# Gulfsands Petroleum plc
# Annual report and accounts
# For the year ended 31 December 2009

**Registered number:** **05302880 (England & Wales)**

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**Description**

Gulfsands Petroleum plc is an independent oil and gas exploration and production company, incorporated in the United Kingdom, whose shares are traded on the Alternative Investment Market ("AIM") of the London Stock Exchange (symbol : GPX).

The Group's major focus is on the Middle East, where it has oil exploration and development projects in the Syrian Arab Republic and upstream and midstream oil and gas business development activities in Iraq. Gulfsands also produces oil and gas from a portfolio of properties in the USA, offshore Gulf of Mexico.

**Annual General Meeting**

The Annual General Meeting of Shareholders will take place at 11 am on Thursday 27 May 2010 at the offices of Buchanan Communications, 45 Moorfields, London, EC2Y 9AE. All shareholders are welcome to attend. If unable to attend, shareholders are encouraged to fill out the form of proxy and return it to our registrars, Capita IRG.

## HIGHLIGHTS

### Financial

- Revenues up by 57% to $84.4 million (2008: $53.6 million)
- Profit after tax of $27.8 million vs. loss of $5.4 million (restated) in 2008
- Cash from operating activities up by 117% to $43.5 million (2008: $20.0 million (restated))
- Loss of $14.2 million in US business before intra-group interest after impairment charge of $6.4 million (2008 : loss of $0.3 million after impairment charge of $1.7 million (restated))
- Free cash balances at year-end of $57.6 million (2008 : $36.8 million)

### Operations

- Group 2P working interest reserves up by 25% to 50.7 mmboe (2008: 40.4 mmboe)
- 2P working interest reserves in Syria up by 31% to 46.0 mmbbls (2008: 35.2 mmbbls)
- Working interest production in Syria up by 70% during 2009 to 8,500 bopd at year-end
- Khurbet East early production facility upgraded to 18,000 bopd capacity
- Commercial development approval obtained for Yousefieh field

### Outlook

- Four well exploration campaign in Syria in 2010
- 500km2 of 3D seismic to be acquired on Block 26
- Two exploration wells and additional 3D seismic to be acquired in Tunisia
- US business to be sold when market conditions favourable

## Vision

Our vision is to become one of the pre-eminent independent exploration and production companies in the Middle East & North Africa region, and to be viewed as a preferred operator and partner.

## Strategy

Our long-term objective is to deliver significant growth in shareholder value via the exploration and development of oil and gas fields in the Middle East and North Africa ("MENA") region.

We intend to achieve this primarily by investment in early stage exploration and appraisal opportunities but do not rule out the acquisition of more mature assets if the opportunity exists for us to add material value.

Where possible we prefer to act as operator, as this allows us to retain control of project execution risk and financial exposure, but will invest in non-operated situations if we are confident that our own interests are sufficiently protected and the operator is capable of managing the business just as well, if not better, than us.

Our first priority is to maximise the potential in Syria, in particular to capture the available upside in Block 26 before the final expiry of the exploration period in August 2012. We will also be looking for ways to add further assets in Syria, capitalising on the strength of the relationships that we have forged over the last decade.

We have ambitions to build a significant business in Iraq in the mid to longer term, where we believe that the opportunities for smaller E&P companies will increase in coming years. Our focus will remain outside Kurdistan until we are satisfied that the issues concerning the exploitation of Kurdistan's hydrocarbon potential have been satisfactorily resolved. We will seek to participate in projects that offer significant upside and can deliver returns that are commensurate with the challenges presented by those projects, and we will assess our risk exposure and capital commitment both on an individual project basis and for the country as a whole.

We will seek attractive opportunities to enter other countries in the region, but will scrutinise such opportunities carefully to ensure they represent compelling justification for investment.

We intend to dispose of our US business as and when we assess the time is right to do so. In the meantime we will pursue a strategy of selective reinvestment in this business in order to be in a position to commence a disposal process when market conditions are favourable.

