which presently comprises the Chairman, the Chief Executive Officer and non-executive Directors, meets formally on a regular basis. The Directors are responsible for ensuring that the Group maintains adequate internal control over the business and its assets. There is an agreed schedule of matters requiring referral to the Board. These matters include the Group's corporate strategy, acquisitions and disposals, approval of major capital expenditure, treasury policy and risk-management policies. Procedures have been formalised

where the Directors may need to take independent professional advice. The Audit Committee has reviewed the necessity for the establishment of an internal audit function, but considers that, due to the nature and size of the Group at present, it would not be appropriate for the Group to have its own internal-audit department.

On the wider aspects of internal control, relating to operational and compliance controls and risk management, as included in provision D.2.1 of the Code, the Board, in setting the control environment, identifies, reviews, and reports on the key areas of business risk facing the Group. These procedures have been in place throughout the current financial year.

There is close day-to-day involvement by the Directors in all of the Group's activities. This includes the comprehensive review of both management and technical reports, the monitoring of foreign exchange and interest-rate fluctuations, commitment to the Health, Safety and the Environment Management System, government and fiscal-policy issues, employment and information-technology requirements and cash-control procedures. Attendance at joint-venture meetings and site visits are made whenever appropriate. In this way, the key risk areas can be monitored effectively and specialist expertise applied in a timely and productive manner.

Any system of internal control can provide only reasonable, and not absolute, assurance that the risk of failure to achieve business objectives is eliminated. The Directors, having reviewed the effectiveness of the system of internal controls and risk management, consider that the system of internal control operated effectively throughout the financial year and up to the date the financial statements were signed.

#### **Performance evaluation**

A formal performance evaluation of the Board, its Committees and its Directors was not undertaken during the year due to the nature and size of the Group at present.

The Board is satisfied that the Board and its Committees are operating in an effective and constructive manner.

#### **Relations with shareholders**

The Group is active in communicating with both its institutional and private investors. The Annual General Meeting, at which Directors are introduced and available for questions, provide further opportunities for dialogue.

#### **Creditor-payment policy**

It is the policy of the Group to ensure that all of its suppliers of goods and services are paid promptly and in accordance with contractual and legal obligations. At 31 December 2009 there were 35 days (2008 - none) purchases remaining unpaid.

#### **Political contributions and charitable donations**

The Group made charitable donations during the year amounting to \$7,961 for Falklands Conservation (2008 - \$5,669).

#### **Auditors**

In accordance with the Companies Act 2006, a resolution is to be proposed at the Annual General Meeting for the re-appointment of UHY Hacker Young Manchester LLP as the Auditors of the Company.

### **Statement of disclosure to Auditors**

Each of the persons who is a Director at the date of approval of this annual report confirms that:

- A so far as the Director is aware, there is no relevant audit information of which the Company's Auditors are unaware, and
- B the Director has taken all steps that he ought to have taken as a Director in order to make himself aware of any relevant audit information and to establish that the Company's Auditors are aware of that information.

This report was approved by the Board on 19 April 2010 and signed on its behalf by:

**Mrs A R Neve BA** Secretary

## **Report of the Remuneration and Nomination Committees**

### **Remuneration Committee and Nomination Committee**

The Committees met as required during the year.

The Chairman and other Directors may also attend meetings but are not involved in any matter relating to themselves.

The Group considers that it has, to the extent appropriate given the Company's particular circumstances, applied the Combined Code throughout the year regarding remuneration committees. In formulating remuneration policy the Committees gives due consideration to the best practice provisions section of the Code.

### **Remuneration policy**

The remit of the Committees is to advise on all aspects of the remuneration packages of Directors.

The policy of the Committees is to ensure that the remuneration packages offered are competitive and designed to attract, retain and motivate Directors of a high calibre, with a significant proportion of the remuneration package linked to performance.

The Directors' emoluments are not pensionable.

Details of Directors' emoluments are set out in note 4 to the financial statements.

### **Directors' contracts**

The Directors' Service contracts are for an indefinite period but can be terminated with six-months' notice by either party.

Details of the Directors' contracts are summarized as follows:-

	<b>Effective date of service contract</b>
Mr S L Phipps	7 April 1998
Dr I G Duncan	14 March 2005
Mr A G Windham	1 May 2005
Mr E Wisniewski	13 June 2006
Mr R Lyons	14 January 2008
Mrs A R Neve	15 July 2008

## Directors' interests

The interests (all of which are beneficial) of the Directors in office at the end of the year in the ordinary shares of the Company are shown below, together with their share options under the Desire Petroleum PLC Unapproved Share Option Scheme and their share appreciation rights.

	10 March 2010 1p ordinary shares	31 December 2009 1p ordinary shares	1 January 2009 1p ordinary shares
Dr I G Duncan	485,169	413,946	332,834
Mr S L Phipps	36,702,633	33,722,633	33,422,633
Mr E Wisniewski	-	-	-
Mr A G Windham	8,155	7,100	7,100
Mr R Lyons	-	-	-
Mrs A R Neve	36,482,633	33,522,633	33,422,633

Mr S L Phipps' and Mrs A R Neve's interests in 33,532,633 (31 December 2009 and 2008 - 30,582,633) shares are through their shareholding in Phipps & Company Limited.

Mr S L Phipps and Mrs A R Neve have an interest (included above) in 2,840,000 (31 December 2009 and 2008 - 2,840,000) shares through their interest in the Phipps & Company Retirement Benefit Scheme.

At 31 December 2009, the interest of Dr I G Duncan includes 107,143 (2008 - 107,143) held by Chase Energy Limited of which he is a director and shareholder. His interest also includes 92,571 (2008 - 92,571) shares held by Hargreave Hale Nominees Limited.

## Share options

A share option reorganisation was carried out during the year as a result of the Placing in November 2009, under which 60,000,000 new ordinary shares were issued. The original options and exercise prices have been restated such that the potential percentage holding of options in the Company is the same as prior to the share issue.

The restatement has been approved by the Company's auditors.

