

28 April 2017

## REGAL PETROLEUM PLC

### 2016 AUDITED RESULTS

Regal Petroleum plc (the “Company”, and with its subsidiaries, the “Group”), the AIM-quoted (RPT) oil and gas exploration and production group, today announces its audited results for the year ended 31 December 2016.

#### Principal Developments

##### Ukraine Operations

- Average production from the MEX-GOL and SV fields over the year to 31 December 2016 was 157,228 m<sup>3</sup>/d of gas, 41 m<sup>3</sup>/d of condensate and 19 m<sup>3</sup>/d of LPG (1,321 boepd in aggregate) (2015: 144,783 m<sup>3</sup>/d of gas, 44 m<sup>3</sup>/d of condensate and 21 m<sup>3</sup>/d of LPG (1,274 boepd in aggregate))
- Average gas and condensate production from the VAS field for period from 4 July 2016 to 31 December 2016 was 82,624 m<sup>3</sup>/d of gas and 6.5 m<sup>3</sup>/d of condensate (556 boepd in aggregate)
- During 2016, the Group purchased 8,262,121 m<sup>3</sup> of “wet” gas and following treatment of this gas, produced 4,929,386 m<sup>3</sup> of gas, 1,448 m<sup>3</sup> of condensate and 11,034 m<sup>3</sup> of LPG (87,713 boe in aggregate) - this arrangement has now ended
- Operations on the MEX-109 well are continuing with testing expected to commence by May 2017 and, subject to successful testing, production hook-up by the end of the second quarter of 2017

##### Finance

- Revenue for the year to 31 December 2016 of \$25.7 million (2015: \$23.4 million)
- Loss for the year to 31 December 2016 of \$1.3 million (2015: \$1.0 million loss)
- Foreign exchange translation loss for the year of \$5.9 million (2015: \$22.8 million loss) due to devaluation of the Ukrainian Hryvnia against the US Dollar
- Cash generated from operations during the year of \$10.0 million (2015: \$8.8 million)
- Average realised gas, condensate and LPG prices in Ukraine for the year to 31 December 2016 of \$213/Mm<sup>3</sup> (UAH5,441/Mm<sup>3</sup>), \$51/bbl and \$43/bbl respectively (2015: \$318/Mm<sup>3</sup> (UAH6,906/Mm<sup>3</sup>) gas, \$64/bbl condensate and \$69/bbl LPG)
- Cash and cash equivalents at 31 December 2016 of \$20.0 million (31 December 2015: \$19.9 million), with cash and cash equivalents at 26 April 2017 of \$23.0 million, held as to \$11.2 million equivalent in Ukrainian Hryvnia and the balance of \$11.8 million equivalent predominately in US Dollars and Sterling

##### Outlook

- Improving geopolitical outlook in Ukraine has led to gradual increase in development programme for 2017
- Focus during 2017 at MEX-GOL and SV fields on completion of MEX-109 well, further geophysical studies on existing seismic data, joint venture arrangement for workover of SV-2 well, workover of GOL-2 well, installation of additional compression equipment, continued investment in gas processing facilities and pipeline network, and upgrading of existing wells
- Focus during 2017 at VAS field on reinterpretation of existing seismic data, acquisition of new 3D seismic and drilling of VAS-10 well

- Funding of 2017 development programme anticipated to be from existing cash and cash equivalents and operational cash flow

The Annual Report and Financial Statements for 2016, together with the Notice of Annual General Meeting, will be posted to shareholders and published on the Company's website during May 2017.

This announcement contains inside information for the purposes of Article 7 of EU Regulation 596/2014.

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Philip Frank, PhD Geology, Chartered Geologist, FGS, PESGB, consultant to the Company, has reviewed and approved the technical information contained within this press release in his capacity as a qualified person, as required under the AIM Rules.

**Definitions**

bbbl	barrel
boe	barrels of oil equivalent
Bscf	thousands of millions of scf
boepd	barrels of oil equivalent per day
HSES	health, safety, environment and security
km	kilometres
km <sup>2</sup>	square kilometres
LPG	liquefied petroleum gas
MEX-GOL	Mekhediviska-Golotvshinska
m <sup>3</sup>	cubic metres
m <sup>3</sup> /d	cubic metres per day
Mm <sup>3</sup>	thousand cubic metres
MMm <sup>3</sup>	million cubic metres
Mtonnes	thousand tonnes
MMbbl	million barrels
MMboe	million barrels of oil equivalent
%	per cent
scf	standard cubic feet measured at 14.7 pounds per square inch and 60 degrees Fahrenheit
SV	Svyrydivske
\$	United States Dollar
UAH	Ukrainian Hryvnia
VAS	Vasyshevskoye
VVD	Vvdenska

## Chairman's Review

The Group is continuing with the development of its Mekhediviska-Golotvshinska ("MEX-GOL") and Svyrydivske ("SV") gas and condensate fields in north-eastern Ukraine, which are held under 100% owned and operated production licences. Production at these fields has been reasonably steady during the 2016 year, and in July 2016, the Group commenced the drilling of a new well, MEX-109, within the MEX-GOL licence area.

In July 2016, the Group acquired a 100% shareholding interest in LLC Prom-Enerho Produkt ("PEP") for a cash consideration of UAH305 million (approximately \$12.3 million as at that date). Further details of the assets and liabilities acquired are set out in Note 32. PEP holds a production licence over the Vasyshevskoye ("VAS") gas and condensate field, which also includes the Vvdenska ("VVD") prospect, located in the Dnieper-Donets basin in the north-east of Ukraine. The VAS field contained Proved and Probable Reserves (2P) of 1.80 MMboe of gas and condensate, as well as Contingent Resources, and additional Prospective Resources at the VVD prospect, as assessed by Senergy (GB) Limited as at 1 January 2016. Further details of these estimates of Reserves and Resources can be found in the Operations Review section below.

The fiscal and economic situation in Ukraine is improving slowly, with a better economic outlook, lower rates of inflation and less volatility in the Ukrainian Hryvnia exchange rates. The Ukrainian Government has implemented a number of reforms in the oil and gas industry, which include the deregulation of the gas supply market in late 2015. Nevertheless, there continue to be stresses in the economy and weaknesses in the Ukrainian banking sector.

There has been a degree of volatility and weakness in gas prices in Ukraine, following the fall in European gas prices during the year, but the deregulation of the gas supply market has meant that the market gas prices now broadly correlate to the imported gas prices.

As regards the Group's financial performance in the year ended 31 December 2016, a loss of \$1.3 million (2015: \$1.0 million loss) was made, mainly due to lower foreign exchange translation losses offset by lower realised hydrocarbon prices. Cash generated from operations during the year was positive at \$10.0 million (2015: \$8.8 million).

Average daily production of gas, condensate and LPG from the MEX-GOL and SV fields for the year ended 31 December 2016 was 1,321 boepd in aggregate, which was higher compared to 2015 predominately due to the commencement of production from the SV-6 well in late November 2015, which boosted gas production levels (2015: 1,274 boepd in aggregate).

The average daily production of gas and condensate from the VAS field for the period from 4 July 2016 to 31 December 2016 was 521 boepd in aggregate, adding material volumes to the Group's production output.

The MEX-109 well was spudded at the end of July 2016, targeting the Visean reservoirs ("B-Sands") in the MEX-GOL field, and has been drilled to a depth of 4,873 metres. The well had an original target depth of 5,250 metres but, due to some technical issues, further drilling activities were curtailed once the primary reservoir targets were accessible. It is anticipated that completion operations will be concluded in May 2017, after which well testing will commence, and subject to successful testing, production hook-up completed by the end of the second quarter of 2017.

The difficult geopolitical situation in Ukraine over the past few years had meant that the Group considered it necessary to reduce its capital investment programme at the MEX-GOL and SV fields, and consequently, the programme during 2016 was limited to the commencement of drilling of the MEX-109 well, improvements to the Group's gas processing facilities and pipeline network and performing remedial work on existing wells. In addition, the Group engaged P.D.F Limited to undertake a comprehensive review and re-evaluation study of the geology, geophysics, petroleum engineering and well performance at the MEX-GOL and SV fields.

## **Business Review and Outlook**

The slowly improving geopolitical and economic climate in Ukraine is cause for some optimism and the Group is now stepping up its planning for the further development of the MEX-GOL, SV and VAS fields.

As well as drilling the MEX-109 well at the MEX-GOL field, the Group is utilising the results of P.D.F Limited's study to plan additional development of the MEX-GOL and SV fields. The study has provided an enhanced understanding of the subsurface at the fields, as well as recommendations for future development work. Further geophysical studies, using the latest processing technology, are underway to try to further utilise existing seismic data in the programme. In addition, the Group is planning the workover of the GOL-2 well, the installation of additional compression equipment, further investment in the gas processing facilities and pipeline network, and upgrading existing wells.

At the VAS field, following the reinterpretation of existing 3D seismic data, the Group plans to commence drilling a new well, VAS-10, and to acquire new 3D seismic in late 2017.

The Group has also recently entered into an agreement with NJSC Ukrnafta, the partially State-owned oil and gas producer, relating to the SV-2 well, which is a suspended well owned by NJSC Ukrnafta located within the Group's SV licence area. Under the agreement, the Group will carry out a workover of the well and, if successful, operate, produce and sell the gas and condensate from the well under an equal net profit sharing arrangement with NJSC Ukrnafta. Planning for this workover is underway and it is anticipated that work will commence in the second quarter of 2017.

It is hoped that the situation in Ukraine will continue to improve over the coming months, allowing better visibility on the political and economic outlook and in turn assisting with the Group's development planning for its Ukrainian assets.

In conclusion, on behalf of the Board, I would like to thank our staff for the continued dedication and support they have shown over the period.

**Keith Henry**  
Executive Chairman

## **Operations Review**

### **Health, Safety, Environment and Security (“HSES”)**

The Group is committed to maintaining the highest HSES standards and the effective management of these areas is an intrinsic element of the overall business ethos. Through strict enforcement of the Group’s HSES Management System, together with regular management meetings, training and the appointment of dedicated safety professionals, the Group strives to ensure that the impact of its business activities on its staff, contractors and the environment is as low as is reasonably practicable. The Group reports safety and environmental performance in accordance with industry practice and guidelines.

## **Ukraine Operations**

### **Overview of Assets**

#### **1. MEX-GOL and SV fields**

Regal Petroleum Corporation Limited (a wholly owned subsidiary in the Group) holds a 100% working interest in and is the operator of the MEX-GOL and SV fields. The production licences extend over a combined area of 269 km<sup>2</sup>, approximately 200 km east of Kiev. The two licences are adjacent and the interests are operated and managed as one field. The licences were granted in July 2004 and have a duration of 20 years.

The fields are located, geologically, towards the middle of the Dnieper-Donets sedimentary basin which extends across the majority of north-east Ukraine. The vast majority of Ukrainian gas and condensate production comes from this basin. The reservoir comprises a series of gently dipping Carboniferous sandstones of Visean age (“B-Sands”) inter-bedded with shales that form stratigraphic traps at around 4,700 metres below the surface, with a gross thickness between 800 metres and 1,000 metres. Analysis suggests that these deposits range from fluvial to deltaic in origin. Below these reservoirs is a thick sequence of shale above deeper, similar, sandstones which are encountered at a depth of around 5,800 metres. These sands are of Tournasian age (“T-Sands”). Deeper sandstones of Devonian age (“D-Sands”) have also been penetrated in the fields.

#### **2. VAS field**

LLC Prom-Enerho Produkt (a wholly owned subsidiary in the Group) holds a 100% working interest in and is the operator of the VAS field. The production licence extends over an area of 33.2 km<sup>2</sup> and is located approximately 17 km south-east of Kharkiv. The licence was granted in August 2012 and has a duration of 20 years.

The field is also located, geologically, towards the middle of the Dnieper-Donets sedimentary basin in the north-east of Ukraine. The field is trapped in an anticline structure broken into several blocks, which are gently dipping to the north, stretching from the northeast to southwest along a bounding fault. The gas is located in Carboniferous sandstones of Bashkirian, Serpukhovian and Visean age at depths of 2,900 – 3,400 metres below the surface.

### **Production**

Average production from the MEX-GOL and SV fields over the year ended 31 December 2016 was 157,228 m<sup>3</sup>/d of gas, 41 m<sup>3</sup>/d of condensate and 19 m<sup>3</sup>/d of LPG, which equates to a combined total oil equivalent of 1,321 boepd (2015: 144,783 m<sup>3</sup>/d of gas, 44 m<sup>3</sup>/d of condensate and 21 m<sup>3</sup>/d of LPG (1,274 boepd in aggregate). Production rates improved following the commencement of production from the SV-6 well at the end of November 2015.

Average gas and condensate production from the VAS field for the period from the date of acquisition on 4 July 2016 to 31 December 2016 was 82,624 m<sup>3</sup>/d of gas and 6.5 m<sup>3</sup>/d of condensate, which equates to a combined total oil equivalent of 556 boepd.

The Group’s average production for the period from 1 January 2017 to 26 April 2017 from the MEX-GOL and SV field was 129,202 m<sup>3</sup>/d of gas, 33 m<sup>3</sup>/d of condensate and 17 m<sup>3</sup>/d of LPG (1,089 boepd in

aggregate) and from the VAS field was 86,951 m<sup>3</sup>/d of gas and 6.6 m<sup>3</sup>/d of condensate (613 boepd in aggregate).

Since early July 2015, the Group had been purchasing “wet” gas from Pryrodni Resursy, the operator of the adjacent Lutsenky field, and treating such “wet” gas through the Group’s gas processing facilities to strip out and sell the liquids. This operation produced additional income and improved the utilisation of the Group’s gas processing facilities. During 2016, the Group purchased 8,262,121 m<sup>3</sup> of “wet” gas and following treatment of this gas, produced 4,929,386 m<sup>3</sup> of gas, 1,448 m<sup>3</sup> of condensate and 11,034 m<sup>3</sup> of LPG (87,713 boe in aggregate). This arrangement concluded in December 2016 as a result of Pryrodni Resursy constructing its own facilities.

### **Operations**

The geopolitical situation, the volatility in the gas price, the weakness of the Ukrainian Hryvnia, and the fiscal and economic uncertainty in Ukraine over recent years, meant that the Group considered it necessary to reduce its capital investment programme at the MEX-GOL and SV fields during 2016. The programme during the year was limited to the commencement of the drilling of the MEX-109 well, improvements to the Group’s gas processing facilities and pipeline network, and performing remedial work on existing wells.

However, during the year, the Group engaged P.D.F Limited to undertake a comprehensive review and re-evaluation study of the geology, geophysics, petroleum engineering and well performance at the MEX-GOL and SV fields. The results of the study are now being utilised in the planning of the further development of the fields, both in relation to an improved understanding of the geological aspects of the fields and reservoir engineering, drilling and completion techniques. Reprocessing of existing seismic data, using the latest processing technology, is being undertaken to try to improve the definition in such data, and thereafter further interpretation work is planned.

The MEX-109 well was spudded at the end of July 2016, targeting the Visean reservoirs (“B-Sands”) in the MEX-GOL field. The well has been drilled to a depth of 4,873 metres, which is shallower than its original target depth of 5,250 metres following some technical issues during the drilling operations. As a result, it was decided to curtail the well at this depth as access to the main reservoir target had been achieved. The well may be deepened later to access deeper horizons. Completion operations are scheduled to be concluded in May 2017, after which well testing will commence, and subject to successful testing, it is hoped that the well will be hooked-up for production by the end of the second quarter of 2017.

### **Reserves**

#### **1. MEX-GOL and SV fields**

The Group’s estimates of the remaining Reserves and Resources at the MEX-GOL and SV licence areas are derived from an assessment undertaken by independent petroleum consultants, ERC Equipoise Limited (“ERCE”), as at 31 December 2013 (the “ERCE Report”), which was announced on 25 March 2014. During the period from 1 January 2014 to 31 December 2016, the Group has produced 1.45 MMboe from these fields.

The ERCE Report estimated the remaining Reserves as at 31 December 2013 in the Visean B-Sands reservoirs of the MEX-GOL and SV fields, based on the drilling of ten further wells, as follows:-

	Proved (1P)	Proved + Probable (2P)	Proved + Probable + Possible (3P)
Gas	8.3 Bscf	50.1 Bscf	71.2 Bscf
Condensate	0.4 MMbbl	2.5 MMbbl	4.1 MMbbl
LPG	17.4 Mtonnes	105.6 Mtonnes	149.8 Mtonnes
<b>Total</b>	<b>1.9 MMboe</b>	<b>11.7 MMboe</b>	<b>17.2 MMboe</b>

The ERCE Report estimated the Contingent Resources in the Visean B-Sands reservoirs of the MEX-GOL and SV fields as follows, based on the potential drilling of up to 113 future wells (not currently budgeted):-

	Contingent Resources (1C)	Contingent Resources (2C)	Contingent Resources (3C)
Gas	198 Bscf	334 Bscf	519 Bscf
Condensate	8.5 MMbbl	17.4 MMbbl	32.7 MMbbl
<b>Total</b>	<b>41.5 MMboe</b>	<b>73.1 MMboe</b>	<b>119.1 MMboe</b>

## 2. VAS field

The Group's estimates of the remaining Reserves and Resources at the VAS field and the Prospective Resources at the VVD prospect are derived from an assessment undertaken by independent petroleum consultants, Senergy (GB) Limited, as at 1 January 2016 (the "Senergy Report"), which was announced on 5 July 2017 in connection with the Group's acquisition of PEP. During the period from 1 January 2016 to 31 December 2016, 0.2 MMboe were produced from the field.

The Senergy Report estimates the remaining Reserves as at 1 January 2016 in the VAS field, based on the drilling of one further well, as follows:-

	Proved (1P)	Proved + Probable (2P)	Proved + Probable + Possible (3P)
Gas	91.5 MMm <sup>3</sup>	251.5 MMm <sup>3</sup>	448.6 MMm <sup>3</sup>
Condensate	6.90 Mtonne	19.0 Mtonne	33.82 Mtonne
<b>Total</b>	<b>0.66 MMboe</b>	<b>1.80 MMboe</b>	<b>3.21 MMboe</b>

The Senergy Report estimates the Contingent Resources as at 1 January 2016 in the VAS field, based on the drilling of an additional further well, as follows:-

	Contingent Resources (1C)	Contingent Resources (2C)	Contingent Resources (3C)
Gas	153.0 MMm <sup>3</sup>	280.3 MMm <sup>3</sup>	515.4 MMm <sup>3</sup>
Condensate	6.3 Mm <sup>3</sup>	11.4 Mm <sup>3</sup>	20.7 Mm <sup>3</sup>
<b>Total</b>	<b>158.6 MMm<sup>3</sup></b>	<b>294.5 MMm<sup>3</sup></b>	<b>538.0 MMm<sup>3</sup></b>

The Senergy Report estimates the Prospective Resources as at 1 January 2016 in the VVD prospect as follows:-

	Low	Best	High	Mean
Gas and Condensate	441.8 MMm <sup>3</sup>	1,078.9 MMm <sup>3</sup>	2,582.6 MMm <sup>3</sup>	1,234.7 MMm <sup>3</sup>



## Finance Review

The Group's loss for the year ended 31 December 2016 was \$1.3 million (2015: \$1.0 million loss), mainly due to lower foreign exchange translation losses of \$5.9 million (2015: 22.8 million) offset by lower realised hydrocarbon prices. Revenue in 2016, derived from the sale of the Group's Ukrainian gas, condensate and LPG production, was higher at \$25.7 million, including revenue of \$3.7 million from the VAS field following its acquisition in July 2016 (2015: \$23.4 million), primarily due to improved production volumes offset by lower realisations as a result of devaluation of the Ukrainian Hryvnia.

Cash generated from operations during the year was \$10.0 million (2015: \$8.8 million), which was higher due to higher production volumes, despite lower hydrocarbon prices.

For the year ended 31 December 2016, the average realised gas, condensate and LPG prices were \$213/Mm<sup>3</sup> (UAH5,441/Mm<sup>3</sup>), \$51/bbl and \$43/bbl respectively (2015: \$318/Mm<sup>3</sup> (UAH6,906/Mm<sup>3</sup>) gas, \$64/bbl condensate and \$69/bbl LPG).

During the first quarter of 2017, the average realised gas, condensate and LPG prices were \$245/Mm<sup>3</sup> (UAH6,622/Mm<sup>3</sup>), \$59/bbl and \$49/bbl respectively. The current realised gas price is \$199/Mm<sup>3</sup> (UAH5,295/Mm<sup>3</sup>).

Since the deregulation of the gas supply market in Ukraine in October 2015, the market price for gas has broadly correlated to the price of imported gas, which trended lower during 2016 but recovered towards the end of the year, reflecting the movement in European gas prices. In addition, declines in industrial consumption resulting from the economic issues in Ukraine have contributed to weakness in demand and gas price in the gas supply market.

The subsoil taxes rates applicable to gas and condensate production have been stable during the year at 29% for gas produced from deposits at depths above 5,000 metres and 14% for gas produced from deposits below 5,000 metres, and 45% for condensate produced from deposits above 5,000 metres and 21% for condensate produced from deposits below 5,000 metres.

With effect from 1 April 2017, a transmission tariff for use of the Ukrainian national pipeline system became applicable to oil and gas producers in Ukraine, including the Group, which will increase the Group's cost of sales. The tariff is set at UAH296.80/Mm<sup>3</sup> (\$11.00/Mm<sup>3</sup>).

Cost of sales for the year ended 31 December 2016 was lower at \$18.6 million (2015: \$19.8 million), mainly due to the reduction in subsoil tax rates and reduced exchange rate fluctuations.

Administrative expenses for the year were higher at \$4.7 million (2015: \$4.0 million), primarily due to expenditure on consultants related to the acquisition of PEP.

The tax charge for the year of \$4.1 million (2015: \$2.6 million) comprises a current tax charge of \$1.9 million (2015: \$1.3 million) and a deferred tax charge of \$2.2 million (2015: \$1.3 million).

The Group has recognised a deferred tax asset of \$11.1 million at 31 December 2016 (31 December 2015: \$14.4 million). This comprises a deferred tax asset of \$3.7 million (31 December 2015: \$4.4 million) in relation to UK tax losses carried forward, and \$7.4 million (31 December 2015: \$10.0 million) relating to the Group's MEX-GOL and SV asset in Ukraine, which is recognised on the tax effect of temporary timing differences between the carrying value of such asset and its tax base, following its impairment in 2013. The reduction in the deferred tax asset in 2016 is primarily due to a decrease of forecasted taxable income for the following 5 years caused by impairment of the loans receivable and weakening of the Euro against the US Dollar. The Group has also recognised a deferred tax liability of \$1.2 million at 31 December 2016 (31 December 2015: nil) relating to the Group's VAS asset in Ukraine, which is recognised on the tax effect of temporary timing differences between the carrying value of such asset and its tax base mainly due to revaluation of the VAS asset at the date of acquisition by the Group.

Capital investment of \$13.9 million reflects investment in the Group's MEX-GOL and SV oil and gas development and production asset for the year of \$6.2 million and capital additions due to the acquisition of PEP of \$7.7 million (2015: \$2.3 million). Capital investment on the MEX-GOL and SV fields was higher in the period primarily due to the expenditure associated with the drilling of the MEX-109 well.

Cash and cash equivalents held at 31 December 2016 were \$20.0 million (31 December 2015: \$19.9 million). The Group's cash and cash equivalents balance at 26 April 2017 was \$23.0 million, held as to \$11.2 million equivalent in Ukrainian Hryvnia and the balance of \$11.8 million equivalent predominantly in US Dollars and Sterling.

Since early 2014, the Ukrainian Hryvnia has devalued significantly against the US Dollar, falling from UAH8.3/\$1.00 on 1 January 2014 to UAH27.2/\$1.00 on 31 December 2016, which resulted in substantial foreign exchange translation losses for the Group over that period, and in turn adversely impacted the carrying value of the MEX-GOL and SV asset due to the translation of two of the Group's subsidiaries from their functional currency of Ukrainian Hryvnia to the Group's presentation currency of US Dollars. However in 2016, the exchange rate between the Ukrainian Hryvnia and the US Dollar has been reasonably stable averaging UAH27.0/\$1.00 during the period (rate as at 31 December 2016: UAH27.2/\$1.00).

Since 2014, in an effort to combat the weakness in the Ukrainian Hryvnia, the National Bank of Ukraine has imposed comprehensive restrictions on the purchase of foreign currency and the remittance of funds outside Ukraine. Due to these banking restrictions, the Group was unable to remit funds outside Ukraine, which resulted in the Group's cash holdings in Ukrainian Hryvnia remaining at high levels. However, improvements to the stability of the Ukrainian Hryvnia have meant that the National Bank of Ukraine has recently started to relax the banking restrictions. In light of the stresses in the banking sector in Ukraine, the Group is endeavouring to diversify its banking arrangements between a number of banks in Ukraine.

During the year, the Group held bank accounts in Ukraine with PJSC Unex Bank ("Unex Bank") which is indirectly controlled by Mr V Novinskiy, who also controls a majority shareholding in the Group. As a result, Unex Bank is a related party to the Group. At 30 June 2016, the Group had cash deposits of \$12.3 million (held in Ukrainian Hryvnia) in Unex Bank. Such cash deposits were recorded in the financial statements of the Group as short-term investments (with a carrying value equal to the cash deposits), rather than cash or cash equivalents due to the limited liquidity of the asset. On 4 July 2016, in a related party transaction, the Group acquired a 100% interest in PEP from LLC Interregional Pellet Company, a company within the PJSC Smart-Holding Group (the "Smart Holding Group"), for a cash consideration of UAH305 million (approximately \$12.3 million as at that date), thereby utilising substantially all of the Group's cash deposits in Unex Bank.

The Group has undertaken an assessment of the fair value of the assets and liabilities recognised as a result of the acquisition of PEP which demonstrates assets of \$16.2 million and liabilities of \$3.9 million as at the date of acquisition. Further details are set out in Note 32 below.

Cash from operations has funded the capital investment during the year, and the Group's current cash position and positive operating cash flow are the sources from which the Group expects to fund the development programmes for its assets in 2017.

The Group manages its revenue, cash from operations and production volumes as key performance indicators. The achieved results for 2016 were as follows:

- revenue of \$25.7 million (2015: \$23.4 million)
- cash from operations of \$10.0 million (2015: \$8.8 million)
- daily production volumes from the MEX-GOL and SV fields for the year of 157,228 m<sup>3</sup>/d of gas, 41 m<sup>3</sup>/d of condensate and 19 m<sup>3</sup>/d of LPG (1,321 boepd in aggregate) (2015: 144,783 m<sup>3</sup>/d of gas, 44 m<sup>3</sup>/d of condensate and 21 m<sup>3</sup>/d of LPG (1,274 boepd in aggregate))
- aggregate production volumes from the MEX-GOL and SV fields for the year of 57,545,607 m<sup>3</sup> of gas, 15,146 m<sup>3</sup> of condensate and 7,014 m<sup>3</sup> of LPG, equating to a combined total oil equivalent of 483,603 boe (2015: 52,845,895 m<sup>3</sup> of gas, 16,014 m<sup>3</sup> of condensate and 7,620 m<sup>3</sup> of LPG (464,886 boe in aggregate)).

In addition, the Group produced 82,624 m<sup>3</sup>/d of gas and 6.5 m<sup>3</sup>/d of condensate (556 boepd in aggregate) from the VAS field for the period from its acquisition on 4 July 2016 to 31 December 2016, with aggregate production volumes for such period of 14,955,029 m<sup>3</sup> of gas, 1,178 m<sup>3</sup> of condensate, equating to a combined total oil equivalent of 100,701 boe.

The ongoing situation in Ukraine has resulted in a significant devaluation of the Ukrainian Hryvnia against the US Dollar, continued devaluation of which may affect the carrying value of the Group's assets in the future.

## **Operational Environment, Principal Risks and Uncertainties**

The Group has a risk evaluation methodology in place to assist in the review of the risks across all material aspects of its business. This methodology highlights technical, operational, external and fiduciary risks and assesses the level of risk and potential consequences. It is periodically presented to the Audit Committee and the Board for review, to bring to their attention potential concerns and, where possible, propose mitigating actions. Key risks recognised are detailed below:-

### *Risks relating to Ukraine*

The Ukrainian economy is currently characterised by high political and economic risks. As a developing economy, in addition to the impact of local political and economic instability, Ukraine's economy is vulnerable to market downturns and economic slowdowns elsewhere in the world.

Since late 2013, the political and economic situation in Ukraine has experienced significant instability and uncertainty, which has led to a deterioration of Ukrainian State finances, volatility of financial markets, illiquidity on capital markets, high inflation and a substantial depreciation of the Ukrainian Hryvnia against major foreign currencies. This instability and uncertainty continued during 2016, but to a lesser extent than during 2014 - 2015. During 2016, there were signs of economic improvement with Ukraine's GDP returning to growth of 1% and annual inflation declining to 12% (2015: GDP decreased by 10%; inflation increased by 43%).

The conflict in parts of eastern Ukraine, which started in spring 2014, has not been resolved to date. However, there has been no substantial escalation of the conflict since the signing of a ceasefire agreement in February 2015. Russia continues to occupy Crimea and has commenced the construction of a bridge directly between Russia and Crimea.

The Group has no assets in Crimea or the areas of conflict in the east of Ukraine, nor do its operations rely on sales or costs incurred there.

The conflict in the region has put further pressure on relations between Ukraine and Russia, and the political tensions have had an adverse effect on the Ukrainian financial markets, hampering the ability of Ukrainian companies and banks to obtain funding from the international capital and debt markets.

On 1 January 2016, the agreement on the free trade area between Ukraine and the European Union came into force. The Russian Government reacted to this event by implementing a trading embargo on many key Ukrainian export products. In response, the Ukrainian Government implemented similar measures against Russian products.

The banking system in Ukraine remains fragile due to its weak level of capital, low asset quality caused by the economic situation, currency depreciation, changing regulations and other economic pressures generally.

In March 2015, an Extended Funding Facility from the International Monetary Fund amounting to \$17.5 billion over a four year period was agreed. The terms of this funding package stipulated a number of fiscal and economic reforms, including reforms in the banking and energy sectors. Since then, Ukraine has received four tranches under the funding programme totalling \$8.4 billion. Further disbursements of International Monetary Fund tranches depend on the implementation of Ukrainian Government reforms, and other economic, legal and political factors.

Despite some improvements, the final resolution and the ongoing effects of the political and economic situation in Ukraine are difficult to predict but they may have severe effects on the Ukrainian economy and the Group's business.

These events have not materially affected the Group's production operations to date, but the instability has disrupted the Group's development and operational planning for its assets. Furthermore, the political, fiscal and economic instability has impacted the Group's normal business activities, and increased the risks relating to its business operations, financial status, access to secure banking facilities and maintenance of its Ukrainian production licences.

The Ukrainian Government is keen to develop the country's domestic production of hydrocarbons since Ukraine imports a significant proportion of its gas. While this should put the Group in a well-placed

position, as experienced previously, there are significant risks to carrying out business in the country. It is considered that the involvement of Energees Management Limited, as a major shareholder with extensive experience in Ukraine, has helped to mitigate such risks.

#### *Going concern risk*

The Group is exposed to risks relating to Ukraine as well as production, hydrocarbon price and other risks, as detailed in this Operational Environment, Principal Risks and Uncertainties section. In view of this, the Group prepares monthly cash flow forecasts which take into account the risks facing the business, to assess its ability to meet its obligations as they fall due, taking into account the risks of variances in revenues.

Having reviewed the financial statements, budgets and forward plans (including sensitivity analysis), the latest operational results, the risks outlined herein, and having taken into account the Group's cash holdings, the current practice of contracting for drilling services on a fixed-price basis for each well, the assessment of well results prior to entering into firm commitments for future drilling operations and the lower committed expenditure in Ukraine, the Directors continue to believe that the Group is able to manage its business risks successfully despite the current uncertain political and economic outlook. The Directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future regarded as at least 12 months from the date of signing of the Group's financial statements. Therefore they continue to adopt the going concern basis of accounting in preparing the financial statements.

#### *Production risks*

Producing gas and condensate reservoirs are generally characterised by declining production rates which vary depending upon reservoir characteristics and other factors. Future production of the Group's gas and condensate reserves, and therefore the Group's cash flow and income, are highly dependent on the Group's success in operating existing producing wells, drilling new production wells and efficiently developing and exploiting any reserves, and finding or acquiring additional reserves. The Group may not be able to develop, find or acquire reserves at acceptable costs. The experience gained from drilling undertaken to date highlights such risks as the Group targets the appraisal and production of these hydrocarbons. During 2016, the Group engaged external technical consultants to undertake a comprehensive review and re-evaluation study of the MEX-GOL and SV fields in order to gain an improved understanding of the geological aspects of the fields and reservoir engineering, drilling and completion techniques, and the results of this study and further planned technical work will be used by the Group in the future development of these fields.