	At 1 January 2009	Exercised in year	Lapsed in year	Reorgan- isation in year	At 31 December 2009	Exercise Price	Exercise period
Dr I G Duncan	478,239	(478,239)	-	-	-	20.11p	Up to 6 May 2009
	335,356	-	-	(355,356)	-	21.47p	Up to 7 May 2011
	-	-	-	422,949	422,949	31.73p	Up to 7 May 2011
	100,000	-	-	(100,000)	-	33.00p	Up to 1 June 2012
	-	-	-	126,119	126,119	40.66p	Up to 1 June 2012
	1,500,000	-	-	(1,500,000)	-	39.50p	Up to 21 July 2012
	-	-	-	1,891,789	1,891,789	45.82p	Up to 21 July 2012
Mr S L Phipps	478,239	(478,239)	-	-	-	20.11p	Up to 6 May 2009
	335,356	-	-	(355,356)	-	21.74p	Up to 7 May 2011
	-	-	-	422,949	422,949	31.73p	Up to 7 May 2011
	4,857,119	-	-	(4,857,119)	-	17.92p	Up to 23 June 2010
	-	-	-	6,125,763	6,125,763	28.71p	Up to 23 June 2010
	100,000	-	-	(100,000)	-	33.00p	Up to 1 June 2012
	-	-	126,119	126,119	40.66p	Up to 1 June 2012	
Mrs A R Neve	239,121	(239,121)	-	-	-	20.11p	Up to 6 May 2009
	134,356	-	-	(134,356)	-	21.74p	Up to 7 May 2011
	-	-	-	169,449	169,449	31.73p	Up to 7 May 2011
	4,857,119	-	-	(4,857,119)	-	17.92p	Up to 23 June 2010
	-	-	-	6,125,763	6,125,763	28.71p	Up to 23 June 2010
	50,000	-	-	(50,000)	-	33.00p	Up to 1 June 2012
	-	-	63,060	63,060	40.66p	Up to 1 June 2012	
Mr D L Clifton	100,000	-	(100,000)	-	-	33.00p	Up to 1 June 2012
Mr A G Windham	100,000	-	-	(100,000)	-	33.00p	Up to 1 June 2012
	-	-	-	126,119	126,119	40.66p	Up to 1 June 2012
Mr E Wisniewski	100,000	-	-	(100,000)	-	38.75p	Up to 13 June 2012
	-	-	-	126,119	126,119	45.22p	Up to 13 June 2012

Mr S L Phipps' and Mrs A R Neve's interests include share options granted over 6,125,763 (2008 - 4,857,119) shares which are beneficially held by Phipps & Company Limited in which they are interested as directors and shareholders.

The market price when the options were exercised was 30 pence resulting in an aggregate gain of \$173,630.

Following the open offer in January 2010, under which 28,971,544 shares were issued, a further option reorganisation was carried out. The options and exercise prices at 31 December 2009 have been restated such that the potential percentage holding of options in the Company is the same as prior to the share issue.

The restatement was approved by the Company's auditors.

	At 1 January 2010	Reorganisation January 2010	Exercised 2 February 2010	At 10 March 2010	Exercise Price	Exercise Period
Dr I G Duncan	422,949	(422,949)	-	-	31.73p	Up to 7 May 2011
	-	465,244	(465,244)	-	35.21p	Up to 7 May 2011
	126,119	(126,119)	-	-	40.66p	Up to 1 June 2012
	-	138,731	-	138,731	43.33p	Up to 1 June 2012
	1,891,789	(1,891,789)	-	-	45.82p	Up to 21 July 2012
	-	2,080,968	-	2,080,968	48.02p	Up to 21 July 2012
Mr S L Phipps	422,949	(422,949)	-	-	31.73p	Up to 7 May 2011
	-	465,244	-	465,244	35.21p	Up to 7 May 2011
	6,125,763	(6,125,763)	-	-	28.71p	Up to 23 June 2010
	-	6,738,339	(6,738,339)	-	32.46p	Up to 23 June 2010
	126,119	(126,119)	-	-	40.66p	Up to 1 June 2012
	-	138,731	-	138,731	43.33p	Up to 1 June 2012
Mrs A R Neve	169,449	(169,449)	-	-	31.73p	Up to 7 May 2011
	-	186,394	-	186,394	35.21p	Up to 7 May 2011
	6,125,763	(6,125,763)	-	-	28.71p	Up to 23 June 2010
	-	6,738,339	(6,738,339)	-	32.46p	Up to 23 June 2010
	63,060	(63,060)	-	-	40.66p	Up to 1 June 2012
	-	69,366	-	69,366	43.33p	Up to 1 June 2012
Mr A G Windham	126,119	(126,119)	-	-	40.66p	Up to 1 June 2012
	-	138,731	-	138,731	43.33p	Up to 1 June 2012
Mr E Wisniewski	126,119	(126,119)	-	-	45.22p	Up to 13 June 2012
	-	138,731	-	138,731	47.47p	Up to 13 June 2012

## Share Appreciation Rights ('SARS')

In 2005, the Company replaced its existing Unapproved Executive Share Option Scheme (under which it is currently intended that no further awards will be made to existing directors or senior staff) with a new incentive plan that would permit the grant of awards over up to 5% of the issued share capital of the Company. The Remuneration Committee, sought advice from external independent remuneration consultants as to its design and implementation, and in 2006 the Company adopted the new Desire Incentive Plan 2006 (the "Plan").

As has previously been the case with the operation of the Unapproved Share Option Scheme, the Plan will operate for the potential benefit of both executive and non-executive directors. The Committee is aware that, under normal circumstances, it would be unusual for non-executive directors to participate in share-based incentive arrangements. However, the Committee believes that offering participation in such arrangements to non-executive directors should be continued. This approach reflects the specific roles and responsibilities of the non-executive directors which are wider than is typically the case at other companies, an approach that keeps head office full-time staff levels and costs to a minimum. It also ensures that each member of the Board is fully aligned with both their colleagues' interests and with the interests of all other shareholders.

The awards under the Plan are structured as "Share Appreciation Rights" ("SARs"). SARs are designed to deliver a net gain equal to the increase in the price of a share between grant and exercise. The number of shares actually issued following exercise will therefore be less than the percentage of the current issued share capital to which the grant relates as referred to below.

On 26 January 2006, the Company granted SARs over shares representing 4% of the issued, ordinary-share capital of the Company.

On 26 February 2008, the Company granted SARs over shares representing 0.4% of the issued, ordinary-share capital of the Company.

SARs have been granted to the following Directors, as shown in the table below.

As described above, upon exercise of the SARs, the relevant Awardee will be issued with shares, or the cash equivalent, with a market value at the date of exercise equivalent to the notional gain that the Awardee would have made, being the amount by which the aggregate market value on exercise of the number of shares, in respect of which the SAR is exercised, exceeds the aggregate base price of that number of shares. The base price of a SAR will be the middle-market quotation of a share on the dealing day immediately preceding the date of grant.

SARs can be satisfied by either the issue of new shares, the transfer of existing shares or the cash equivalent.

No further awards of SARs will be made to the listed Awardees.  
No consideration is payable on the grant of a SAR.

The market price of the shares on 31 December 2009 was 92.00p and the range during the year was 25.25p to 106.25p

Other than shown in this report, no Director had any interest in the shares of the Company or any of its subsidiaries at 31 December 2009.

<b>Name</b>	<b>Position</b>	<b>SARs (percentage at time of award of issued- share capital)</b>	<b>Base Price</b>	<b>Date of Award</b>	<b>Exercise period</b>
Mr S L Phipps	Chairman	0.4	33.75p	26 January 2006	Up to 23 January 2016
Dr I G Duncan	Chief Executive Officer	1.1	33.75p	26 January 2006	Up to 23 January 2016
Mr A G Windham	Non-Executive Director	0.4	33.75p	26 January 2006	Up to 23 January 2016
Mr D L Clifton	Non-Executive Director	0.4	33.75p	26 January 2006	Up to 23 January 2016
Mr E Wisniewski	Non-Executive Director	0.4	33.75p	26 January 2006	Up to 23 January 2016
Mrs A R Neve	Non-Executive Director	0.2	33.75p	26 January 2006	Up to 23 January 2016
Mr R Lyons	Non-Executive Director	0.4	46.50p	26 February 2008	26 February 2011 to 26 February 2018

The SARs of Mr D L Clifton lapsed on 4 February 2009.