#### *Risks relating to further development and operation of the Group's gas and condensate fields in Ukraine*

The planned development and operation of the Group's gas and condensate fields in Ukraine is susceptible to appraisal, development and operational risk. This could include, but is not restricted to, delays in delivery of equipment in Ukraine, failure of key equipment, lower than expected production from wells that are currently producing, or new wells that are brought on-stream, problematic wells and complex geology which is difficult to drill or interpret. The generation of significant operational cash is dependent on the successful delivery and completion of the development and operation of the fields. These risks have been demonstrated by the previous downgrade in the Group's remaining reserves which resulted in the reduction in the value in use, and consequent impairment loss relating to the Group's MEX-GOL and SV asset in Ukraine. Furthermore, the optimisation of the Group's assets is dependent on maintaining constructive relationships between all business stakeholders.

#### *Exposure to credit, liquidity and cash flow risk*

The Group does not currently have any loans outstanding. Local customers are managed in Ukraine and their financial position, the Group's past experience and other factors are evaluated. Internal financial projections are regularly made based on the latest estimates available, and various scenarios are run to assess the robustness of the liquidity of the Group. The Group currently holds sufficient cash and cash equivalents for the anticipated short to medium term needs of the business. Whilst much of the future capital requirement is expected to be derived from operational cash generated from production, including from wells yet to be drilled, there is a risk that in the longer term insufficient operational cash is generated, or that additional funding, should the need arise, cannot be secured. As the risk to future capital funding is inherent in the oil and gas exploration and development industry and reliant in part on future development success, it is difficult for the Group to take any particular measures at this time to mitigate this risk, other than tailoring its development activities to its available capital funding from time to time.

### *Risks relating to the Ukrainian banking sector*

The instability in Ukraine has led to a significant deterioration of Ukraine's finances, volatility in financial markets, illiquidity on capital markets and a substantial depreciation of the Ukrainian Hryvnia against major foreign currencies. As a result, significant external financing is required to maintain the country's economic stability. In 2014, the National Bank of Ukraine, amongst other measures, imposed comprehensive restrictions on the processing of client payments by banks, on the purchase of foreign currency on the inter-bank market and on the remittance of funds outside Ukraine, with particular restrictions on operations with foreign currency including temporary bans on the payment of dividends in foreign currency and the early repayment of debts to non-residents and the mandatory sale of 75% of revenue in foreign currency. However, during 2016 there was some limited easing of these restrictions, with the required share of foreign currency for mandatory sale being reduced to 65%, the settlement period for export-import transactions in foreign currency being increased from 90 to 120 days and Ukrainian companies being permitted to pay dividends to non-residents up to a limit of \$5 million per month.

These banking restrictions and the many other economic issues in Ukraine have put great strain on the Ukrainian banking system, with increasing risks in the capital strength, liquidity and creditworthiness of a number of banks, and very high rates in the wholesale and overnight markets. In addition, there have been significant deposit outflows from the banking system and widespread restructuring of bank clients' maturing liabilities, as well as the failure and/or bail out of a number of Ukrainian banks.

The Extended Funding Facility from the International Monetary Fund approved in March 2015, required significant reforms to the Ukrainian banking sector, which are now being implemented. The reforms are being overseen by the National Bank of Ukraine and involve all banks being inspected and assessed, with particular emphasis on lending to a bank's related parties. The inspections are designed to enable the National Bank to assess the financial strength and liquidity of the banks in Ukraine, and may lead to the National Bank imposing remedial measures, ranging from the imposition of requirements for a bank to bolster its capital strength, requirements for a bank to reduce its exposure to related party lending, the appointment of an administrator to manage the priority of payments by a bank, or in the most extreme cases, the liquidation of a bank.

In light of the deterioration in the banking sector in Ukraine, the Group has taken and continues to take steps to diversify its banking arrangements between a number of banks in Ukraine. These measures are designed to spread the risks associated with each bank's creditworthiness, but the Ukrainian banking sector remains weakly capitalised and so the risks associated with the banks in Ukraine remain significant.

The creditworthiness and potential risks relating to the majority of banks in Ukraine are regularly reviewed by the Group, but the ongoing geopolitical and economic events in Ukraine have significantly weakened the Ukrainian banking sector and so the risks associated with the banks in Ukraine remain significant, including in relation to the banks with which the Group operates bank accounts.

### *Currency risk*

The Group's main activities are (i) investment into the development of the Group's Ukrainian gas and condensate assets; (ii) the production and sale of gas, condensate and LPG; and (iii) the continued exploration for further hydrocarbon reserves.

The Group receives sales proceeds in Ukrainian Hryvnia, and the majority of the capital expenditure costs for the 2017 investment programme will be incurred in Ukrainian Hryvnia, thus revenue and costs are largely matched. As with all currencies, the value of the Ukrainian Hryvnia is subject to foreign exchange fluctuations, but as the Ukrainian Hryvnia does not benefit from the range of currency hedging instruments which are available in more developed economies, the Group had previously adopted a policy that, where possible, funds not required for use in Ukraine be retained on deposit in the United Kingdom, principally in US Dollars. However, the banking restrictions, referred to above, on the purchase of foreign currency and the remittance of funds outside Ukraine have meant that the Group was unable to follow this policy during 2016, and as a result, the Group's cash holdings of Ukrainian Hryvnia in Ukraine remained at a high level during the year. However, there has recently been some relaxation in the restrictions which has enabled the Group to reduce its cash holdings of Ukrainian Hryvnia in Ukraine.

Furthermore, since the beginning of 2014, the Ukrainian Hryvnia has significantly devalued against major world currencies, including against the US Dollar, where it has fallen from UAH8.3/\$1.00 on 1 January

2014 to UAH27.2/\$1.00 on 31 December 2016. As at 26 April 2017, the Ukrainian Hryvnia was trading at UAH26.6/\$1.00. This devaluation was one of the main reasons for the imposition of the abovementioned banking restrictions by the National Bank of Ukraine. In addition, the events in Ukraine over recent years, as outlined above in *“Risks relating to Ukraine”*, are likely to continue to impact the valuation of the Ukrainian Hryvnia against major world currencies. Further devaluation of the Ukrainian Hryvnia against the US Dollar will affect the carrying value of the Group’s assets.

#### *Ukraine Production Licences*

The Group operates in a region where the right to production can be challenged by State and non-State parties. During 2010, this manifested itself in the form of a Ministry Order instructing the Group to suspend all operations and production from its MEX-GOL and SV production licences, which was not resolved until mid-2011. In 2013, new rules relating to the updating of production licences led to further challenges being raised by the Ukrainian authorities to the production licences held by independent oil and gas producers in Ukraine, including the Group, which may result in requirements for remediation work, financial penalties and/or the suspension of such licences, which, in turn, may adversely affect the Group’s operations and financial position. All such challenges affecting the Group have thus far been successfully defended through the Ukrainian legal system. However, the business environment is such that these type of challenges may arise at any time in relation to the Group’s operations, licence history, compliance with licence commitments and/or local regulations. The Group endeavours to ensure compliance with commitments and regulations through Group procedures and controls or, where this is not immediately feasible for practical or logistical considerations, seeks to enter into dialogue with the relevant Government bodies with a view to agreeing a reasonable time frame for achieving compliance or an alternative, mutually agreeable course of action.

The Group’s production licences for the MEX-GOL and SV field currently expire in 2024. However, in the estimation of its reserves, it is assumed that the field development will continue until the end of the field’s economic life in 2036, and a consequent assumption is made that licence extensions will be granted in accordance with current Ukrainian legislation. Despite such legislation, it is possible that licence extensions will not be granted, which would affect the achievement of full economic field development and consequently the carrying value of the Group’s MEX-GOL and SV asset in the future.

#### *Hydrocarbon price risk*

The Group derives its revenue principally from the sale of its Ukrainian gas, condensate and LPG production. These revenues are subject to commodity price volatility and political influence. A prolonged period of low gas, condensate and LPG prices may impact the Group’s ability to maintain its long-term investment programme with a consequent effect on growth rate which in turn may impact the share price or any shareholder returns. Lower gas, condensate and LPG prices may not only decrease the Group’s revenues per unit, but may also reduce the amount of gas, condensate and LPG which the Group can produce economically, as would increases in costs associated with hydrocarbon production, such as subsoil taxes and royalties.

There has been a degree of volatility and weakness in gas prices in Ukraine during 2016, arising from the geo-political situation in Ukraine during the year, as well as reflecting a global decline in oil commodity prices. Since the deregulation of the gas supply market in Ukraine in October 2015, the market price for gas has generally correlated to the price of imported gas, which has decreased in recent months, reflecting the decline in European gas prices.

The overall economics of the Group’s key assets (being the net present value of the future cash flows from its Ukrainian projects) are far more sensitive to long term gas, condensate and LPG prices than short term price volatility. However, short term volatility does affect liquidity risk, as, in the early stage of the projects, income from production revenues is offset by capital investment.

#### *Production based taxes*

At the end of July 2014, the Ukrainian Government approved emergency fiscal measures designed to assist in alleviating the fiscal and economic pressures affecting the economy of Ukraine. These imposed significant increases to the subsoil tax rates payable on gas and condensate production, and were imposed for the period from 1 August 2014 to 31 December 2015. With effect from 1 January 2016, the subsoil tax rates relating to gas production reverted to substantially the same levels as prior to the temporary increases, but it is possible that similar significant increases to subsoil tax rates may be implemented in the future.

### *Industry risks*

The Group's ability to execute its strategy is subject to risks which are generally associated with the oil and gas industry. For example, the Group's ability to pursue and develop its projects and development programmes depends on a number of uncertainties, including the availability of capital, seasonal conditions, regulatory approvals, gas, oil, condensate and LPG prices, development costs and drilling success. As a result of these uncertainties, it is unknown whether potential drilling locations identified on proposed projects will ever be drilled or whether these or any other potential drilling locations will be able to produce gas, oil or condensate. In addition, drilling activities are subject to many risks, including the risk that commercially productive reservoirs will not be discovered. Drilling for hydrocarbons can be unprofitable, not only due to dry holes, but also as a result of productive wells that do not produce sufficiently to be economic. In addition, drilling and production operations are highly technical and complex activities and may be curtailed, delayed or cancelled as a result of a variety of factors. Furthermore, whilst the Group is committed to maintaining the highest standards of health, safety, environmental and security in its operational activities, hydrocarbon drilling and production operations carry inherent risks, which in the event of an incident may significantly affect the operational, production, financial and/or business activities of the Group.

### *Financial Markets and Economic Outlook*

The performance of the Group will be influenced by global economic conditions and, in particular, the conditions prevailing in the United Kingdom and Ukraine. The economies in these regions have been subject to volatile pressures during the period, with the global economy having experienced a long period of difficulties, and more particularly the events that have occurred in Ukraine over recent years. If these events recur, the Group may be exposed to increased counterparty risk as a result of business failures in Ukraine or elsewhere and will continue to be exposed if counterparties fail or are unable to meet their obligations to the Group. The precise nature of all the risks and uncertainties the Group faces as a result of these risks cannot be predicted and many of these are outside of the Group's control.

### *Risks relating to key personnel*

The Group has a relatively small team of executives and senior management. Whilst this is sufficient for a group of this nature, there is a dependency risk relating to the loss of key individuals. However, the Group has developed relationships with a number of technical and other professional experts and advisers, who are used to provide specialist services as required.



**Consolidated Income Statement  
for the year ended 31 December 2016**

	Note	2016 \$000	2015 \$000
Revenue	5	25,659	23,438
Cost of sales	6	(18,633)	(19,779)
<b>Gross profit</b>		<b>7,026</b>	3,659
Administrative expenses	7	(4,681)	(4,006)
Other operating gains and (losses), (net)	11	30	66
<b>Operating profit / (loss)</b>		<b>2,375</b>	(281)
Interest income		770	1,981
Finance costs	10	(185)	(26)
Other gains and (losses) (net)		(121)	(73)
<b>Profit on ordinary activities before taxation</b>		<b>2,839</b>	1,601
Income tax expense	12	(4,098)	(2,581)
<b>Loss for the year</b>		<b>(1,259)</b>	(980)
<b>Loss per share (cents)</b>			
Basic and diluted	14	(0.4c)	(0.3c)

The Notes set out below are an integral part of these consolidated financial statements.

**Consolidated Statement of Comprehensive Income  
for the year ended 31 December 2016**

	<b>2016</b>	2015
	<b>\$000</b>	\$000
Loss for the year	<b>(1,259)</b>	(980)
<b>Other comprehensive expense:</b>		
<i>Items that may be subsequently reclassified to profit or loss:</i>		
Equity – foreign currency translation	<b>(5,900)</b>	(24,767)
<i>Items that will not be subsequently reclassified to profit or loss:</i>		
Re-measurements of post-employment benefit obligations	<b>(104)</b>	(71)
<hr/>		
Total other comprehensive expense	<b>(6,004)</b>	(24,838)
<hr/>		
<b>Total comprehensive expense for the year</b>	<b>(7,263)</b>	(25,818)

The Notes set out below are an integral part of these consolidated financial statements.

**Consolidated Balance Sheet  
at 31 December 2016**

	Note	2016 \$000	2015 \$000
<b>Assets</b>			
<b>Non-current assets</b>			
Property, plant and equipment	15	21,354	18,503
Intangible assets	16	6,530	63
Corporation tax receivable		54	200
Deferred tax asset	24	11,121	14,433
		<b>39,059</b>	<b>33,199</b>
<b>Current assets</b>			
Inventories	18	1,200	1,458
Trade and other receivables	19	4,243	2,055
Other short-term investments	31	-	13,067
Cash and cash equivalents	20	19,966	19,920
		<b>25,409</b>	<b>36,500</b>
<b>Total assets</b>		<b>64,468</b>	<b>69,699</b>
<b>Liabilities</b>			
<b>Current liabilities</b>			
Trade and other payables	21	(1,435)	(1,521)
Corporation tax payable		(300)	(592)
		<b>(1,735)</b>	<b>(2,113)</b>
<b>Net current assets</b>		<b>23,674</b>	<b>34,387</b>
<b>Non-current liabilities</b>			
Provision for decommissioning	22	(1,915)	(831)
Defined benefit liability	23	(303)	(164)
Deferred tax liability		(1,187)	-
		<b>(3,405)</b>	<b>(995)</b>
<b>Total liabilities</b>		<b>(5,140)</b>	<b>(3,108)</b>
<b>Net assets</b>		<b>59,328</b>	<b>66,591</b>
<b>Equity</b>			
Called up share capital	25	28,115	28,115
Share premium account		555,090	555,090
Foreign exchange reserve		(99,684)	(93,784)
Other reserves	26	4,273	4,273
Accumulated losses		(428,466)	(427,103)
<b>Total equity</b>		<b>59,328</b>	<b>66,591</b>

The Notes set out below are an integral part of these consolidated financial statements.

**Consolidated Statement of Changes in Equity  
at 31 December 2016**

	Called up share capital \$000	Share premium account \$000	Merger reserve \$000	Capital contributions reserve \$000	Foreign exchange reserve* \$000	Accumulated losses \$000	Total equity \$000
As at 1 January 2015	28,115	555,090	(3,204)	7,477	(69,017)	(426,052)	92,409
Loss for the year	-	-	-	-	-	(980)	(980)
Other comprehensive expense							
- exchange differences	-	-	-	-	(24,767)	-	(24,767)
- re-measurements of post- employment benefit obligations	-	-	-	-	-	(71)	(71)
Total comprehensive expense	-	-	-	-	(24,767)	(1,051)	(25,818)
As at 31 December 2015	28,115	555,090	(3,204)	7,477	(93,784)	(427,103)	66,591

	Called up share capital \$000	Share premium account \$000	Merger reserve \$000	Capital contributions reserve \$000	Foreign exchange reserve* \$000	Accumulated losses \$000	Total equity \$000
As at 1 January 2016	28,115	555,090	(3,204)	7,477	(93,784)	(427,103)	66,591
Loss for the year	-	-	-	-	-	(1,259)	(1,259)
Other comprehensive expense							
- exchange differences	-	-	-	-	(5,900)	-	(5,900)
- re-measurements of post- employment benefit obligations	-	-	-	-	-	(104)	(104)
Total comprehensive expense	-	-	-	-	(5,900)	(1,363)	(7,263)
<b>As at 31 December 2016</b>	<b>28,115</b>	<b>555,090</b>	<b>(3,204)</b>	<b>7,477</b>	<b>(99,684)</b>	<b>(428,466)</b>	<b>59,328</b>

\* Predominantly as a result of exchange differences on non-monetary assets and liabilities where the subsidiaries' functional currency is not the US Dollar.

The Notes set out below are an integral part of these consolidated financial statements.

**Consolidated Cash Flow Statement  
for the year ended 31 December 2016**

	Note	2016 \$000	2015 \$000
<b>Operating activities</b>			
Cash generated from operations	28	9,971	8,795
Taxation paid		(2,219)	(679)
Interest received		809	1,956
<b>Net cash inflow from operating activities</b>		<b>8,561</b>	<b>10,072</b>
<b>Investing activities</b>			
Acquisition of subsidiary, net of cash acquired	32	(11,560)	-
Purchase of property, plant and equipment		(7,242)	(2,150)
Purchase of intangible assets		(60)	(4)
Proceeds from sale of property, plant and equipment		11	5
Other short-term investment		12,635	(13,067)
<b>Net cash outflow from investing activities</b>		<b>(6,216)</b>	<b>(15,216)</b>
<b>Financing activities</b>			
Repayment of non-interest bearing borrowings		(1,095)	-
<b>Net cash outflow from financing activities</b>		<b>(1,095)</b>	<b>-</b>
<b>Net increase / (decrease) in cash and cash equivalents</b>		<b>1,250</b>	<b>(5,144)</b>
<b>Cash and cash equivalents at beginning of year</b>		<b>19,920</b>	<b>31,836</b>
Effect of foreign exchange rate changes		(1,204)	(6,772)
<b>Cash and cash equivalents at end of year</b>	20	<b>19,966</b>	<b>19,920</b>

The Notes set out below are an integral part of these consolidated financial statements.

## Notes forming part of the financial statements

### 1. Statutory Accounts

The financial information set out above does not constitute the Company's statutory accounts for the year ended 31 December 2016 or 2015, but is derived from those accounts. The Auditor has reported on those accounts, and its reports were unqualified and did not contain statements under sections 498(2) or (3) of the Companies Act 2006.

The statutory accounts for 2016 will be delivered to the Registrar of Companies following the Company's Annual General Meeting.

While the financial information included in this preliminary announcement has been prepared in accordance with International Financial Reporting Standards as adopted by the European Union ("IFRS"), this announcement does not itself contain sufficient information to comply with IFRS. The Company expects to distribute the full financial statements that comply with IFRS in May 2017.

### 2. General Information and Operational Environment

Regal Petroleum plc (the "Company") and its subsidiaries (the "Group") is a gas, condensate and LPG production group.

Regal Petroleum plc is a company quoted on the AIM Market of London Stock Exchange plc and incorporated in England and Wales under the Companies Act 2006. The Company's registered office is at 16 Old Queen Street, London SW1H 9HP, United Kingdom and its registered number is 4462555. The principal activities of the Group and the nature of the Group's operations are set out above.

As of 31 December 2016 and 2015 the Company's immediate parent company was Energiees Management Limited, which is 100% owned by Pelidona Services Limited, which is 100% owned by Lovitia Investments Ltd, which is 100% owned by Mr V Novinskiy. Accordingly, the Company was ultimately controlled by Mr V Novinskiy.

The Group's gas, condensate and LPG extraction and production facilities are located in Ukraine. The ongoing political and economic instability in Ukraine, which commenced in late 2013, has led to a deterioration of Ukrainian State finances, volatility of financial markets, illiquidity on capital markets, higher inflation and a depreciation of the national currency against major foreign currencies and has continued in 2016, though to a lesser extent as compared to 2014–2015.

The inflation rate in Ukraine during 2016 reduced to 12% (as compared to 43% in 2015), while GDP returned to growth of 1% (after a 10% decline in 2015).

Devaluation of the Ukrainian Hryvnia during 2016 has been moderate. As at 26 April 2017, the official exchange rate of the Ukrainian Hryvnia against the US Dollar was UAH26.6/\$1.00, compared to UAH27.2/\$1.00 as at 31 December 2016 (31 December 2015: UAH24.0/\$1.00).

During 2014, the National Bank of Ukraine ("NBU") imposed currency control restrictions to support the Ukrainian Hryvnia, and these restrictions were prolonged several times during 2015 – 2016. The current restrictions remain in effect until rescinded by the NBU (with minor exceptions, including mandatory conversion of foreign currency proceeds, which are set to expire on 16 June 2017). However, during 2016, the NBU has taken certain steps to ease these currency control restrictions. In particular, the required share of foreign currency for mandatory sale was decreased from 75% to 65% from 9 June 2016 and the settlement period for export-import transactions in foreign currency was increased from 90 to 120 days from 28 July 2016. In addition, from 13 June 2016, the NBU allowed Ukrainian companies to pay dividends to non-residents with a limit of \$5 million per month.

The International Monetary Fund ("IMF") continued to support the Ukrainian Government under the four-year Extended Fund Facility Programme approved in March 2015, providing the third fourth of approximately \$1 billion in April 2017. Further disbursements of IMF tranches depend on the continued implementation of Ukrainian Government reforms, and other economic, legal and political factors.

The banking system remains fragile due to its weak level of capital, low asset quality caused by the economic situation, currency depreciation, changing regulations and other factors.

The conflict in parts of Eastern Ukraine, which started in spring 2014, has not been resolved to date. However, there has been no substantial escalation of the conflict since the signing of a ceasefire agreement in February 2015. The relationship between Ukraine and the Russian Federation remains strained.

On 1 January 2016, the agreement on the free trade area between Ukraine and the European Union came into force. Shortly thereafter, the Russian Government implemented a trading embargo on many key Ukrainian export products. In response, the Ukrainian Government implemented similar measures against Russian products.

Despite some improvements in 2016, the final resolution and the ongoing effects of the political and economic situation are difficult to predict but they may have further severe effects on the Ukrainian economy and the Group's business.

Further details of risks relating to Ukraine, can be found within the Operational Environment, Principal Risks and Uncertainties section above.

For the reasons outlined in the Operational Environment, Principal Risks and Uncertainties section, the Directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future regarded as at least 12 months after the date of signing of these financial statements. Accordingly, the going concern basis has been adopted in preparing its consolidated financial statements for the year ended 31 December 2016. The use of this basis of accounting takes into consideration the Company's and the Group's current and forecast financing position, additional details of which are provided in the "Going concern risk" section.

### **3. Accounting Policies**

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

#### **Basis of Preparation**

The Group has prepared its consolidated financial statements (the "financial statements") under International Financial Reporting Standards ("IFRSs") and interpretations issued by the IFRS Interpretations Committee ("IFRS IC"), as adopted by the European Union. The financial statements have been prepared in accordance with the Companies Act 2006 as applicable to companies using IFRS.

The financial statements are prepared on the historical cost basis as modified by the initial recognition of subsidiary acquisition and financial instruments based on fair value.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 4.

#### **New standards, amendments and interpretations adopted by the Group**

The Group has applied the following new and revised Standards and Interpretations for the first time for their annual reporting period commencing 1 January 2016. The improvements relate to the following areas:

- IAS 1, 'Presentation of financial statements', amended to clarify guidance on materiality and aggregation, the presentation of subtotals, the structure of financial statements and the disclosure of accounting policies.

- Annual improvements to IFRSs 2012-2014 Cycle, improves and amends existing standards, basis of conclusions and guidance, and includes changes to:
  - IFRS 7, 'Financial instruments: Disclosures', amended to (i) add guidance on whether an arrangement to service a financial asset which has been transferred constitutes continuing involvement, and (ii) clarify that the additional disclosure required by the amendments to IFRS 7, 'Disclosure – Offsetting financial assets and financial liabilities', is not specifically required for interim periods, unless required by IAS 34.
  - IAS 19, 'Employee benefits', amended to clarify guidance on discount rates for post-employment benefit obligations.
  - IAS 34, 'Interim financial reporting', amended to (i) clarify what is meant by "information disclosed elsewhere in the interim financial report" and (ii) require a cross reference to the location of that information.

The adoption of these amendments did not have any impact on the current period or any prior period and is not likely to affect future periods.

No other new standards, amendments and interpretations were adopted by the Group for the first time for the annual reporting period commencing 1 January 2016.

### **New standards, amendments and interpretations not yet adopted**

Certain new accounting standards and interpretations have been published that are not mandatory for 31 December 2016 reporting periods and have not been early adopted by the Group. None of these is expected to have a significant effect on the financial statements of the Group or the Company. The Group's assessment of the impact of these new standards and interpretations is set out below:

- IFRS 9, 'Financial instruments', addresses the classification, measurement and recognition of financial assets and financial liabilities. The complete version of IFRS 9 was issued in July 2014. It replaces the guidance in IAS 39 that relates to the classification and measurement of financial instruments. IFRS 9 retains but simplifies the mixed measurement model and establishes three primary measurement categories for financial assets: amortised cost, fair value through other comprehensive income ("OCI") and fair value through profit and loss. The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset. Investments in equity instruments are required to be measured at fair value through profit or loss with the irrevocable option at inception to present changes in fair value in OCI not recycling. There is now a new expected credit losses model that replaces the incurred loss impairment model used in IAS 39. For financial liabilities there were no changes to classification and measurement except for the recognition of changes in own credit risk in other comprehensive income, for liabilities designated at fair value through profit or loss. IFRS 9 relaxes the requirements for hedge effectiveness by replacing the bright line hedge effectiveness tests. It requires an economic relationship between the hedged item and hedging instrument and for the 'hedged ratio' to be the same as the one management actually use for risk management purposes. Contemporaneous documentation is still required but is different to that currently prepared under IAS 39. The standard is effective for accounting periods beginning on or after 1 January 2018. Early adoption is permitted subject to EU endorsement. The Group is yet to assess IFRS 9's full impact.
- IFRS 15, 'Revenue from contracts with customers' deals with revenue recognition and establishes principles for reporting useful information to users of financial statements about the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity's contracts with customers. Revenue is recognised when a customer obtains control of a good or service and thus has the ability to direct the use and obtain the benefits from the good or service. The standard replaces IAS 18 'Revenue' and IAS 11 'Construction contracts' and related interpretations. The standard is effective for annual periods beginning on or after 1 January 2018 and earlier application is permitted subject to EU endorsement. Implementation of IFRS 15 requires a thorough review of existing contractual agreements. The Group is assessing the impact of IFRS 15.
- IFRS 16 'Leases' replaces the current guidance in current guidance in IAS 17 and is a far-reaching change in accounting by lessees in particular. Under IAS 17, lessees were required to make a



distinction between a finance lease (on balance sheet) and an operating lease (off balance sheet). IFRS 16 now requires lessees to recognise a lease liability reflecting future lease payments and a 'right-of-use asset' for virtually all lease contracts. The IASB has included an optional exemption for certain short-term leases and leases of low-value assets; however, this exemption can only be applied by lessees. For lessors, the accounting stays almost the same. However, as the IASB has updated the guidance on the definition of a lease (as well as the guidance on the combination and separation of contracts), lessors will also be affected by the new standard. At the very least, the new accounting model for lessees is expected to impact negotiations between lessors and lessees. Under IFRS 16, a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. The standard is effective for annual periods beginning on or after 1 January 2019 with earlier application permitted if IFRS 15, 'Revenue from contracts with customers', is also applied, subject to EU endorsement. The Group is yet to assess IFRS 16's full impact.

The Group is currently assessing the full impact of the new standards, amendments and interpretations not yet adopted. The Directors do not expect that the adoption of the Standards and Interpretations listed above will have a material impact on the financial statements of the Group.

There are no other IFRSs or IFRS IC interpretations that are not yet effective that would be expected to have a material impact on the Group in the current or future reporting periods and on foreseeable future transactions.

### **Basis of Consolidation**

The consolidated financial statements incorporate the financial information of the Company and entities controlled by the Company (and its subsidiaries) made up to 31 December each year.

### **Subsidiaries**

Subsidiaries are all entities (including structured entities) over which the Group has control. The Group controls an entity when the Group is exposed to, or has rights to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are deconsolidated from the date that control ceases.

The Group applies the acquisition method to account for business combinations. The consideration transferred for the acquisition of a subsidiary is the fair value of the assets transferred, the liabilities incurred to the former owners of the acquiree and the equity interests issued by the Group. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The Group recognises any non-controlling interest in the acquiree on an acquisition-by-acquisition basis at the non-controlling interest's proportionate share of the recognised amounts of the acquiree's identifiable net assets.

Acquisition-related costs are expensed as incurred.

If the business combination is achieved in stages, the acquisition date carrying value of the acquirer's previously held equity interest in the acquiree is re-measured to fair value at the acquisition date; any gains or losses arising from such re-measurement are recognised in profit or loss.

Any contingent consideration to be transferred by the Group is recognised at fair value at the acquisition date. Subsequent changes to the fair value of the contingent consideration that is deemed to be an asset or liability is recognised in accordance with IAS 39 either in profit or loss or as a change to other comprehensive income. Contingent consideration that is classified as equity is not re-measured, and its subsequent settlement is accounted for within equity.

Inter-company transactions, balances and unrealised gains on transactions between Group companies are eliminated. Unrealised losses are also eliminated. When necessary, amounts reported by subsidiaries have been adjusted to conform with the Group's accounting policies.

## **Segment reporting**

The Group's only class of business activity is oil and gas exploration, development and production. The Group's primary operations are located in Ukraine, with its head office in the United Kingdom. The geographical segments are the basis on which the Group reports its segment information to management. Operating segments are reported in a manner consistent with the internal reporting provided to the Board of Directors.

## **Commercial Reserves**

Proved and probable oil and gas reserves are estimated quantities of commercially producible hydrocarbons which the existing geological, geophysical and engineering data show to be recoverable in future years from known reservoirs. The proved and probable reserves conform to the definition approved by the Petroleum Resources Management System.

## **Oil and Gas Development and Producing Assets**

The Group applies the successful efforts method of accounting for oil and gas assets, having regard to the requirements of IFRS 6 "Exploration for and Evaluation of Mineral Resources".

All licence acquisition, exploration and evaluation costs are initially capitalised as intangible assets in cost centres by field or by exploration area, as appropriate, pending determination of commerciality of the relevant property. Directly attributable administration costs are capitalised insofar as they relate to specific exploration activities, as are finance costs to the extent they are directly attributable to financing development projects. Pre-licence costs and general exploration costs not specific to any particular licence or prospect are expensed as incurred.

If prospects are deemed to be impaired ('unsuccessful') on completion of the evaluation, the associated costs are charged to the Income Statement. If the field is determined to be commercially viable, the attributable costs are transferred to development / producing assets within property, plant and equipment in single field cost centres.

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.

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. Gains and losses on disposals of development / producing assets are determined by comparing proceeds from sale with the appropriate portion of the net capitalised costs of the asset and are recognised in the Income Statement for the year.

## **Depreciation, Depletion and Amortisation**

All expenditure carried within each field is amortised from the commencement of commercial production on a unit of production basis, which is the ratio of gas production in the period to the estimated quantities of commercial reserves at the end of the period plus the production in the period, generally on a field by field basis. In certain circumstances, fields within a single development area may be combined for depletion purposes. Costs used in the unit of production calculation comprise the net book value of capitalised costs plus the estimated future field development costs necessary to bring the reserves into production.

## **Impairment**

At each balance sheet date, the Group reviews the carrying amount of development and producing assets to determine whether there is any indication that those assets have suffered an impairment loss. This includes exploration and appraisal costs capitalised which are assessed for impairment in accordance with IFRS 6. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss.

For development / producing assets, the recoverable amount is the greater of fair value less costs to dispose and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using an expected weighted average cost of capital. If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. Impairment losses are recognised as an expense immediately.

Should an impairment loss subsequently reverse, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is recognised as income immediately.

### **Decommissioning Provision**

Where a material liability for the removal of existing production facilities and site restoration at the end of the productive life of a field exists, a provision for decommissioning is recognised. The amount recognised is the present value of estimated future expenditure determined in accordance with local conditions and requirements. The cost of the relevant property, plant and equipment is increased with an amount equivalent to the provision and depreciated on a unit of production basis. Changes in estimates are recognised prospectively, with corresponding adjustments to the provision and the associated fixed asset. The unwinding of the discount on the decommissioning provision is included within finance costs.