Following the Open Offer in January 2010 a SARs rebasing was carried out. The SARs percentages and base prices have been rebased to maintain the inherent value of the awards as if the Open Offer had not occurred.

The restatement has been approved by the Company's auditors.

<b>Awardee</b>	<b>SARs at 1 January 2010 (percentage of issued- share capital at time of award)</b>	<b>Reorganisation January 2010</b>	<b>At 10 March 2010 (percentage of issued- share capital at 11 January 2010)</b>	<b>Base Price</b>	<b>Exercise Period</b>
Mr S L Phipps	0.40%	(0.40%) <b>0.28%</b>	<b>0.28%</b>	33.75p <b>33.07p</b>	Up to 23 January 2016 <b>Up to 23 January 2016</b>
Dr I G Duncan	1.10%	(1.10%) <b>0.78%</b>	<b>0.78%</b>	33.75p <b>33.07p</b>	Up to 23 January 2016 <b>Up to 23 January 2016</b>
Mr A G Windham	0.40%	(0.40%) <b>0.28%</b>	<b>0.28%</b>	33.75p <b>33.07p</b>	Up to 23 January 2016 <b>Up to 23 January 2016</b>
Mr E Wisniewski	0.40%	(0.40%) <b>0.28%</b>	<b>0.28%</b>	33.75p <b>33.07p</b>	Up to 23 January 2016 <b>Up to 23 January 2016</b>
Mrs A R Neve	0.20%	(0.20%) <b>0.14%</b>	<b>0.14%</b>	33.75p <b>33.07p</b>	Up to 23 January 2016 <b>Up to 23 January 2016</b>
Mr R Lyons	0.40%	(0.40%) <b>0.29%</b>	<b>0.29%</b>	46.50p <b>45.57p</b>	26 February 2011 to 26 February 2018 <b>26 February 2011 to 26 February 2018</b>

## **Approval**

This Report was approved by the Board on 19 April 2010:

Mr A G Windham            Chairman of the Remuneration Committee

Mr R Lyons                Chairman of the Nomination Committee

## **Statement of Directors' Responsibilities in respect of the Accounts**

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

Company law requires the directors to prepare such financial statements for each financial year. Under the law the directors are required to prepare group financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union and Article 4 of the IAS Regulation and have also chosen to prepare the parent company financial statements under IFRSs as adopted by the European Union. Under company law the directors must not approve the accounts 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 period. In preparing these financial statements, the directors are required to:

- properly select and apply accounting policies;
- present information, including accounting policies, in a manner that provide relevant, reliable, comparable and understandable information; and

- provide additional disclosures when compliance with the specific requirements in IFRSs are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance; and
- Make an assessment of the company's ability to continue as a going concern.

The directors are responsible for keeping proper 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.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

### **Directors' responsibility statement**

We confirm to the best of our knowledge:

- The financial statements, prepared in accordance with International Financial Reporting Standards as adopted by the European Union, give a true and fair view of the assets, liabilities, financial position and profit or loss of the company and the undertakings included in the consolidation taken as a whole; and
- the management report, which is incorporated into the directors' report, include a fair review of the development and performance of the business and the position of the company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

By order of the Board

**S L Phipps** Chairman

## **Independent Report of the Auditors**

**Registered Auditor**  
**UHY Hacker Young Manchester LLP**  
St. James Building  
79 Oxford Street  
Manchester M1 6HT

19 April 2010

### **To the shareholders of Desire Petroleum PLC**

We have audited the Group and Parent Company financial statements of Desire Petroleum PLC for the year ended 31 December 2009 which comprise the Income Statement, the Statements of Comprehensive Income, the Balance Sheets, the cash flow statements, the statements of changes in equity and the related notes 1 to 24. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards ("IFRSs") as adopted by the European Union.

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an 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**

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

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

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

### **Opinion on financial statements**

#### **In our opinion:**

- The financial statements give a true and fair view of the state of the Group's and Parent Company's affairs as at 31 December 2009 and of the Group's loss for the year then ended;
- The financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- The financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

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

**In our opinion:**

- The part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006; and
- The information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

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

We have nothing to report in respect of the following:

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

- Adequate accounting records have not been kept by the Parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- The Parent Company financial and the part of the Directors' Remuneration Report to be audited are not in agreement with the account records and returns; or
- Certain disclosures of directors' remuneration specified by law are not made; or
- We have not received all the information and explanations we require for our audit.

**Clive S Maudsley** (Senior Statutory Auditor)

For and on behalf of  
**UHY Hacker Young Manchester LLP**  
**Chartered Accountants and Statutory Auditors**  
Manchester

## Consolidated Income Statement

For the year ended 31 December 2009	Note	2008 \$000	2009 \$000
Administrative expenses	3	(1,461)	(1,103)
Share-based payment expense		(498)	(82)
Foreign exchange loss		(937)	(2,731)
<b>Operating Loss</b>		<b>(2,896)</b>	<b>(3,916)</b>
Finance expenses		(13)	-
Investment revenues	6	1,135	148
<b>Loss before tax</b>		<b>(1,774)</b>	<b>(3,768)</b>
Tax	7	302	-
<b>Loss for the financial year</b>	19	<b>(1,472)</b>	<b>(3,768)</b>
<b>Earnings per share</b>			
Loss per share (cents): Basic	8	(0.61)	(1.59)
Loss per share (cents): Diluted	8	n/a	n/a

Movements on reserves are shown in note 19 to these Accounts.

There is no difference between the results as disclosed above and the results on an historical cost basis.

All operating income and operating gains and losses relate to continuing activities.

## Consolidated Statement of Comprehensive Income

For the year ended 31 December 2009	2008 \$000	2009 \$000
<b>Loss for the financial year</b>	<b>(1,472)</b>	<b>(3,768)</b>
Other comprehensive income for the year	-	-
<b>Total comprehensive income for the year</b>	<b>(1,472)</b>	<b>(3,768)</b>

## Balance Sheets

At 31 December 2009	Note	The Group		The Company	
		31.12.08 \$000	31.12.09 \$000	31.12.08 \$000	31.12.09 \$000
<b>Non-current assets</b>					
Intangible assets	10	16,668	<b>26,052</b>	16,668	<b>26,052</b>
Property, plant & equipment	11	4,561	<b>4,557</b>	4,561	<b>4,557</b>
		21,229	<b>30,609</b>	21,229	<b>30,609</b>
<b>Current assets</b>					
Trade and other receivables	13	386	<b>349</b>	386	<b>349</b>
Restricted cash	14	-	<b>24,748</b>	-	<b>24,748</b>
Cash and cash equivalents	15	40,690	<b>87,574</b>	40,690	<b>87,574</b>
		41,076	<b>112,671</b>	41,076	<b>112,671</b>
<b>Total assets</b>		62,305	<b>143,280</b>	62,305	<b>143,280</b>
<b>Current liabilities</b>					
Trade and other payables	16	(444)	<b>(18,240)</b>	(444)	<b>(18,240)</b>
Bank overdrafts		(59)	<b>(6)</b>	(59)	<b>(6)</b>
<b>Total liabilities</b>		(503)	<b>(18,246)</b>	(503)	<b>(18,246)</b>
<b>Net assets</b>		61,802	<b>125,034</b>	61,802	<b>125,034</b>
<b>Equity</b>					
<b>Share capital</b>	18	4,549	<b>5,569</b>	4,549	<b>5,569</b>
<b>Share premium account</b>	19	93,337	<b>159,235</b>	93,337	<b>159,235</b>
<b>Retained earnings</b>	19	(36,084)	<b>(39,770)</b>	(36,084)	<b>(39,770)</b>
<b>Total equity</b>		61,802	<b>125,034</b>	61,802	<b>125,034</b>

These Accounts were approved by the Board of Directors and authorised for issue on 20 April 2010.

**Company Registration No:** 3168611

They were signed on its behalf by:

**S L Phipps**  
Chairman

## Statement of Changes in Equity

	Equity attributable to equity holders of the Company			
	Share Capital \$000	Share premium \$000	Retained earnings \$000	Total equity \$000
<b>Balance as at 1 January 2008</b>	<b>4,521</b>	<b>92,775</b>	<b>(35,110)</b>	<b>62,186</b>
Loss for the period	-	-	(1,472)	(1,472)
Issue of share capital	28	562	-	590
Credit to equity for share-based payments	-	-	498	498
<b>Balance as at 31 December 2008</b>	<b>4,549</b>	<b>93,337</b>	<b>(36,084)</b>	<b>61,802</b>
<b>Balance as at 1 January 2009</b>	<b>4,549</b>	<b>93,337</b>	<b>(36,084)</b>	<b>61,802</b>
Loss for the period	-	-	(3,768)	(3,768)
Issue of share capital	1,020	65,898	-	66,918
Credit to equity for share-based payments	-	-	82	82
<b>Balance as at 31 December 2009</b>	<b>5,569</b>	<b>159,235</b>	<b>(39,770)</b>	<b>125,034</b>

## Consolidated and Company Cash Flow Statement

For the year ended 31 December 2009	Note	2008 \$000	2009 \$000
<b>Net cash from operating activities</b>	21	(2,078)	<b>8,928</b>
<b>Investing activities</b>			
Interest received		1,135	<b>148</b>
Purchase of tangible and intangible assets		(1,040)	<b>(1,549)</b>
Cash places in escrow		-	<b>(24,748)</b>
<b>Net cash from/(invested in) investing activities</b>		95	<b>(26,149)</b>
<b>Financing activities</b>			
Proceeds on issue of shares (net of costs)		590	<b>66,917</b>
<b>Net cash from financing activities</b>		590	<b>66,917</b>
<b>Net increase/(decrease) in cash and cash equivalents</b>		(1,393)	<b>49,696</b>
Cash and cash equivalents at the beginning of the year		43,042	<b>40,631</b>
Effect of foreign-exchange rate changes		(1,018)	<b>(2,759)</b>
<b>Cash and cash equivalents at the end of the year</b>	22	40,631	<b>87,568</b>

## Notes to the Financial Statements

### 1 Accounting policies

The Accounts are based on the following policies which have been consistently applied:

#### Basis of preparation

The results for the year ended 31 December 2009 have been prepared in accordance with IFRS as adopted by the EU and the International Accounting Standards Board.

The Group has continued to apply the full cost accounting policy, explained further in the Goodwill and intangible asset accounting policy note, as permitted by IFRS 6 'Exploration for and Evaluation of Mineral Resources'.

#### Accounting estimates

The Group's accounting policies make use of accounting estimates and judgments in the following areas; impairment, depreciation and share based payments. These are described in more detail in the relevant accounting policy.

#### Basis of consolidation

The Group accounts consolidate the accounts of the Parent Company and all its subsidiary undertakings, all of which were made up to 31 December 2009.

#### Goodwill and intangible assets

##### a. Goodwill

When the fair value of the consideration for an acquired undertaking exceeds the fair value of its separable net assets, the difference is treated as purchased goodwill and is capitalised. When the fair value of the consideration for an acquired undertaking is less than the fair value of its separable net assets, the difference is taken directly to the income statement. Goodwill is not amortised but is reviewed at least annually for impairment.

##### b. Acquired intangibles

Intangible assets, which are capable of being recognised separately and measured reliably on acquisition, are capitalised at fair value on acquisition. Where these assets have a finite life, they are amortised over the period that they are expected to generate benefits, but generally not exceeding ten years.

##### c. Research and development

Research expenditure is recognised as an expense as incurred. Costs incurred on development projects are recognised as intangible assets when it is probable that the project will be a technological and commercial success. Other development expenditure is recognised as an expense as incurred.

##### d. Computer software

Computer software costs are amortised over their expected useful lives, as follows:

<b>Computer software</b>	20% straight line basis
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##### e. Oil and gas expenditure

The Group applies the full-cost method of accounting, in accordance with IFRS 6 'Exploration for and Evaluation of Mineral Resources' (IFRS 6), under which expenditure relating to the acquisition, exploration, and evaluation of oil and gas interests, including an appropriate share of directly attributable overheads and relevant financing cost, is capitalised. If no discoveries are made, the accumulated capitalised costs will be written off through the income statement. Where the facts and circumstances indicate that exploration and evaluation costs exceed their recoverable amount, the intangible costs are tested for impairment. The cost of plant acquired to carry out exploration activities is treated as a tangible asset. The depreciation of such plant is capitalised as intangible assets.

## Notes to the Financial Statements (continued)

### f. Consortia and farm out agreements

In addition to holding licences on its own account, the Group is a member of consortia (a joint arrangement). The Group's proportionate share of the consortia costs are included in intangible assets or PPE, as appropriate. During the year, the Group continued with farm out agreements with third parties in respect of certain licences. The Group's proportionate share of the costs is included in intangible assets and PPE as appropriate.

Where the Group acts as operator to a joint arrangement and has a direct legal liability to third party creditors or a similar entitlement in respect of debtors then the gross liabilities and receivables (including amounts due to or from non-operating partners) are included in the Group balance sheet.

Where the Group acts as a non-operating participant to a joint arrangement, the entitlement or liability in respect of its share of the working capital balances relating to the joint arrangement is analysed across the underlying elements of working capital such as stocks, debtors, cash and creditors.