### **Property, Plant and Equipment other than Oil and Gas Assets**

Property, plant and equipment other than oil and gas assets are stated at cost less accumulated depreciation and any provision for impairment. Depreciation is charged so as to write off the cost of assets on a straight-line basis over their useful lives as follows:

	<u>Useful lives in years</u>
Buildings and constructions	10 to 20 years
Machinery and equipment	2 to 5 years
Vehicles	5 years
Office and other equipment	4 to 12 years

Inventory purchased with the intention to be used in future capital investment projects is recognised as development and production assets within property, plant and equipment.

### **Inventories**

Inventories typically consist of materials, spare parts and hydrocarbons, and are stated at the lower of cost and net realisable value. Cost is determined using the first-in, first-out (FIFO) method. Net realisable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution.

### **Revenue Recognition**

Revenue from sale of goods represents amounts invoiced in respect of sales of gas, condensate and LPG exclusive of indirect taxes and excise duties and is recognised at the point of transfer of risks and rewards of ownership of the goods, normally when the goods are shipped. To the extent that revenue arises from test production during an evaluation programme, an amount is charged from intangible exploration assets to cost of sales so as to reflect a zero net margin.

Interest income is accrued on a time basis, by reference to the principal outstanding and at the effective rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.

## Foreign Currencies

The Group's consolidated financial statements and those of the Company are presented in US Dollars. The functional currency of the subsidiaries which operate in Ukraine is Ukrainian Hryvnia. The remaining entities have US Dollars as their functional currency.

The functional currency of individual companies is determined by the primary economic environment in which the entity operates, normally the one in which it primarily generates and expends cash. In preparing the financial statements of the individual companies, transactions in currencies other than the entity's functional currency ("foreign currencies") are recorded at the rates of exchange prevailing on the dates of the transactions. At each balance sheet date, monetary assets and liabilities that are denominated in foreign currencies are retranslated at the rates prevailing on the balance sheet date. 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. Non-monetary assets and liabilities carried at fair value that are denominated in foreign currencies are translated at the rates prevailing at the date when the fair value was determined. Non-monetary items which are measured in terms of historical cost in a foreign currency are not retranslated. Gains and losses arising on retranslation are included in net profit or loss for the period, except for exchange differences arising on balances which are considered long term investments where the changes in fair value are recognised directly in other comprehensive income.

On consolidation, the assets and liabilities of the Group's subsidiaries which do not use US Dollars as their functional currency are translated into US Dollars as follows:

- (a) assets and liabilities for each Balance Sheet presented are translated at the closing rate at the date of that Balance Sheet;
- (b) income and expenses for each Income Statement are translated at average monthly exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the rate on the dates of the transactions); and
- (c) all resulting exchange differences are recognised in Other Comprehensive Income.

The principal rates of exchange used for translating foreign currency balances at 31 December 2016 were \$1:UAH27.2 (2015: \$1:UAH24.0), \$1:£0.8 (2015: \$1:£0.7), \$1:€0.9 (2015: \$1:€0.9).

None of the Group's operations are considered to use the currency of a hyperinflationary economy, however this is kept under review.

## Pensions

The Group contributes to a local government pension scheme in Ukraine and defined benefit plans. The Group has no further payment obligations towards the local government pension scheme once the contributions have been paid.

Defined benefit plans define an amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors such as age, years of service and compensation.

The Group companies participate in a mandatory Ukrainian State-defined retirement benefit plan, which provides for early pension benefits for employees working in certain workplaces with hazardous and unhealthy working conditions. The Group also provides lump sum benefits upon retirement subject to certain conditions. The early pension benefit (in the form of a monthly annuity) is payable by employers only until the employee has reached the statutory retirement age (60 – for males and females). The pension scheme is based on a benefit formula which depends on each individual member's average salary, his/her total length of past service and total length of past service at specific types of workplaces ("list II" category). The employer is responsible for 100% for "list II" categories of early pensioners. The amount of attributed pension payments depends on the employees' respective lengths of service at the

Group in specific types of positions/workplaces during the last 12.5/10 years – for males and females respectively.

The liability recognised in the Balance Sheet in respect of defined benefit pension plans is the present value of the defined benefit obligation at the end of the reporting period less the fair value of plan assets. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high-quality corporate bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating to the terms of the related pension obligation. Since Ukraine has no deep market in such bonds, the market rates on government bonds are used.

The current service cost of the defined benefit plan, recognised in the Income Statement in employee benefit expense, except where included in the cost of an asset, reflects the increase in the defined benefit obligation resulting from employee service in the current year, benefit changes curtailments and settlements. Past-service costs are recognised immediately in the Income Statement.

The net interest cost is calculated by applying the discount rate to the net balance of the defined benefit obligation and the fair value of plan assets. This cost is included in employee benefit expense in the Income Statement.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are charged or credited to equity in other comprehensive income in the period in which they arise.

## **Leases**

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Rentals payable / receivable under operating leases are charged / credited to the Income Statement on a straight-line basis over the term of the relevant lease. Benefits received or given as an incentive to enter into an operating lease are also spread on a straight-line basis over the lease term.

## **Taxation**

The tax expense represents the sum of the tax currently payable and deferred tax.

Current tax, including UK corporation and overseas tax, is provided at 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.

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, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the tax profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries and associates, and interests in joint ventures, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred tax is calculated at the tax rates which are expected to apply in the period when the liability is settled or the asset is realised. Deferred tax is charged or credited in the Income Statement, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

Other taxes which include recoverable value added tax, sales tax and custom duties represent the amounts receivable or payable to local tax authorities in the countries where the Group operates.

### **Financial Instruments**

Financial assets and financial liabilities are recognised on the Group's Balance Sheet when the Group becomes a party to the contractual provisions of the instrument.

The Group classifies its financial assets as loans and receivables. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

The Group does not currently utilise derivative financial instruments.

### **Trade Receivables**

Trade receivables are amounts due from customers for goods sold in the ordinary course of business. If collection is expected in one year or less, they are classified as current assets. If not, they are presented as non-current assets.

Trade receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment.

The Group assesses at the end of each reporting period whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

For the financial assets carried at amortised cost the evidence of impairment may include indications that the debtors or a group of debtors is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation, and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

For loans and receivables category, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced and the amount of the loss is recognised in the consolidated Income Statement.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the reversal of the previously recognised impairment loss is recognised in the consolidated Income Statement.

### **Investments and loans to subsidiaries**

Investments in subsidiaries and loans issued to subsidiaries for subsequent finance of the business are stated at cost and reviewed for impairment if there are indications that the carrying value may not be recoverable.

### **Trade Payables**

Trade payables are obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Accounts payable are classified as current liabilities if payment is due within one year or less. If not, they are presented as non-current liabilities.



Trade payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

### **Equity Instruments**

Ordinary shares are classified as equity. Equity instruments issued by the Company and the Group are recorded at the proceeds received, net of direct issue costs. Any excess of the fair value of consideration received over the par value of shares issued is recorded as share premium in equity.

### **Cash and Cash Equivalents**

Cash and cash equivalents comprise cash on hand and deposits held at call with banks and other short-term highly liquid investments which are readily convertible to a known amount of cash with no significant loss of interest.

### **Other short-term investments**

Other short-term investments include current accounts and deposits held at banks, which do not meet cash and cash equivalents definition. Other short-term investments are measured initially at fair value and subsequently carried at amortised cost using the effective interest method.

## **4. Critical Accounting Estimates and Assumptions**

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions which have a risk of causing material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

### **(a) Recoverability of Development and Production Assets in Ukraine**

According to the Group's accounting policies, costs capitalised as assets are assessed for impairment at each balance sheet date. In assessing whether an impairment loss has occurred, the carrying value of the asset is compared to its recoverable amount, which IAS 36 Impairment of Assets defines as the higher of fair value less costs of disposal and value in use. Management does not believe it possible to measure fair value reliably, due to both the absence of an active market in which to sell the asset and the current political and economic climate in Ukraine. Therefore, as in previous years, management has used value in use, using a discounted cash flow model to measure its recoverable amount. The cash flows in the model are projected in real terms, i.e. they do not take into account the impact on cash flows of the estimated commodity price index during the period of projection. The discount rate is adjusted accordingly and represents a real terms discount rate.

The valuation method used for determination of recoverable value in use is based on unobservable market data, which is within Level 3 of the fair value hierarchy.

The estimate of value in use requires judgment in the following areas:

- (i) *Sales price* – The estimate used in the calculation is based on the World Bank natural gas price forecast for Europe.
- (ii) *Reserves* – Management's estimate of reserves is based on a third party reserves report which relies on a combination of technical and operational data and independent reservoir interpretations.
- (iii) *Production levels* – Management's estimate of production levels is derived from the field development plan, which in turn is related to the estimate of recoverable reserves.
- (iv) *Capital expenditures* – Management's estimate of capital expenditures is based on the assessments of internal technical experts and market data about prices for projected types and volumes of expenditures. The prices are obtained from tender offers as well as different public

sources. The part of capital expenditures which is pegged to the US Dollar is recalculated using the expected USD/UAH exchange rates based on the forecasts of independent external financial institutions. A capital expenditure allowance of \$1,000,000 per year (2015: \$1,000,000) is assumed for maintenance of development and production assets of the MEX-GOL and SV gas and condensate fields. A capital expenditure allowance of \$250,000 per year is assumed for maintenance of development and production assets of the VAS gas and condensate field.

- (v) *Discount rate* - Management applies an expected weighted average cost of capital as a discount rate, which reflects both the time value of money and its assessment of the risk associated with development and producing oil and gas assets in Ukraine. For 2017 and onwards the discount rate applied was 13.8%. The discount rates represent a real weighted average cost of capital, i.e. they do not take into account the impact of the estimated commodity price index during the period of projection.
- (vi) *Life of field, MEX-GOL and SV gas and condensate fields* - Management's estimate of recoverable amount is based on recovering reserves beyond the validity of its current production licences. Management believes that the current licences, which are due to expire in July 2024 will be extended under applicable legislation in Ukraine until the end of the economic life of the field, which is assessed to be June 2036. No application for such an extension has been made at the date of this announcement, however management considers the assumption to be reasonable based on its intention to seek such an extension in due course and that the Group is legally entitled to request an extension.
- (vii) *Life of field, VAS gas and condensate field* - Management's estimate of recoverable amount is based on recovering reserves assessed in Senergy (GB) Limited's Report as of 1 January 2016 according to which 2P reserves are recovered by 2024. However, after additional planned technical work has been undertaken (i.e. acquisition of new 3D seismic and drilling of an additional well), management plans to undertake a further reserves assessment at the end of 2017 or at the beginning of 2018.

The impairment assessment carried out at 31 December 2016 has not resulted in an impairment loss.

Further details of this assessment, including the sensitivity to the above assumptions, are set out in Note 15.

## **(b) Decommissioning**

The Group has decommissioning obligations in respect of its Ukrainian assets. The full extent to which the provision is required depends on the legal requirements at the time of decommissioning, the costs and timing of any decommissioning works and the discount rate applied to such costs.

Starting from 2013, a detailed assessment of gross decommissioning cost was undertaken on a well-by-well basis using local data on day rates and equipment costs. The discount rate applied on the decommissioning cost provision at 31 December 2016 was 6.11% (31 December 2015: 7.17%). The discount rate is calculated based on the yield to maturity of Ukrainian Government bonds denominated in the currency in which the liability is expected to be settled and with the settlement date that approximates the timing of settlement of decommissioning obligations.

The change in estimate during 2016 reflects a combination of a revision in the estimated costs (increase of \$119,000) and the discount rate applied (increase of \$191,000).

The decommissioning costs are estimated to be incurred by June 2036 on the MEX-GOL and SV gas and condensate fields, which is the end of the economic life of the fields, and by 2024 on the VAS gas and condensate field. As outlined in (a)(vi) above, management believes that the current licences for the MEX-GOL and SV gas and condensate fields, which are due to expire in July 2024, will be extended until June 2036.



### **(c) Depreciation of Development and Production Assets**

Development and production assets held in property, plant and equipment are depreciated on a unit of production basis at a rate calculated by reference to proven and probable reserves and incorporating the estimated future cost of developing and extracting those reserves. Future development costs are estimated using assumptions about the number of wells required to produce those reserves, the cost of the wells, future production facilities and operating costs, together with assumptions on oil and gas realisations, and are revised annually. The reserves estimates used are determined using estimates of gas in place, recovery factors, future hydrocarbon prices and also take into consideration the Group's latest development plan for the associated development and production asset. Additionally, as outlined in (a)(vi) above, the latest development plan and therefore the inputs used to determine the depreciation charge, assume that the current licences for the MEX-GOL and SV gas and condensate fields which are due to expire in July 2024, can be extended until June 2036.

Since there were no drilling or other works showing new information on reserves performed during 2014 - 2016 on the MEX-GOL and SV gas and condensate fields, no significant changes in the development programme for such fields and no other information available to management which may significantly change the assessment of reserves performed by ERC Equipoise Limited as of 31 December 2013, there are no sufficient reasons to revise the estimate of reserves for such fields, and management considers that the report prepared by ERC Equipoise Limited as of 31 December 2013 is still effective and should not be updated as of 31 December 2016.

Project outcomes and recommendations by P.D.F. Limited, reprocessing and reinterpretation of seismic data to be performed in 2017, and updates on new and existing well performance may provide grounds for revising the approach to further development of the MEX-GOL and SV fields, and as a consequence provide grounds for undertaking a new assessment of the Group's reserves at such fields at the end of 2017.

Hydrocarbon reserves of the VAS field were assessed by Senergy (GB) Limited as of 1 January 2016. Since there were no drilling or other works on the VAS field showing new information on reserves performed in 2016 and there is no other information available to management which may significantly change the assessment of reserves performed by Senergy (GB) Limited, there are no sufficient reasons to revise this estimate and management considers that the report prepared by Senergy (GB) Limited as of 1 January 2016 is still effective and should not be updated as of 31 December 2016. However, after additional planned technical work has been undertaken (i.e. acquisition of new 3D seismic and drilling of an additional well), management plans to undertake a further reserves assessment at the end of 2017 or at the beginning of 2018.

### **(d) Recoverability of materials inventory**

The majority of the Group's materials inventory balance comprises items to be used in the Ukraine drilling programme. Where there is uncertainty whether the materials will be realised through the drilling programme, or through sale, the materials are recorded at selling price, less any associated costs. Where materials inventory is intended for sale, management uses current market rates to estimate the recoverable amount through sale.

### **(e) Recognition of deferred tax asset**

The recognition of deferred tax assets is based upon whether it is more likely than not that sufficient and suitable taxable profits will be available in the future against which the reversal of temporary differences can be deducted. This requires judgment for forecasting future profits.

Further details of the deferred tax assets recognised can be found in Note 24.

### **(f) Functional currency**

An entity's functional currency is the currency of the primary economic environment in which the entity operates. If a foreign entity conducts significant amounts of business in more than one underlying

currency, management's judgment will be required to determine the functional currency in which financial results are measured with the greatest degree of relevance and reliability.

## 5. Segmental Information

In line with the Group's internal reporting framework and management structure, the key strategic and operating decisions are made by the Board of Directors, who review internal monthly management reports, budget and forecast information as part of this process. Accordingly, the Board of Directors is deemed to be the Chief Operating Decision Maker within the Group.

The Group's only class of business activity is oil and gas exploration, development and production. The Group's operations are located in Ukraine, with its head office in the United Kingdom. These geographical regions are the basis on which the Group reports its segment information. The segment results as presented represent operating profit / (loss) before depreciation, amortisation and impairment loss.

	<b>Ukraine</b>	<b>United Kingdom</b>	<b>Total</b>
	<b>2016</b>	<b>2016</b>	<b>2016</b>
	<b>\$000</b>	<b>\$000</b>	<b>\$000</b>
<b>Revenue</b>			
Gas sales	16,529	-	16,529
Condensate sales	5,696	-	5,696
Liquefied Petroleum Gas sales	3,434	-	3,434
Total revenue	25,659	-	25,659
<b>Segment result</b>	13,773	(2,257)	11,516
<b>Depreciation and amortisation</b>			<b>(9,141)</b>
<b>Operating profit</b>			<b>2,375</b>
<b>Segment assets</b>	50,960	13,508	64,468
<b>Capital additions*</b>	13,899	-	13,899

There are no inter-segment sales within the Group and all products are sold in the geographical region in which they are produced. Gas sales to the Group's two largest customers in 2016 amounted to \$2,874,000 and \$2,821,000 (2015: gas sales to two largest customers amounted to \$2,894,000 and \$2,469,000).