### g. Decommissioning costs

Provision for the future cost of decommissioning an installation is recognised as part of the total investment to gain access to future economic benefit. The asset is established and included as part of the overall cost pool. Provision is made when the Group has an obligation to dismantle and remove a facility or an item of plant and to restore the site on which it is located, and when a reasonable estimate of that liability can be made.

The decommissioning asset is recognised and capitalised as the related facilities are installed, simultaneously with the recognition of the provision. The incremental amount capitalised on each phase of installation should equal the incremental amount provided in respect of each phase.

## Property, plant and equipment (PPE)

### a. Oil and gas interests

The Group applies the full-cost method of accounting, in accordance with IFRS 6 'Exploration for and Evaluation of Mineral Resources' (IFRS 6), and the Statement of Recommended Practice' Accounting for Oil and Gas Exploration, Development, Production and Decommissioning Activities', under which expenditure relating to the development of oil and gas interests, including an appropriate share of directly attributable overheads and relevant financing cost, is capitalised in cost pools on the basis of income generating units. Capitalised costs are amortised on a unit of production basis, over proven and probable reserves, taking account of estimates of future costs of development relating to those reserves. Depreciation of plant acquired to carry out exploration activities is capitalised as intangible assets.

### b. Other

Property plant and equipment are stated at cost or valuation less depreciation. Depreciation is provided at rates calculated to write off the cost or valuation, less estimated residual value of each asset, over its expected useful life, as follows:

<b>Equipment and fixtures</b>	20% straight line basis
-------------------------------	-------------------------

### Investments

Investments in subsidiary undertakings are shown at cost less provisions for estimated impairments in value.

### Foreign currencies

#### a. Functional and presentation currency

Items included in the financial statements of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The functional and presentational currency is US Dollars, and the 2009 Annual Report is presented in US Dollars as this better reflects the primary economic environment in which the Group operates.

## Notes to the Financial Statements (continued)

### b. Transactions and balances

Transactions denominated in foreign currencies are translated into the functional currency at the exchange rate prevailing at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency at the exchange rates ruling at the year-end. Foreign exchange gains and losses resulting from the settlement of such transactions, and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement, except when deferred in equity as qualifying cash flow hedges and qualifying investment hedges. Exchange differences arising from the translation of the balance sheets and income statements of foreign operations into US\$ are recognised as a separate component of equity on consolidation. When a foreign operation is sold, such exchange differences are recognised in the income statement as part of the gain or loss on sale.

### Taxation

#### a. Current income tax

Current tax, including UK corporation tax, is provided on amounts expected to be paid or recovered using the tax rates and laws that have been enacted or substantially enacted by the balance sheet date.

#### b. Deferred income tax

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income tax is determined using tax rates and laws that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled. Deferred income tax assets are recognised to the extent that it is probable that future taxable profits will be available against which the temporary differences can be utilised. Deferred income tax is provided on temporary differences arising on investments in subsidiaries, except where the timing of the reversal of the temporary differences are controlled by the Group, and it is probable that the temporary differences will not reverse in the foreseeable future.

### Cash and cash equivalents

Cash and cash equivalents includes cash in hand, deposits held at call with banks and bank overdrafts. Bank overdrafts are shown within current liabilities on the balance sheet.

### Restricted cash

Where cash is deposited with financial institutions, securing various guarantees and performance bonds associated with the Group's operating activities, it is treated as a financial asset of the Group and released on maturity of the guarantee or performance bond.

Where cash balances are not under the exclusive control of the Company, such amounts are disclosed as restricted cash.

### Share based payments

The Group operates equity-settled, share-based compensation plans. The economic cost of awarding shares and share options is recognised as an expense in the income statement equivalent to the fair value of the benefit awarded. The fair value is determined by reference to option pricing models. The charge is recognised in the income statement over the vesting period of the award.

### Financial instruments

The Group uses certain financial instruments in its operating and investing activities that are appropriate to its strategy and circumstances.

Financial instruments currently comprise cash and short-term debtors and creditors. The Group regularly reviews the funding opportunities available to it in order to finance its operations, including considering the use of borrowings, as well as equity, to fund short-term cash requirements.

## **Notes to the Financial Statements (continued)**

The main risks arising from the Group's present use of financial instruments are currently risk relating to the Group's non-US\$ cash resources. The addition of any borrowings to the Group's portfolio of financial instruments will introduce interest rate risk.

### **Operating segments**

The Group considers itself to have a single purpose, the exploration and exploitation of its licences in the North Falkland Basin, and therefore concludes that it has only one business segment and only one geographic segment.

### **Adoption of new and revised Standards**

In the current year, the following significant new and revised Standards and Interpretations have been adopted and have affected the amounts reported in these financial statements.

### **Standards affecting presentation and disclosure**

#### **IAS1 (revised 2007) Presentation of Financial Statements**

IAS1(2007) introduced format and content changes to the financial statements. In particular it has required the presentation of a Consolidated statement of changes in equity as a primary statement.

#### **Standards affecting the reported results and financial position**

There were no standards adopted in the year which affected the reported results and financial position of the Group.

#### **Standards not affecting the reported results nor the financial position**

In the current year, the following significant new and revised Standards and Interpretations were effective but did not affect the amounts reported in these financial statements but may affect future periods:

IFRS 2 Share based payment

(Amendment relating to vesting conditions and cancellations)

IFRS 7 Financial Instruments: Disclosures

(Amendment enhancing disclosure about fair value and liquidity risk)

IFRS 8 Operating Segments

(New standard)

IAS 23 Borrowing Costs

(Revision to prohibit immediate expensing)

IAS 32 Financial Instruments: Presentation

(Amendments relating to puttable instruments and obligations arising on liquidation)

IFRIC 16 Hedges of a Net Investment in a Foreign Currency

IFRIC 18 Transfers of Assets from Customers

## **Notes to the Financial Statements (continued)**

### **Amendments resulting from May 2008 Annual Improvements to IFRSs:**

IAS 1 Presentation of Financial Statements  
IAS 16 Property Plant and Equipment  
IAS 19 Employees Benefits  
IAS 20 Government Grants and Disclosure of Government Assistance  
IAS 27 Consolidated and Separate Financial Statements  
IAS 28 Investments in Associates  
IAS 29 Financial Reporting in Hyperinflationary Economies  
IAS 31 Interest in Joint Ventures  
IAS 36 Impairment of Assets  
IAS 38 Intangible Assets  
IAS 39 Financial Instruments: Recognition and Measurement  
IAS 40 Investment Property

At the date of authorisation of these financial statements, the following Standards and Interpretations which have not been applied in these financial statements were in issue but not yet effective. The directors do not expect the adoption of these in future periods will have material impact on the financial statements of the Group.

IFRS 1 (amended)/IAS 27 amended  
Cost of investment in a subsidiary, Jointly Controlled entity or Associate

IFRS 2 (June 2009)  
Share based payments

IFRS 3 (revised 2008)  
Business Combinations

IFRS 5 (revised 2008)  
Non current Assets Held for Sale and Discounted Operations

IFRS 8 (April 2009)  
Operating Segments

IAS 27 (revised 2008)  
Consolidated and Separate Financial Statements

IAS 28 (revised 2008)  
Investments in Associates

IAS 32 (2009)  
Financial Instruments : Presentation

IAS 34 (November 2009)  
Related Party Disclosures

IFRIC 17  
Distributions of Non cash Assets to Owners

### **Annual Improvements to IFRSs (April 2009)**

## Notes to the Financial Statements (continued)

### 2 Production costs incurred

Pre-production costs incurred, or provided in, Oil and Gas Exploration Activities were as follows:

	Falkland Islands	
	2008	2009
	\$000	\$000
<b>Acquisition of unproved properties</b>		
Operating Lease – Licence costs	238	200
Exploration and appraisal costs	1,204	9,185
Total costs capitalised	1,442	9,385

### 3 Operating expenses

	2008	2009
	\$000	\$000
<b>Administrative and other expenses</b>		
Auditors' remuneration - audit fees	37	32
- other services		
a) taxation	3	14
b) Consultancy and review of Interim Accounts	6	10
Directors' fees	410	315
Wages and salaries	48	33
Legal and professional fees	381	337
Management fees	625	480
Miscellaneous expenses	94	72
Travel and entertaining	68	49
Depreciation	6	5
Operating leases – land and buildings	22	18
Recharge of administrative expenses	(239)	(262)
	1,461	1,103

In addition to the Auditors' remuneration stated above, the Auditors received \$59,971 (2008 - \$nil) in respect of other review costs, the cost of which is included in share premium account.

## Notes to the Financial Statements (continued)

### 4 Directors

	2008 Fees \$000	2009 Fees \$000
The emoluments of the Directors were as follows:		
Dr C B Phipps	12	-
Mr S L Phipps	28	23
Dr I G Duncan	245	200
Mr D L Clifton	28	-
Mr A G Windham	28	23
Mr E Wisniewski	28	23
Mr R Lyons	28	23
Mrs A R Neve	13	23
	410	315

Further information on the remuneration of Directors and their share awards can be found in the Remuneration and Nomination Committee's report.

Information on related-party transactions is disclosed in note 23 to these Accounts.

### 5 Employment costs

	2008 \$000	2009 \$000
Wages and salaries (excluding Directors fees)	13	8
Social security costs	35	25
	48	33
The average monthly number of employees, including Directors, during the year was as follows:		
	2008 Number	2009 Number
Directors	7	6
Administrators	1	1
	8	7

### 6 Investment revenues

	2008 \$000	2009 \$000
Interest on bank deposits	1,135	148

## Notes to the Financial Statements (continued)

### 7 Taxation

<b>a) Analysis of charge in the period</b>	2008 \$000	2009 \$000
Current tax:		
Current tax in the period	-	-
In respect of previous years	(302)	-
	(302)	-
<b>b) Reconciliation of the total tax charge</b>	2008 \$000	2009 \$000
The tax assessed for the period is different from the standard rate of corporation tax in the UK of 28% (2008-28%)	(1,774)	<b>(3,768)</b>
Accounting loss before tax		
Tax at the standard rate of corporation tax in the UK of 28% (2008-28%)	(497)	<b>(1,055)</b>
Effects of:		
Adjustments in respect of prior years	(302)	-
Share-based payments	139	<b>23</b>
Expenses carried forward	358	<b>1,032</b>
	(302)	-

### c) Factors that may affect future tax charges

The Company is carrying forward an amount of tax-deductible expenditure under the assumption that it will have an income from oil exploration in the future.

The amount currently available for offset against future revenue is estimated at \$57million.

No deferred tax asset is provided on this expenditure as it is not reasonably certain that the income from this source will materialise.

### 8 Earnings per share

The calculation of basic earnings per ordinary share is based on a loss of \$3,768,000 (2008: loss \$1,472,000) and on 237,103,714 (2008: 228,021,821) ordinary shares, being the weighted-average number of ordinary shares in issue during the year.

As the Group reports a loss for the current and comparative year, then in accordance with IAS 33, the share options and Share Appreciation Rights in issue are not considered dilutive. Details of such instruments that could potentially dilute basic-earnings per share in the future are included in note 18.

### 9 Profit for the financial year

Desire Petroleum PLC has not presented its own income statement, as permitted by section 408 of the Companies Act 2006. The loss for the financial year dealt with in the accounts of the Holding Company amounts to \$3,768,000 (2008: loss \$1,508,000).

## Notes to the Financial Statements (continued)

### 10 Intangible fixed assets

The Group	Goodwill \$000	Oil and gas interests \$000	Computer software \$000	Total \$000
<b>Cost</b>				
At 1 January 2009	1,873	16,666	6	18,545
Additions	-	9,385	-	9,385
<b>At 31 December 2009</b>	<b>1,873</b>	<b>26,051</b>	<b>6</b>	<b>27,930</b>
<b>Amortisation/impairment</b>				
At 1 January 2009	1,873	-	4	1,877
Charge for the year	-	-	1	1
<b>At 31 December 2009</b>	<b>1,873</b>	<b>-</b>	<b>5</b>	<b>1,878</b>
<b>Net Book Value at 31 December 2009</b>	<b>-</b>	<b>26,051</b>	<b>1</b>	<b>26,052</b>
Net Book Value at 31 December 2008	-	16,666	2	16,668

The Group's oil and gas interests all relate to the Falkland Islands.

The Company	Oil and gas interests \$000	Computer software \$000	Total \$000
<b>Cost</b>			
At 1 January 2009	16,666	6	16,672
Additions	9,385	-	9,385
<b>At 31 December 2009</b>	<b>26,051</b>	<b>6</b>	<b>26,057</b>
<b>Amortisation/impairment</b>			
At 1 January 2009	-	4	4
Charge for the year	-	1	1
<b>At 31 December 2009</b>	<b>-</b>	<b>5</b>	<b>5</b>
<b>Net Book Value at 31 December 2009</b>	<b>26,051</b>	<b>1</b>	<b>26,052</b>
Net Book Value at 31 December 2008	16,666	2	16,668

The Company's oil and gas interests all relate to the Falkland Islands.