	Ukraine 2015 \$000	United Kingdom 2015 \$000	Total 2015 \$000
Revenue			
Gas sales	14,784	-	14,784
Condensate sales	5,622	-	5,622
Liquefied Petroleum Gas sales	3,032	-	3,032
Total revenue	23,438	-	23,438
Segment result	9,247	(1,858)	7,389
Depreciation and amortisation			(7,670)
Operating loss			(281)
Segment assets	52,340	17,359	69,699
Capital additions*	2,279	-	2,279

\*Comprises additions to property, plant and equipment (Note 15)

## 6. Cost of Sales

	2016 \$000	2015 \$000
Depreciation of development and producing asset (Note 15)	8,620	7,599
Production taxes	4,401	8,083
Cost of purchased gas	1,712	1,171
Staff costs (Note 9)	1,402	1,222
Cost of inventories recognised as an expense	760	661
Amortisation of mineral reserves (Note 16)	417	-
Rent expenses (Note 27)	93	45
Geological services	40	43
Other expenses	1,188	955
	<b>18,633</b>	<b>19,779</b>

## 7. Administrative Expenses

	<b>2016</b>	2015
	<b>\$000</b>	\$000
Staff costs (Note 9)	<b>2,580</b>	2,423
Consultancy fees	<b>1,063</b>	613
Auditors' remuneration	<b>281</b>	259
Rent expenses (Note 27)	<b>279</b>	302
Depreciation of other assets (Note 15)	<b>68</b>	59
Amortisation of other intangible assets	<b>36</b>	12
Other expenses	<b>374</b>	338
	<b>4,681</b>	4,006

	<b>2016</b>	2015
	<b>\$000</b>	\$000
Audit of the Company and subsidiaries	<b>209</b>	179
Audit related assurances services – interim review	<b>50</b>	52
<b>Total assurance services</b>	<b>259</b>	231
Tax compliance services	<b>22</b>	28
<b>Total non-audit services</b>	<b>22</b>	28
<b>Total audit and other services</b>	<b>281</b>	259

All amounts shown as auditor's remuneration in 2016 and 2015 were payable to the Group auditors, PricewaterhouseCoopers LLP and other member firms of PricewaterhouseCoopers.

## 8. Remuneration of Directors

	<b>2016</b>	2015
	<b>\$000</b>	\$000
Directors' emoluments	694	764

The emoluments of the individual Directors were as follows:

	<b>Total emoluments 2016 \$000</b>	Total emoluments 2015 \$000
<b>Executive Directors:</b>		
Keith Henry	337	382
Sergei Glazunov	121	129
<hr/>		
<b>Non-executive Directors:</b>		
Alastair Graham	74	69
Adrian Coates	61	69
Alexey Pertin	61	69
Yulia Kirianova	40	-
Alexey Timofeyev	-	46
	<b>694</b>	<b>764</b>

Yuliia Kirianova was appointed as a Non-Executive Director in May 2016 and is a nominee of the Company's majority shareholder, Energiees Management Limited. She is paid £45,000 per year paid quarterly.

The emoluments include base salary and fees. According to the register of Directors' interests, no rights to subscribe for shares in or debentures of the Group companies were granted to any of the Directors or their immediate families during the financial year, and there were no outstanding options to Directors.

## 9. Staff Numbers and Costs

The average monthly number of employees on a full time equivalent basis during the year (including Executive Directors) was as follows:

	<b>Number of employees</b>	
	<b>2016</b>	2015
<b>Group</b>		
Management / operational	113	101
Administrative support	58	52
	<b>171</b>	<b>153</b>

The aggregate staff costs of these employees were as follows:

	<b>2016 \$000</b>	2015 \$000
Wages and salaries	3,435	3,054
Other pension costs	499	534
Social security costs	48	57
	<b>3,982</b>	<b>3,645</b>

The increase in the average monthly number of employees is due to an increase in employees upon the acquisition of PEP.

## 10. Finance Costs

	<b>2016 \$000</b>	2015 \$000
Loss on early settlement of non-interest bearing loan	103	-
Unwinding of discount on decommissioning provision (Note 22)	82	26
	<b>185</b>	<b>26</b>

At the date of the acquisition of PEP, a non-interest bearing loan was owed by PEP to the Smart Holding Group, which under the terms of acquisition, was required to be repaid by 31 December 2016. Following the completion of the acquisition of PEP, this non-interest bearing loan was repaid and a corresponding loss of \$103,000 on early settlement of the non-interest bearing loan was recognised.

#### 11. Other operating gains and (losses), (net)

	<b>2016</b>	2015
	<b>\$000</b>	\$000
Gain on sales of current assets	<b>91</b>	165
Rental income	<b>22</b>	15
Income /(loss) from write off / recovery of non-current assets	<b>14</b>	(333)
Reversal of impairment of VAT receivables and related balances	-	225
Agency remuneration	<b>(29)</b>	-
Loss from write off of doubtful debts	<b>(64)</b>	-
Other operating expense (net)	<b>(4)</b>	(6)
	<b>30</b>	66

Other operating gains and losses (net) for the year ended 31 December 2016 include a loss from the write off of doubtful debts of \$64,000 related to an allowance of trade receivable for gas sold in August 2016. This allowance was made in accordance with the accounting policy of the Group.

Other operating gains and losses (net) for the year ended 31 December 2016 also include agency remuneration of \$29,000, which was paid to a related party under an agency agreement for gas sales to third parties during the period from September - December 2016.

In addition, other operating gains and losses (net) for the year ended 31 December 2016 include income of \$22,000 related to the rent of equipment to a related party.

Other operating gains and losses (net) for the year ended 31 December 2015 include income from the reversal of the provision on VAT receivables of \$335,000 related to Regal Petroleum Corporation (Ukraine) Limited. Since the VAT receivable mostly relates to capital expenditures, in prior periods it was uncertain that the amount provided for would be offset against VAT payable on future sales. In 2015, the provision for VAT receivable was reversed as the Group was able to offset its VAT receivable balance against VAT payable.

In addition, other operating gains and losses (net) for the year ended 31 December 2015 include impairment of VAT receivables of \$110,000 related to another Group company, Regal Petroleum Corporation (Ukraine) Limited. This amount was written off as uncollectable due to the inability of the Group to offset this amount against VAT payable or utilise it in any other way.

Also, other operating gains and losses (net) for the year ended 31 December 2015 include expenses of \$333,000 relating to the write-off of preparatory works in respect of wells SV-67 and MEX-122 located on the SV and MEX-GOL gas and condensate fields. The decision to abort these drilling projects was made in 2015 following reconsideration of the chances of success of these wells, and the associated costs were written off in the 2015 year.

## 12. Income tax expense

a) Income tax expense:

	2016 \$000	2015 \$000
<i>Current tax</i>		
Overseas – current year	1,977	1,279
Overseas – prior year	(38)	15
<i>Deferred tax (Note 24)</i>		
UK - current year	312	3,658
UK - prior year	1,847	(2,371)
Income tax expense	4,098	2,581

b) Factors affecting tax charge for the year:

The tax assessed for the year is different than the blended rate of corporation tax in the UK of 20%. The expense / (income) for the year can be reconciled to the profit / (loss) as per the Income Statement as follows:

	2016 \$000	2015 \$000
Profit on ordinary activities before taxation	2,838	1,601
Tax charge at UK tax rate of 20% (2015: 20.25%)	568	324
<b>Tax effects of:</b>		
Lower foreign corporate tax rates in Ukraine (18%)	(18)	1
Disallowed expenses and non-taxable income	(1,962)	(9,891)
Losses not recognised as deferred tax assets	3,212	12,922
Adjustment for reduction in UK corporate tax rate	492	1,628
Realisation of previously unrecognised deferred tax assets on provision for unused vacations	(3)	(47)
Adjustments in respect of prior periods	1,809	(2,356)
Tax expense for the year	4,098	2,581

## 13. Loss for the Financial Year

The Company has taken advantage of the exemption allowed under section 408 of the Companies Act 2006 and has not presented its own Income Statement in these financial statements. The Group loss for the year includes a Parent Company loss after tax of \$15,616,000 for the year ended 31 December 2016. For the year ended 31 December 2015, the Group loss included a Parent Company loss after tax of \$24,637,000.

## 14. Earnings / (Loss) per Share

The calculation of basic profit or loss per ordinary share has been based on the profit or loss for the year and 320,637,836 (2015: 320,637,836) ordinary shares, being the weighted average number of shares in issue for the year. There are no dilutive instruments.

## 15. Property, Plant and Equipment

Group	2016			2015		
	Development and Production assets Ukraine \$000	Other fixed assets \$000	Total \$000	Development and Production assets Ukraine \$000	Other fixed assets \$000	Total \$000
<b>Cost</b>						
At beginning of year	99,254	719	99,973	148,254	984	149,238
Additions	5,973	229	6,202	2,199	80	2,279
Additions due to acquisition of subsidiary	7,610	87	7,697	-	-	-
Change in decommissioning provision	359	-	359	640	-	640
Disposals	(153)	(17)	(170)	(857)	(21)	(878)
Exchange differences	(12,553)	(116)	(12,669)	(50,982)	(324)	(51,306)
At end of year	100,490	902	101,392	99,254	719	99,973
<b>Accumulated depreciation and impairment</b>						
At beginning of year	81,114	356	81,470	113,514	457	113,971
Charge for year	8,620	68	8,688	7,599	59	7,658
Disposals	(1)	(11)	(12)	(430)	(15)	(445)
Exchange differences	(10,084)	(24)	(10,108)	(39,569)	(145)	(39,714)
At end of year	79,649	389	80,038	81,114	356	81,470
<b>Net book value at beginning of year</b>	<b>18,140</b>	<b>363</b>	<b>18,503</b>	<b>34,740</b>	<b>527</b>	<b>35,267</b>
<b>Net book value at end of year</b>	<b>20,841</b>	<b>513</b>	<b>21,354</b>	<b>18,140</b>	<b>363</b>	<b>18,503</b>

In accordance with the Group's accounting policies, oil and gas development and producing assets are tested for impairment at each balance sheet date. In assessing whether an impairment loss has occurred, the carrying amount of the asset is compared to the value in use. The Group estimates value in use of its development and producing assets using a discounted cash flow model.

The impairment assessment carried out at 31 December 2016 has not resulted in an impairment loss.

The calculation of value in use is most sensitive to the following assumptions, the bases of which are set out in Note 4(a):

- (i) *Commodity prices* – the model assumes gas prices of \$231/Mm<sup>3</sup> (UAH6,300/Mm<sup>3</sup>) in 2017 increasing to \$248/Mm<sup>3</sup> (UAH6,746/Mm<sup>3</sup>) during 2018 – 2024 for the VAS gas and condensate fields and to \$291/Mm<sup>3</sup> (UAH7,920/Mm<sup>3</sup>) during 2018 – 2033 for the MEX-GOL and SV gas and condensate fields. The prices were estimated based on World Bank natural gas price forecast for Europe.
- (ii) *Discount rate* - reflects the current market assessment of the time value of money and risks specific to each field. The discount rate has been determined as the weighted average cost of capital based on observable inputs and inputs from third party financial analysts. For 2017 and onwards the discount rate applied was 13.8% (2016: 15%). The discount rates represent a real weighted average cost of capital, i.e. they do not take into account the impact of the estimated commodity price index during the period of projection.
- (iii) *Production levels and Reserves, MEX-GOL and SV fields* – production levels at the MEX-GOL and SV gas and condensate fields are based on the data included in the third party reserves report performed by ERC Equipoise Limited as of 31 December 2013. This report



includes estimated production volumes, including from new wells, over the remaining useful life of the MEX-GOL and SV gas and condensate fields in Ukraine. The estimated production is based on the Group's current development programme, which includes the drilling of six new wells (2015: six new wells), and the workover of existing currently non-producing wells, which will recover the same reserves with lower capital expenditure. As there was no drilling in 2014 - 2015, the reserves report prepared by ERC Equipoise Limited as of 31 December 2013 is still effective and was not updated as of 31 December 2016.

- (iv) *Production levels and Reserves, VAS field* – production levels at the VAS gas and condensate field are based on the data included in the third party reserves report performed by Senergy (GB) Limited as of 1 January 2016. The NPV, discounted at 15.38%, of the 2P Reserves for the VAS field is estimated in such report at UAH343.9 million. The report is consistent with the Group's current development plans for the VAS field, which comprise continued production from the existing three wells and the drilling of one additional well to recover the 2P and 3P Reserves.
- (v) *Production taxes* - management assumed production tax rates of 29% for gas and 45% for condensate extracted from deposits up to depths of 5,000 metres and 14% for gas and 21% for condensate extracted from deposits deeper than 5,000 metres. These rates are based on the Ukrainian Tax Code that became effective from 1 January 2016.
- (vi) *Capital expenditures, MEX-GOL and SV gas and condensate fields* - management assumed that most capital expenditures are to be incurred during 2017 – 2021. A capital expenditure allowance of \$1,000,000 per year is assumed for maintenance of the development and producing assets of the MEX-GOL and SV gas and condensate fields.
- (vii) *Capital expenditures, VAS gas and condensate fields* - management assumed that most capital expenditures are to be incurred during 2017 and 2018. A capital expenditure allowance of \$250,000 per year is assumed for maintenance of the development and producing assets of the VAS gas and condensate field.
- (viii) *Life of field, MEX-GOL and SV gas and condensate fields* - the current licences, which are due to expire in July 2024, can be extended under applicable legislation in Ukraine until the end of the economic life of the field, which is assessed to be June 2036 on the basis of the reserves report by ERC Equipoise Limited. No application for such an extension has been made at the date of this announcement, but management consider the assumption to be reasonable based on their intention to seek such an extension in due course and that the Group is legally entitled to request an extension. However, if the extension were not granted, it would result in a further reduction of \$17,140,000 in the recoverable amount.
- (ix) *Life of field, VAS gas and condensate field* – according to reserves report by Senergy (GB) Limited, the economic life of the VAS field is limited to 2024. However, after additional planned technical work has been undertaken (i.e. acquisition of 3D and drilling of an additional well), management plans to undertake a further reserves assessment at the end of 2017 or at the beginning of 2018.

The Group's discounted cash flow model for the MEX-GOL and SV gas and condensate fields in Ukrainian Hryvnia, flexed for sensitivities, produced the following results:

	<b>Recoverable amount</b>	<b>Net book value</b>	<b>Headroom</b>
	<b>\$000</b>	<b>\$000</b>	<b>\$000</b>
31 December 2016	30,521	15,112	15,409

Sensitivities:

1. \$25/Mm <sup>3</sup> reduction in gas price	22,438	15,112	7,326
2. \$25/Mm <sup>3</sup> increase in gas price	38,586	15,112	23,474
3. Breakeven gas price \$205/Mm <sup>3</sup>	15,171	15,112	59
4. Breakeven flow rates 39 Mm <sup>3</sup> /day for all new wells	15,218	15,112	106
5. Breakeven discount rate 22.6%	15,115	15,112	3
6. Natural gas subsoil taxes go up to 50%/25% from 2018	17,734	15,112	2,622
7. No payment for entrance to the Ukrainian gas system from 1 April 2017 - \$12.47/Mm <sup>3</sup>	35,376	15,112	20,264

The Group's discounted cash flow model for the VAS gas and condensate fields in Ukrainian Hryvnia, flexed for sensitivities, produced the following results:

	<b>Recoverable amount</b>	<b>Net book value*</b>	<b>Headroom / (Shortfall)</b>
	<b>\$000</b>	<b>\$000</b>	<b>\$000</b>
31 December 2016	13,104	12,772	332

Sensitivities:

1. \$25/Mm <sup>3</sup> reduction in gas price	11,004	12,772	(1,768)
2. \$25/Mm <sup>3</sup> increase in gas price	15,259	12,772	2,487
3. Breakeven gas price \$231/Mm <sup>3</sup>	12,228	12,772	(544)
4. Breakeven flow rates 46 Mm <sup>3</sup> /day for all new wells	12,489	12,772	(283)
5. Breakeven discount rate 15%	12,541	12,772	(231)
6. Natural gas subsoil taxes go up to 50%/25% from 2018	8,510	12,772	(4,262)
7. No payment for entrance to the Ukrainian gas system from 1 April 2017 - \$12.47/Mm <sup>3</sup>	14,505	12,772	1,733

\*Net book value of the VAS asset is derived from property, plant and equipment, mineral reserve rights and other intangible assets (Note 16).