## Notes to the Financial Statements (continued)

### 11 Property, plant and equipment

The Group and Company	Long lead items \$000	Equipment and fixtures \$000	Total \$000
<b>Cost</b>			
At 1 January 2009	4,552	27	4,579
Additions	-	-	-
<b>At 31 December 2009</b>	<b>4,552</b>	<b>27</b>	<b>4,579</b>
<b>Depreciation</b>			
At 1 January 2009	-	18	18
Charges for the year	-	4	4
<b>At 31 December 2009</b>	<b>-</b>	<b>22</b>	<b>22</b>
<b>Net Book Value at 31 December 2009</b>	<b>4,552</b>	<b>5</b>	<b>4,557</b>
Net Book Value at 31 December 2008	4,552	9	4,561

### 12 Investments

The Company	2009 \$000
Cost at 1 January 2009 and at 31 December 2009	2,166
Provision at 1 January 2009 and at 31 December 2009	(2,166)
<b>At 1 January 2009 and at 31 December 2009</b>	<b>-</b>

Particulars of the principal subsidiary undertakings at 31 December 2009 were as follows:

Name of subsidiary	Holding	Proportion of voting rights and shares held	Country of Incorporation	Nature of business
Gaelic Resources plc	Ordinary shares	100%	Republic of Ireland	Holding Company
Interoil Limited	Ordinary shares*	99.80%	England	Non-trading
Anglo Scandinavian Petroleum plc	Ordinary shares*	100%	England	Non-trading

\*Held in the name of Gaelic Resources

### 13 Trade and other receivables

	The Group		The Company	
	2008 \$000	2009 \$000	2008 \$000	2009 \$000
Other receivables	368	335	368	335
Prepayments and accrued income	18	14	18	14
	386	349	386	349

## Notes to the Financial Statements (continued)

### 14 Restricted cash

	The Group		The Company	
	2008 \$000	2009 \$000	2008 \$000	2009 \$000
Restricted cash	-	24,748	-	24,748
	-	24,748	-	24,748

On 2 October 2009 the Group signed a rig contract for a minimum 80-day drilling campaign. Pursuant to this contract, the Group has \$25million held in an escrow account at the year end. The amount is treated as restricted cash as the balance is not under the exclusive control of the Group.

### 15 Cash and cash equivalents

	The Group		The Company	
	2008 \$000	2009 \$000	2008 \$000	2009 \$000
Cash at bank and short term deposits	40,690	87,574	40,690	87,574
	40,690	87,574	40,690	87,574

### 16 Trade and other payables

	The Group		The Company	
	2008 \$000	2009 \$000	2008 \$000	2009 \$000
Payments received in advance	-	10,160	-	10,160
Other tax and social-security creditors	8	10	8	10
Other creditors	112	794	112	794
Accruals	324	7,276	324	7,276
	444	18,240	444	18,240

### 17 Financial Instruments

The Group's policies as regards to financial instruments are set out in the accounting policies. The Company does not trade in financial instruments. The risks and uncertainties facing the Group include, but are not limited to:

#### Currency rate risk

The Group currency risk is primarily attributable to GBP cash deposits held at the bank. These deposits are held in GBP as the Group incurs some expenditure in this currency. Foreign exchange movements on monetary assets and liabilities are taken to the income statement and potential exposure is set out in the table below.

## Notes to the Financial Statements (continued)

### Credit risk and counter-party risk

The Group's principal financial assets are cash at bank and other receivables. The Company's credit risk is primarily attributable to amounts included in other receivables. The maximum credit-risk exposure relating to financial assets is represented by the carrying values as at the Balance Sheet date.

<b>At 31 December 2009</b>	<b>US\$ (\$000)</b>	<b>GB£ (\$000)</b>	<b>FI£ (\$000)</b>	<b>Total \$000</b>
Non-monetary assets	30,623	-	-	<b>30,623</b>
Cash and short term deposits	22,297	65,234	43	<b>87,574</b>
Other monetary assets	24,748	335	-	<b>25,083</b>
Monetary liabilities	(10,160)	(8,086)	-	<b>(18,246)</b>
	67,508	57,483	43	<b>125,034</b>
<b>At 31 December 2008</b>	<b>US\$ (\$000)</b>	<b>GB£ (\$000)</b>	<b>FI£ (\$000)</b>	<b>Total \$000</b>
Non-monetary assets	21,247	-	-	<b>21,247</b>
Cash and short term deposits	38,565	2,088	37	<b>40,690</b>
Other monetary assets	-	368	-	<b>368</b>
Monetary liabilities	-	(503)	-	<b>(503)</b>
	59,812	1,953	37	<b>61,802</b>

### Liquidity risk

The Group manages liquidity risk via maintaining adequate cash reserves, and by continuously monitoring forecast and actual cash flows relating to oil exploration and administrative costs.

### Interest rate risk

The Group is exposed to the risk that investment income may be reduced by interest rate cuts in the UK and USA. The Group keeps the majority of its cash deposits in short term fixed rate accounts. At 31 December 2009, short term deposits were earning interest at a weighted average fixed deposit rate of 0.27%. Cash at bank earns interest at floating rates based on US\$/GBP LIBOR

The floating rate liabilities comprise bank borrowings which bear interest based on GBP LIBOR.

<b>Interest rate risk profile</b>	<b>2008 \$000</b>	<b>2009 \$000</b>
Short term fixed rate financial assets	39,928	63,871
Floating rate financial assets	762	23,703
Floating rate financial liabilities	(59)	(6)
Short term restricted floating rate financial asset	-	24,748

### Capital risk management

The Group manages its capital to ensure that the Group will be able to continue as a going concern while maximising the return to shareholders through the use of equity. The overall strategy remains unchanged from 2008.

The capital structure consists of cash and cash equivalents and equity. The Group is not subject to any externally imposed capital requirements.

## Notes to the Financial Statements (continued)

### 18 Share capital

The Group and Company	2008 Number of shares	2008 £000	2009 Number of shares	2009 £000
<b>Authorised</b>				
Ordinary shares of £0.01 Pounds Sterling each	400,000,000	4,000	<b>400,000,000</b>	<b>4,000</b>
			Ordinary £0.01 shares Number	
<b>Allotted, called-up and fully-paid</b>				
<b>At 1 January 2009</b>			228,519,846	
Issued in year			61,195,599	
<b>At 31 December 2009</b>			<b>289,715,445</b>	
			Ordinary £0.01 shares \$000	
<b>At 1 January 2009</b>			4,549	
Issued in year			1,020	
<b>At 31 December 2009</b>			<b>5,569</b>	

The Company has one class of ordinary shares which carry no rights to fixed income.

### Share options

On 27 April 2009, options were exercised over 1,195,600 shares raising \$375,480.

The share options in issue at 31 December 2009 were as follows:

Date of grants	At 1 January 2009	Exercised in year	Lapsed in year	Reorganisation in year	At 31 December 2009	Exercise price	Exercise period
7 May 2002	1,195,600	(1,195,600)	-	-	-	20.11p	up to 6 May 2009
26 June 2003	4,857,119	-	-	(4,857,119)	-	17.92p	up to 23 June 2010
26 June 2003	-	-	-	6,125,763	6,125,763	28.71p	up to 23 June 2010
27 May 2004	1,475,780	-	-	(1,475,780)	-	21.74p	up to 7 May 2011
27 May 2004	-	-	-	1,861,243	1,861,243	31.73p	up to 7 May 2011
1 June 2005	450,000	-	(100,000)	(350,000)	-	33.00p	up to 1 June 2012
1 June 2005	-	-	-	441,417	441,417	40.66p	up to 1 June 2012
13 June 2005	100,000	-	-	(100,000)	-	38.75p	up to 13 June 2012
13 June 2005	-	-	-	126,119	126,119	45.22p	up to 13 June 2012
21 July 2005	1,500,000	-	-	(1,500,000)	-	39.50p	up to 21 July 2012
21 July 2005	-	-	-	1,891,789	1,891,789	45.82p	up to 21 July 2012
1 January 2006	25,000	-	-	(25,000)	-	33.00p	up to 1 January 2013
1 January 2006	-	-	-	31,530	31,530	40.66p	up to 1 January 2013
15 August 2008	100,000	-	-	(100,000)	-	79.75p	15 August 2011 to 15 August 2015
15 August 2008	-	-	-	126,119	126,119	77.73p	15 August 2011 to 15 August 2015

## Notes to the Financial Statements (continued)

There were no share options or SARs awarded during the year. There have been no awards since the year end. The share options reorganisation during the year was carried out as a result of the Placing in November 2009 under which 60,000,000 shares were issued. The original options and exercise price have been restated such that the potential percentage holding of options in the Company is the same as prior to the share issue.