According to the results of the impairment tests performed, there is no impairment of the Group's development and production assets at 31 December 2016.

## 16. Intangible assets

Group	2016			2015		
	Mineral reserve rights \$000	Other intangible assets \$000	Total \$000	Mineral reserve rights \$000	Other intangible assets \$000	Total \$000
<b>Cost</b>						
At beginning of year	-	94	94	-	78	78
Additions	-	71	71	-	37	37
Additions due to acquisition of subsidiary	7,479	4	7,483	-	-	-
Disposals	-	(9)	(9)	-	-	-
Exchange differences	(647)	(16)	(663)	-	(21)	(21)
At end of year	6,832	144	6,976	-	94	94
<b>Accumulated amortisation and impairment</b>						
At beginning of year	-	31	31	-	30	30
Charge for year	417	36	453	-	12	12
Disposals	-	(9)	(9)	-	-	-
Exchange differences	(24)	(5)	(29)	-	(11)	(11)
At end of year	393	53	446	-	31	31
<b>Net book value at beginning of year</b>	-	63	63	-	48	48
<b>Net book value at end of year</b>	6,439	91	6,530	-	63	63

Intangible assets consist mainly of the hydrocarbon production licence relating to the VAS gas and condensate field which is owned by PEP. The Group amortises this intangible asset using the straight-line method over the term of the licence until 2024.

In accordance with the Group's accounting policies, intangible assets are tested for impairment at each balance sheet date as part of the impairment testing of the Group's oil and gas development and producing assets. Pursuant to the results of the impairment tests performed, there is no impairment of the Group's intangible assets at 31 December 2016 (Note 15).

## 17. Investments and loans to subsidiaries

	Shares in subsidiary undertakings \$000	Loans to subsidiary undertakings \$000	Total \$000
<b>Company</b>			
<b>Cost</b>			
At 1 January 2015	17,279	67,598	84,877
Additions including accrued interest	-	6,557	6,557
Impairment of loans to subsidiary	-	(19,027)	(19,027)
Exchange differences	-	(6,817)	(6,817)
At 31 December 2015	17,279	48,311	65,590
<b>Cost</b>			
At 1 January 2016	17,279	48,311	65,590
Additions including accrued interest	-	5,384	5,384
Impairment of loans to subsidiary	-	(16,209)	(16,209)
Disposals	-	-	-
Exchange differences	-	(1,817)	(1,817)
<b>At 31 December 2016</b>	<b>17,279</b>	<b>35,669</b>	<b>52,948</b>

In accordance with the Company's accounting policies, loans to subsidiaries have been reviewed to assess recoverability. At 31 December 2016, the Company recognised the impairment of \$16,209,000 against the carrying value of loans to reflect the significant decrease in the carrying value of the Ukrainian assets due to devaluation of Ukrainian Hryvnia (2015: \$19,027,000).

### Subsidiary undertakings

At 31 December 2016, the Company's subsidiary undertakings, all of which are included in the consolidated financial statements, were:

	Registered address	Country of incorporation	Country of operation	Principal activity	% of shares held
Regal Petroleum Corporation Limited	26 New Street, St Helier, Jersey Jersey JE2 3RA	Jersey	Ukraine	Oil & Natural Gas Extraction	100%
Regal Petroleum Corporation (Ukraine) Limited	162 Shevchenko Str., Yakhnyky Village, Lokhvytsya District, Poltava Region, 37212	Ukraine	Ukraine	Service Company	100%
Refin Limited	162 Shevchenko Str., Yakhnyky Village, Lokhvytsya District, Poltava Region, 37212	Ukraine	Ukraine	Service Company	100%
LLC Prom-Enerho Produkt	3 Klemanska Str., Kiev, 02081	Ukraine	Ukraine	Oil & Natural Gas Extraction	100%
Regal Petroleum (Jersey) Limited	26 New Street, St Helier, Jersey Jersey JE2 3RA	Jersey	United Kingdom	Holding Company	100%
Regal Group Services Limited	16 Old Queen Street, London, SW1H 9HP	United Kingdom	United Kingdom	Service Company	100%

The Parent Company, Regal Petroleum plc, holds direct interests in 100% of the share capital of Regal Petroleum (Jersey) Limited and Regal Group Services Limited, with all other companies owned indirectly by the Parent Company. Regal Petroleum Corporation Limited is controlled through its 100% ownership by Regal Petroleum (Jersey) Limited. Regal Petroleum Corporation (Ukraine) Limited is controlled

through its 100% ownership by Regal Petroleum (Jersey) Limited and Regal Group Services Limited, Refin Limited is controlled through its 100% ownership by Regal Petroleum (Jersey) Limited and Regal Petroleum Corporation (Ukraine) Limited and LLC Prom-Enerho Produkt is controlled through its 100% ownership by Regal Petroleum Corporation (Ukraine) Limited.

Regal Group Services Limited, company number 5252958, has adopted the subsidiary audit exemption allowed under section 479A of the Companies Act 2006 for the year ended 31 December 2016.

## 18. Inventories

	<b>Group</b>	
	<b>2016</b>	2015
	<b>\$000</b>	\$000
<b>Current</b>		
Materials	<b>1,150</b>	1,337
Condensate stock	<b>50</b>	121
	<b>1,200</b>	1,458

There was no write down of materials inventory as at 31 December 2016 (2015: nil).

## 19. Trade and Other Receivables

	<b>Group</b>		<b>Company</b>	
	<b>2016</b>	2015	<b>2016</b>	2015
	<b>\$000</b>	\$000	<b>\$000</b>	\$000
Trade receivables	<b>2,203</b>	1,005	-	-
Prepayments and accrued income	<b>1,300</b>	193	<b>29</b>	47
VAT receivable	<b>543</b>	616	<b>50</b>	29
Other receivables	<b>197</b>	241	<b>460</b>	450
	<b>4,243</b>	2,055	<b>539</b>	526

Due to the short-term nature of the current trade and other receivables, their carrying amount is assumed to be the same as their fair value. All trade receivables except provided for are considered to be of high credit quality.

An impairment provision of \$64,000 was charged against trade and other receivables during 2016 (2015: \$nil).

At 31 December 2016, the Group's total trade receivables amounted to \$2,203,000 and 100% were denominated in Ukrainian Hryvnia (31 December 2015: \$1,005,000 and 100% were denominated in Ukrainian Hryvnia). Further description of financial receivables is disclosed in Note 29.

Current VAT receivable in respect of the Group includes \$543,000 (2015: \$616,000) relating to capital expenditure in Ukraine which is expected to be recovered via an offset against VAT payable on future sales in that country. The Group expects to offset the total amount of VAT receivable at 31 December 2016 during the 2017 year, and therefore no VAT receivable was included within non-current trade and other receivables.

## 20. Cash and Cash Equivalents

	<b>Group</b>		<b>Company</b>	
	<b>2016</b>	2015	<b>2016</b>	2015
	<b>\$000</b>	\$000	<b>\$000</b>	\$000
Cash at bank and on hand	<b>19,966</b>	19,920	<b>9,645</b>	11,913
	<b>19,966</b>	19,920	<b>9,645</b>	11,913

Cash at bank earns interest at floating rates based on daily bank deposit rates. Short-term deposits are made for varying periods depending on the immediate cash requirements of the Group and earn interest at the respective short-term deposit rates. The terms and conditions upon which the Group's short-term deposits are made allow immediate access to all cash deposits, with no significant loss of interest.

The credit quality of cash and cash equivalents balances may be summarised based on Moody's ratings as follows at 31 December 2016:

	Cash at bank and on hand 2016 \$000	Short- term deposits 2016 \$000	Total 2016 \$000	Cash at bank and on hand 2015 \$000	Short- term deposits 2015 \$000	Total 2015 \$000
A- to A+ rated	9,975	-	9,975	12,255	-	12,255
Unrated	9,991	-	9,991	7,665	-	7,665
	<b>19,966</b>	<b>-</b>	<b>19,966</b>	<b>19,920</b>	<b>-</b>	<b>19,920</b>

## 21. Trade and Other Payables

	Group		Company	
	2016 \$000	2015 \$000	2016 \$000	2015 \$000
Accruals and deferred income	764	553	149	183
Taxation and social security	651	773	-	-
Advances received	20	193	-	-
Trade payables	-	2	-	-
	<b>1,435</b>	<b>1,521</b>	<b>149</b>	<b>183</b>

The carrying amounts of trade and other payables are assumed to be the same as their fair values, due to their short-term nature. Description of financial payables is disclosed in Note 29.

## 22. Provision for Decommissioning

	2016 \$000	2015 \$000
<b>Group</b>		
At beginning of year	831	255
Amounts provided	49	42
Amounts provided due to acquisition of subsidiary	816	-
Unwinding of discount (Note 10)	82	26
Change in estimate	310	598
Exchange differences	(173)	(90)
At end of year	<b>1,915</b>	<b>831</b>

The provision for decommissioning is based on the net present value of the Group's estimated liability for the removal of the Ukraine production facilities and well site restoration at the end of production life.

Amounts provided as a result of the acquisition of PEP amounted to \$816,000, reflecting a provision for decommissioning of existing wells, pipeline and the gas production plant at the VAS gas and condensate field.

The change in estimate during 2016 reflects a combination of a revision in the estimated costs (increase of \$119,000) and the discount rate applied (increase of \$191,000). The discount rate applied on the decommissioning cost provision at 31 December 2016 was 6.11% (31 December 2015: 7.17%). The decrease of the discount rate at 31 December 2016 came as a result of a Ukrainian Eurobonds' yield

decrease and a respective decrease of Country Risk Premium. These costs are expected to be incurred by 2036 on the MEX-GOL and SV gas and condensate fields (2015: by 2036), and by 2024 on the VAS gas and condensate field, although if the costs on the MEX-GOL and SV gas and condensate fields were to be incurred at the current expiry of the production licences in 2024, the provision for decommissioning at 31 December 2016 would be \$2,219,000 (31 December 2015: \$1,908,000).

The principal assumptions used are as follows:

	31 December 2016	31 December 2015
Discount rate, %	6.11%	7.17%
Average cost of restoration per well, \$000	184	164

The sensitivity of the restoration provision to changes in the principal assumptions is presented below:

	31 December 2016	31 December 2015
	\$000	\$000
Discount rate (increase)/decrease by 1%	(240)/284	(144)/176
Change in average cost of restoration increase/ (decrease) by 10%	192/(192)	83/(83)

### 23. Defined benefit liability

	2016	2015
	\$000	\$000
<b>Group</b>		
At the beginning of the year	164	120
Amounts provided due to subsidiary acquisition	26	-
Income statement charge included in operating profit	42	22
Re-measurements	104	70
Benefits paid	(2)	-
Exchange differences	(31)	(48)
At end of year	303	164

The principle assumptions used in calculation of the retirement benefit obligations are as follows:

	2016	2015
Nominal discount rate, %	12.00%	13.08%
Nominal salary increase, %	25.00%	25.00%

The sensitivity of the defined benefit obligation to changes in the principal assumptions is presented below:

	2016	2015
	\$000	\$000
Nominal discount rate increase/decrease by 1%	(37)/44	(16)/19
Nominal salary increase increase/decrease by 1%	12/(22)	3/(5)

## 24. Deferred Tax

	2016 \$000	2015 \$000
<b>Deferred tax asset recognised on tax losses – Company and Group</b>		
At beginning of year	4,470	7,861
Charged to Income Statement - current year	(753)	(3,391)
<b>At end of year</b>	<b>3,717</b>	<b>4,470</b>
	2016 \$000	2015 \$000
<b>Deferred tax asset recognised relating to development and production asset – Group</b>		
At beginning of year	9,963	12,552
Credited / (charged) to Income Statement - current year	250	(267)
(Charged) / credited to Income Statement – prior year	(1,847)	2,371
Effect of exchange difference	(962)	(4,693)
<b>At end of year</b>	<b>7,404</b>	<b>9,963</b>
	2016 \$000	2015 \$000
<b>Deferred tax liability recognised relating to development and production asset – Group</b>		
At beginning of year	-	-
Acquisition of subsidiary	(1,499)	-
Charged to Income Statement - current year	191	-
Effect of exchange difference	121	-
<b>At end of year</b>	<b>(1,187)</b>	<b>-</b>

At 31 December 2016, the Group recognised a deferred tax asset of \$3,717,000 in relation to UK tax losses carried forward (31 December 2015: \$4,470,000). There was a further \$85 million (31 December 2015: \$73 million) of unrecognised UK tax losses carried forward for which no deferred tax asset has been recognised. These losses can be carried forward indefinitely, subject to certain rules regarding capital transactions and changes in the trade of the Company. The Directors consider it appropriate to recognise deferred tax assets resulting from accumulated tax losses at 31 December 2016 to the extent that it is probable that there will be sufficient future taxable profits.

The deferred tax asset relating to the Group's development and production assets at 31 December 2016 of \$7,404,000 (31 December 2015: \$9,963,000) was recognised on the tax effect of the temporary differences between the carrying value of the Group's development and production asset at the MEX-GOL and SV gas and condensate fields, and its tax base. This is deemed recoverable on the projected future profits generated by the Group's operations in Ukraine. The forecast profits are based on the current field development plan at the MEX-GOL and SV gas and condensate fields, and are determined using data from the same cash flow model which was used for impairment review of such development and production asset, as outlined in Note 15. Based on these projections, the deferred tax asset recognised will be recovered by 2023. However, should future field development not result in additional production, only \$1 million of the \$7 million deferred tax recognised would be recoverable based on forecast profits available from the Group's existing wells.

The deferred tax liability relating to the Group's development and production assets at 31 December 2016 of \$1,187,000 was recognised on the tax effect of the temporary differences between the carrying value of the Group's development and production asset at the VAS gas and condensate fields, and its tax base.



The impact of the UK losses surrendered to the Ukrainian operating subsidiary in relation to losses was \$4,649,000 for 2015. There were no UK losses surrendered for the year ended 31 December 2016.

Losses accumulated in a Ukrainian subsidiary service company of UAH2,448,430,023 (\$90,046,074) at 31 December 2016 and UAH2,061,576,860 (\$85,897,000) at 31 December 2015 mainly originated as foreign exchange differences on inter-company loans and for which no deferred tax asset was recognised as this subsidiary is not expected to have taxable profits to utilise these losses in the future.

### UK Corporation tax change

A change to the UK corporation tax rate was announced in the Chancellor's Budget on 16 March 2016. The change announced is to reduce the main tax rate to 17% from 1 April 2020. Changes to reduce the UK corporation tax rate to 19% from 1 April 2017 and to 18% from 1 April 2020 were substantively enacted on 26 October 2015. Changes to reduce the UK corporation tax rate to 17% from 1 April 2020 were substantively enacted on 6 September 2016 and the effect of these changes are included in consolidated financial statement.

### 25. Called Up Share Capital

	Number	2016 \$000	Number	2015 \$000
<b>Allotted, called up and fully paid</b>				
Opening balance at 1 January	320,637,836	28,115	320,637,836	28,115
Issued during the year	-	-	-	-
Closing balance at 31 December	<b>320,637,836</b>	<b>28,115</b>	320,637,836	28,115

There are no restrictions over ordinary shares issued.

### 26. Other Reserves

Other reserves, the movements in which are shown in the statements of changes in equity, comprise the following:

#### Capital contributions reserve

The capital contributions reserve is non-distributable and represents the value of equity invested in subsidiary entities prior to the Company listing.

#### Merger reserve

The merger reserve represents the difference between the nominal value of shares acquired by the Company and those issued to acquire subsidiary undertakings. This balance relates wholly to the acquisition of Regal Petroleum (Jersey) Limited and that company's acquisition of Regal Petroleum Corporation Limited during 2002.

#### Foreign exchange reserve

Exchange reserve movement for the year attributable to currency fluctuations. This balance predominantly represents the result of exchange differences on non-monetary assets and liabilities where the subsidiaries' functional currency is not the US Dollar.

### 27. Operating Lease Arrangements

#### The Group as Lessee

	Group		Company	
	2016 \$000	2015 \$000	2016 \$000	2015 \$000
Minimum lease payments under operating leases recognised as an expense for the year	<b>372</b>	347	<b>145</b>	181

Minimum lease payments under operating leases recognised as an expense for the year ended 31 December 2016 are mainly represented by the rentals of office properties in Ukraine and the UK of \$279,000 (2015: \$302,000) and the leases of land and well SV-6 of \$93,000 (2015: \$45,000).

At the balance sheet date, the Group had outstanding off-balance sheet commitments for future minimum lease payments under non-cancellable operating leases which fall due as follows:

	<b>Land and buildings</b>	
	<b>2016</b>	2015
<b>Group and Company</b>	<b>\$000</b>	\$000
Amounts payable due:		
- Within one year	<b>97</b>	136
	<b>97</b>	136

Operating lease payments represent rentals payable by the Group for office properties, which were negotiated and fixed for an average of one year.

## 28. Reconciliation of Operating Profit / (Loss) to Operating Cash Flow

	<b>2016</b>	2015
	<b>\$000</b>	\$000
<b>Group</b>		
Operating profit / (loss)	<b>2,375</b>	(281)
Depreciation, amortisation and impairment charges	<b>9,141</b>	7,670
Gain on sales of current assets, net	<b>(91)</b>	(165)
Loss from write off of doubtful debts	<b>64</b>	-
(Gain)/ loss from write off of non-current assets	<b>(14)</b>	333
Reversal of impairment of VAT receivables and related balances	<b>-</b>	(225)
Movement in provisions	<b>(20)</b>	(50)
Decrease in inventory	<b>90</b>	45
(Increase) / decrease in receivables	<b>(1,730)</b>	1,260
Decrease in payables	<b>156</b>	208
<b>Cash generated from operations</b>	<b>9,971</b>	8,795
	<b>2016</b>	2015
	<b>\$000</b>	\$000
<b>Company</b>		
Operating loss	<b>(18,430)</b>	(20,863)
Movement in provisions (including impairment of subsidiary loans)	<b>16,209</b>	19,027
Increase in receivables	<b>(13)</b>	(112)
Decrease in payables	<b>(34)</b>	(77)
<b>Cash used in operations</b>	<b>(2,268)</b>	(2,025)

## 29. Financial Instruments

### Capital Risk Management

The Group's objectives when managing capital are to safeguard the Group's and the Company's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital.

The Group defines its capital as equity. The primary source of the Group's liquidity has been cash generated from operations.

In order to maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets.

The capital structure of the Group consists of equity attributable to the equity holders of the parent, comprising issued share capital, share premium, reserves and retained deficit.

There are no capital requirements imposed on the Group.

The Group's financial instruments comprise cash and cash equivalents and various items such as debtors and creditors that arise directly from its operations. The Group has bank accounts denominated in British Pounds, US Dollars, Euros, Canadian Dollars and Ukrainian Hryvnia. The Group does not have any borrowings. The main future risks arising from the Group's financial instruments are currently currency risk, interest rate risk, liquidity risk and credit risk.

The Group's financial assets and financial liabilities, measured at amortised cost, which approximates their fair value comprise the following:

### Financial Assets

	<b>2016</b>	2015
	<b>\$000</b>	\$000
<b>Group</b>		
Cash and cash equivalents	<b>19,966</b>	19,920
Other short-term investments	-	13,067
Trade and other receivables	<b>2,224</b>	1,074
	<b>22,190</b>	34,061
	<b>2016</b>	2015
	<b>\$000</b>	\$000
<b>Company</b>		
Cash and cash equivalents	<b>9,645</b>	11,913
Trade and other receivables	<b>442</b>	398
	<b>10,087</b>	12,311

### Financial Liabilities

	<b>2016</b>	2015
	<b>\$000</b>	\$000
<b>Group</b>		
Trade and other payables	-	2
Accruals	<b>345</b>	242
	<b>345</b>	244
	<b>2016</b>	2015
	<b>\$000</b>	\$000
<b>Company</b>		
Trade and other payables	-	-
Accruals	<b>149</b>	183
	<b>149</b>	183

All assets and liabilities of the Group where fair value is disclosed are level 2 in the fair value hierarchy and valued using the current cost accounting technique.

### Currency Risk

The functional currencies of the Group's entities are US Dollars and Ukrainian Hryvnia. The following analysis of net monetary assets and liabilities shows the Group's currency exposures. Exposures comprise the monetary assets and liabilities of the Group that are not denominated in the functional currency of the relevant entity.

<b>Currency</b>	<b>2016 \$000</b>	2015 \$000
British Pounds	<b>316</b>	424
Euros	<b>4</b>	96
Canadian Dollars	<b>2</b>	2
US Dollars	<b>-</b>	(40)
Net monetary assets less liabilities	<b>322</b>	482

### Foreign Currency Sensitivity Analysis

The following table presents sensitivities of profit and loss to reasonably possible changes in exchange rates applied at the end of the reporting period, with all other variables held constant:

	<b>At 31 December 2016 After tax impact on profit or loss \$000</b>	At 31 December 2015 After tax impact on profit or loss \$000
GBP strengthening by 30% (2015: 30%)	<b>95</b>	127
EUR strengthening by 30% (2015: 30%)	<b>1</b>	29

A positive number above indicates a decrease in loss / increase in profit where the indicated currency strengthens against the functional currency. For a weakening of the indicated currency against the functional currency, there would be an equal and opposite impact on the loss / profit, and the balances above are shown negative. A negative number above indicates an increase in loss / decrease in profit where the indicated currency strengthens against the functional currency. For a weakening of the indicated currency against the functional currency, there would be an equal and opposite impact on the loss / profit, and the balances above are shown positive. The Group holds currencies to match the currencies of future capital and operational expenditure.

### Interest Rate Risk Management

The Group is not exposed to interest rate risk on financial liabilities as none of the entities in the Group have any external borrowings. The Group does not use interest rate forward contracts and interest rate swap contracts as part of its strategy.

The Group is exposed to interest rate risk on financial assets as entities in the Group hold money market deposits at floating interest rates. The risk is managed by fixing interest rates for a period of time when indications exist that interest rates may move adversely.

The Group's exposure to interest rates on financial assets and financial liabilities are detailed in the liquidity risk section below.

### Interest Rate Sensitivity Analysis

The sensitivity analysis below has been determined based on exposure to interest rates for non-derivative instruments at the balance sheet date. A 0.5% increase or decrease is used when reporting interest rate risk internally to key management personnel and represents management's assessment of a reasonably possible change in interest rates.

If interest rates earned on money market deposits had been 0.5% higher / lower and all other variables were held constant, the Group's:

- loss for the year ended 31 December 2016 would increase by \$87,000 in the event of 0.5% higher interest rates and decrease by \$87,000 in the event of 0.5% lower interest rates (2015: increase of profit for the year ended 31 December 2015 by \$92,000 in the event of 0.5% higher interest rates and

decrease by \$92,000 in the event of 0.5% lower interest rates). This is mainly attributable to the Group's exposure to interest rates on its money market deposits; and

- other equity reserves would not be affected (2015: not affected).

Interest payable on the Group's liabilities would have an immaterial effect on the profit or loss for the year.

### **Liquidity Risk**

The Group's objective throughout the year has been to ensure continuity of funding. Operations have primarily been financed through revenue from Ukrainian operations.

Details of the Group's cash management policy are explained in Note 20.

Liquidity risk for the Group is further detailed under the "Going concern risk" section above.

### **Credit Risk**

Credit risk principally arises in respect of the Group's cash balance. In the UK, where \$10.0 million of the overall cash is held (31 December 2015: \$12.3 million), the Group only deposits cash surpluses with major banks of high quality credit standing (Note 20). The remaining balance of \$10.0 million was held in Ukraine (31 December 2015: \$7.6 million). In June 2016 Standard & Poor's affirmed Ukraine's sovereign credit rating of "B-/B", Outlook Stable. There is no international credit rating information available for the specific banks in Ukraine where the Group currently holds its cash and cash equivalents.

The significant devaluation of the Ukrainian Hryvnia has resulted in the National Bank of Ukraine, among other measures, imposing comprehensive restrictions on the processing of client payments by banks, on the purchase of foreign currency on the inter-bank market and on the remittance of funds outside Ukraine. These restrictions, and the many other economic issues in Ukraine, have put great strain on the Ukrainian banking system, with increasing risks in the capital strength, liquidity and creditworthiness of a large number of Ukrainian banks, and very high rates in the wholesale and overnight markets. In addition, there have been significant deposit outflows from the banking system and widespread restructuring of bank clients' maturing liabilities. Furthermore, as a result of recommendations from the International Monetary Fund, significant reforms to the Ukrainian banking sector are being implemented, which are intended to strengthen the capitalisation of the Ukrainian banks.

In light of the deterioration in the banking sector in Ukraine, the Group is taking steps to diversify its banking arrangements between a number of banks in Ukraine. These measures are designed to spread the risks associated with each bank's creditworthiness, but the Ukrainian banking sector remains weakly capitalised and so the risks associated with the banks in Ukraine remain significant, including in relation to the banks with which the Group operates bank accounts.

None of the Group's trade receivables are past due or impaired. All trade receivables are considered to be of high credit quality.

## Interest Rate Risk Profile of Financial Assets

The Group had the following cash and cash equivalent and other short-term investments balances which are included in financial assets as at 31 December 2016 with an exposure to interest rate risk:

Currency	Total 2016 \$000	Floating rate financial assets 2016 \$000	Fixed rate financial assets 2016 \$000	Total 2015 \$000	Floating rate financial assets 2015 \$000	Fixed rate financial assets 2015 \$000
Canadian Dollars	2	2	-	2	2	-
Euros	4	4	-	91	38	53
British Pounds	471	471	-	596	596	-
Ukrainian Hryvnia	9,992	-	9,992	20,679	-	20,679
US Dollars	9,497	9,497	-	11,619	11,619	-
	<b>19,966</b>	<b>9,974</b>	<b>9,992</b>	<b>32,987</b>	<b>12,255</b>	<b>20,732</b>

Cash deposits included in the above balances comprise short term deposits.

## Interest Rate Risk Profile of Financial Liabilities

The Group had no interest bearing financial liabilities at the year end (2015: \$nil).

## Maturity of Financial Liabilities

The maturity profile of financial liabilities, on an undiscounted basis, is as follows:

	2016 \$000	2015 \$000
<b>Group</b>		
In one year or less	345	244
	<b>345</b>	<b>244</b>
	2016 \$000	2015 \$000
<b>Company</b>		
In one year or less	149	183
	<b>149</b>	<b>183</b>

## Borrowing Facilities

The Group did not have any borrowing facilities available to it at the year end (2015: \$nil).

## Fair Value of Financial Assets and Liabilities

The fair value of all financial instruments is not materially different from the book value.

## 30. Capital Commitments

Amounts contracted in relation to the Group's 2016 investment programme in the MEX-GOL and SV gas and condensate fields in Ukraine, but not provided for in the financial statements at 31 December 2016, were \$1,212,000 (2015: \$319,000). As of 31 December 2016, there were no amounts contracted in relation to the Group's 2016 investment programme in the VAS gas and condensate field in Ukraine.

## 31. Related Party Disclosures

Key management personnel of the Group are considered to comprise only the Directors. Details of Directors' remuneration are disclosed in Note 8.

During the year, Group companies entered into the following transactions with related parties who are not members of the Group:

	<b>2016</b>	2015
	<b>\$000</b>	\$000
Sale of goods / services	<b>65</b>	469
Purchase of goods / services	<b>230</b>	120
Amounts owed by related parties	-	57
Amounts owed to related parties	<b>20</b>	9

All related party transactions were with subsidiaries of the ultimate Parent Company, and primarily relate to rental of office facilities and a vehicle and the sale of equipment. The amounts outstanding were unsecured and will be settled in cash.

As of 31 December 2016, the Company's immediate parent company was Energiees Management Limited, which is 100% owned by Pelidona Services Limited, which is 100% owned by Lovitia Investments Ltd, which is 100% owned by Mr V Novinskiy. Accordingly, the Company was ultimately controlled by Mr V Novinskiy.

The Group operates bank accounts in Ukraine with a related party bank, Unex Bank, which is ultimately controlled by Mr V Novinskiy. There were the following transactions and balances with Unex Bank during the year:

	<b>2016</b>	2015
	<b>\$000</b>	\$000
Interest income	<b>365</b>	1,829
Bank charges	<b>1</b>	3
Other short-term investments	-	13,067

At 31 December 2016, no other short-term investments were held with a related party bank, Unex Bank (31 December 2015: \$13,067,000).

Prior to acquisition by the Group, PEP, an entity under common control, was a 100% subsidiary of LLC Interregional Pellet Company, which is a company under the control of Mr V Novinskiy and consequently a related party of the Group. Further details of acquisition are disclosed in Note 32.

At the date of this announcement, none of the Company's controlling parties prepares consolidated financial statements available for public use.

### **32. Acquisition of subsidiary**

On 4 July 2016, the Group acquired a 100% shareholding interest in PEP for a cash consideration of UAH305,000,000 (\$12,284,000 as at that date), with all such consideration paid entirely from the Group's cash balances held in Unex Bank. PEP is a Ukrainian incorporated company, which holds a production licence over the VAS gas and condensate field, which also includes the VVD prospect, located in the Dnieper-Donets basin in the north-east of Ukraine. The production licence was granted in August 2012 with a duration of 20 years, and is in respect of a 100% interest in the licence.

Prior to acquisition by the Group, PEP was a 100% subsidiary of LLC Interregional Pellet Company, a company also under the control of Mr V Novinskiy meaning that the acquisition is considered to be an acquisition of a company under common control and therefore not within the scope of IFRS 3, "Business combinations". Accordingly, the Directors are required to determine an appropriate accounting policy and have elected to apply the acquisition method as set out in IFRS 3.

In accordance with IFRS 3, the Group has undertaken an assessment of the fair value of the assets and liabilities recognised as a result of the acquisition, which are as follows:

	<b>Fair value</b>
	<b>\$000</b>
Cash and cash equivalents	724
Trade and other receivables	177
Inventories	60
Property, plant and equipment	7,697
Mineral reserves	7,479
Intangible assets	4
Trade and other payables	(340)
Corporation tax payable	(164)
Non-Interest bearing loans and borrowings	(1,012)
Deferred tax liability	(1,499)
Provision for decommissioning	(816)
Defined benefit liability	(26)
<b>Net assets acquired</b>	<b>12,284</b>
<b>Consideration paid – cash from realisation of short-term investment</b>	<b>12,284</b>
<b>Difference between net assets acquired and consideration paid</b>	<b>-</b>

Acquisition related costs of \$472,000 have been charged to administrative expenses in the income statement for the year ended 31 December 2016.

As a result of the valuation of the VAS asset at the date of acquisition, the Group recognised Mineral reserves as intangible assets of \$7,479,000, the value of property, plant and equipment increased to \$7,697,000 and the respective deferred tax liability increased to \$1,499,000.

The revenue included in the income statement contributed by PEP since acquisition on 4 July 2016 was \$3,681,000. PEP also contributed profit after tax of \$637,000 over the same period.

Had PEP been consolidated from 1 January 2016, the consolidated income statement would show pro-forma revenue of \$29,304,000 and a loss for the year of \$589,000.

### **33. Post Balance Sheet Events**

Temporary capital controls, imposed by the National Bank of Ukraine (“NBU”) in 2014, remain in place in an attempt by the Ukrainian Government to safeguard the economy and protect foreign exchange reserves in the short term.

On 23 February 2017, the NBU introduced changes to the currency control restrictions. In particular, representative offices registered in Ukraine, may purchase foreign currency if they have less than \$100,000 (or equivalent) on their current and/or deposit account in all banks (previously the threshold amount was \$25,000).

The currency restrictions have significantly affected the Group's ability to purchase foreign currency and to remit funds outside Ukraine, which has affected the Group's treasury and currency management.

The Group has recently entered into an agreement with NJSC Ukrnafta, the partially State-owned oil and gas producer, relating to the SV-2 well, which is a suspended well owned by NJSC Ukrnafta located within the Group's SV licence area. Under the agreement, the Group will carry out a workover of the well and, if successful, operate, produce and sell the gas and condensate from the well under an equal net profit sharing arrangement with NJSC Ukrnafta. Planning for this workover is underway and it is anticipated that work will commence in the second quarter of 2017.