The restatement has been approved by the Company's auditors.

### Share Appreciation Rights ("SARs")

Further details relating to SARs can be found within the Report of the Remuneration and Nomination Committees report. In addition to the SARs in the report, there were SARs over 0.78% of the issued share capital at 11 January 2010 at a base price of 33.07p, held by the spouse of a former Director.

Following the Open Offer in January 2010, under which 28,971,544 shares were issued, a further share option reorganisation was carried out. The options and exercise prices at 31 December 2009 have been restated so that the potential percentage holding of options in the Company is the same as prior to the share issue.

The restatement has been approved by the Company's auditors.

Date of grants	At 1 January 2010	Reorganisation January 2010	Exercised 2 February 2010	At 10 March 2010	Exercise price	Exercise period
26 June 2003	6,125,763	(6,125,763)	-	-	28.71p	up to 23 June 2010
26 June 2003	-	6,738,339	(6,738,339)	-	32.46p	up to 23 June 2010
27 May 2004	1,861,243	(1,861,243)	-	-	31.73p	up to 7 May 2011
27 May 2004	-	2,047,367	(465,244)	1,582,123	35.21p	up to 7 May 2011
1 June 2005	441,417	(441,417)	-	-	40.66p	up to 1 June 2012
1 June 2005	-	485,559	-	485,559	43.33p	up to 1 June 2012
13 June 2005	126,119	(126,119)	-	-	45.22p	up to 13 June 2012
13 June 2005	-	138,731	-	138,731	47.47p	up to 13 June 2012
21 July 2005	1,891,789	(1,891,789)	-	-	45.82p	up to 21 July 2012
21 July 2005	-	2,080,968	-	2,080,968	48.02p	up to 21 July 2012
1 January 2006	31,530	(31,530)	-	-	40.66p	up to 1 January 2013
1 January 2006	-	34,683	-	34,683	43.33p	up to 1 January 2013
15 August 2008	126,119	(126,119)	-	-	77.73p	15 August 2011 to 15 August 2015
15 August 2008	-	138,731	-	138,731	77.03p	15 August 2011 to 15 August 2015

## Notes to the Financial Statements (continued)

### 19 Reserves

<b>The Group</b>	Share premium reserve \$000	Retained earnings \$000
At 1 January 2009	93,337	(36,084)
Loss for the year	-	(3,768)
Share issue in the year	65,898	-
Share based payment charge	-	82
<b>At 31 December 2009</b>	<b>159,235</b>	<b>(39,770)</b>

  

<b>The Company</b>	Share premium reserve \$000	Retained earnings \$000
At 1 January 2009	93,337	(36,084)
Loss for the year	-	(3,768)
Share issue in the year	65,898	-
Share based payment charge	-	82
<b>At 31 December 2009</b>	<b>159,235</b>	<b>(39,770)</b>

### Share premium

The balance classified as share premium is the premium on issue of the Group's equity share capital, comprising £0.01 Pounds Sterling ordinary shares less any costs of issuing the shares.

### 20 Commitments

<b>Operating leases</b>	2008 Land and buildings \$000	2009 <b>Land and buildings</b> <b>\$000</b>
At the Balance Sheet date, the Group and Company had outstanding commitments for future minimum lease payments under non-cancellable operating leases, which fall due as follows:		
<b>Expiring:</b>		
Within 1 year	239	239
Between 1 and 5 years	17	23

Operating lease payments represent rentals payable by the Group for its office properties and oil exploration licences.

## Notes to the Financial Statements (continued)

### 21 Net cash flows from operating activities

<b>Reconciliation of operating loss to net cash from operating activities</b>	2008 \$000	<b>2009 \$000</b>
<b>Operating loss for the financial year</b>	(2,896)	(3,916)
Foreign exchange	1,018	2,731
Depreciation on property, plant and equipment	7	5
Share-based payment expense	498	82
Operating cash flows before movement in working capital	(1,373)	(1,098)
Decrease in receivables	29	50
Increase/(decrease) in payables	(321)	9,976
<b>Cash generated from operations</b>	<b>(1,665)</b>	<b>8,928</b>
Income tax paid	(400)	-
Interest paid	(13)	-
<b>Net cash from operating activities</b>	<b>(2,078)</b>	<b>8,928</b>

### 22 Cash and cash equivalents

	At 31 December 2008 \$000	Cash flows \$000	Exchange movement \$000	At 31 December 2009 \$000
Cash at bank and in hand	40,960	49,643	(2,759)	87,574
Bank overdraft	(59)	53	-	(6)
Cash at bank and in hand	40,631	49,696	(2,759)	<b>87,568</b>

## Notes to the Financial Statements (continued)

### 23 Related party transactions

The Group entered into transactions with the following companies in which certain of the Directors were materially interested:

<b>Company</b>	<b>Related party</b>			
Phipps & Company Limited	Mr S L Phipps and Mrs A R Neve			
Copernicus Consultancy Limited	Mr E Wisniewski			
Ardoyne Consultants Limited	Mr R Lyons			

  

<b>The transactions with the Group during the year were as follows</b>	<b>Total 2008</b>	<b>Services as a Director</b>	<b>Management services</b>	<b>Consultancy services</b>	<b>Total 2009</b>
	\$000	\$000	\$000	\$000	\$000
Ardoyne Consultants Limited	56	23	-	217	240
Phipps & Company Limited	678	47	481	-	528
Copernicus Consultancy Limited	15	-	-	46	46
Mr A G Windham	42	23	-	6	29
<b>At 31 December the following amounts were included in creditors:</b>				<b>2008 \$000</b>	<b>2009 \$000</b>
Mr A G Windham				-	<b>9</b>
Ardoyne Consultants Limited				-	<b>57</b>
Copernicus Consultancy Limited				-	<b>27</b>

In addition, The Company paid \$24,100 (2008 - \$16,800) to Phipps & Company Limited for the rent of offices.

### 24 Capital Commitments

At the year end, the Group has drilling commitments, as part of the lease agreement with the Falkland Islands Government, for oil exploration before May 2013 on Tranches C and D, before November 2012 on Tranches F, I and L and before August 2012 on PL034.