Finally, we aim to follow a relatively conservative financing policy, ensuring that any leverage is kept at prudent levels and that we have the financial resources available to finance necessary investment even in adverse economic conditions.

## Business Strengths

We consider our key strengths in achieving our strategy to be:

- The relationships that we have formed in Syria and elsewhere in the MENA region, primarily via Mahdi Sajjad, our President

- The reputation for efficient cost effective operation that we have built up in Syria
- The balanced and complementary skill set and expertise of our executive team
- The enthusiasm, competence and dedication of our staff

## Key Performance Indicators

Key Performance Indicators ("KPIs") provide a means of measuring our progress in delivering our strategic objectives and creating shareholder value.

### Financial Key Perfomance Indicators

| KPI | | 2009 | 2008 | 2007 |
|---|---|---|---|---|
| **Working Interest Production** | mmboe | 2.7 | 1.2 | 0.8 |
| | growth % | 126% | 42% | 8% |
| The key driver of cash generation. The working interest measure is preferred to entitlement production because the latter is impacted by the terms of production sharing agreements so is not representative of underlying operational performance | | | | |
| **Production Cost per Barrel (working interest)** | $/bbl | 6.9 | 13.5 | 18.5 |
| The key measure of operating efficiency. Calculated as cost of sales excluding depreciation, impairment charges, decommissioning costs and hurricane repair costs, divided by working interest production | | | | |
| **Cash flow available for Exploration** | $ MM | 22.6 | -1.0 | -5.4 |
| Calculated as net cash provided by operating activities, less net cash used in investing activities but excluding exploration and evaluation expenditure. This gives a measure of the cash flow available to the Group for exploration after investment in the development of its existing reserves, purchase of other fixed assets and payment of decommissioning costs. | | | | |
| **Earnings per Share** | US cents | 23.1 | -4.7 | -1.1 |
| The standard measure of profit attributable to shareholders calculated on a diluted basis assuming the exercise of options | | | | |
| **Underlying Reserves Growth** | % | 32% | 8% | 304% |
| The growth in proved and probable working interest reserves over the year after adding back production in that year | | | | |

### Non-financial Key Perfomance Indicators

| KPI | | 2009 | 2008 | 2007 |
|---|---|---|---|---|
| **Lost Time Incidents** | Number | Nil | Nil | Nil |
| The number of incidents during the year which resulted in a loss of working time | | | | |

**Chairman's Statement**

Dear Shareholder,

It gives me much pleasure to report on another year of solid progress towards our goal of becoming a leading independent exploration and production company in the Middle East and North Africa ("MENA") region. A number of key achievements are worthy of mention.

Proven & probable working interest reserves increased by 25% to more than 50 mmboe, all of which increase related to our assets in Syria.

We ended the year with unrestricted cash balances of $ 57.6 million and no debt. This strong financial position has been crucial to our ability to continue to function unimpeded by the very difficult financial circumstances of the past eighteen months and leaves the Group well placed to fund our plans for development and exploration in Syria from our own resources.

The "investment profile" of the Group improved significantly during the course of the year. We are now covered actively by research analysts at eight independent brokerage firms. Liquidity in our shares has improved considerably, with an approximate average daily volume of 420,000 shares during the first two months of 2010. More than 200 institutional investors are now represented on our share register, while our previous Chief Executive and Chief Financial Officer have ceased to be substantial shareholders following sales of their shares.

We made a number of key management appointments during the year, the foremost being that of Khalid Almogharbel, a Syrian citizen with many years experience working for Schlumberger in the Middle East, as our Operations Manager for Syria and as General Manager of our joint venture with the Syrian Petroleum Company.

I would like to take this opportunity to thank the Syrian Government, the Syrian Petroleum Company and Syria's General Petroleum Corporation for the exemplary level of support and cooperation we continue to receive from them. As but one example, the increase in the capacity of the early production facility in Khurbet East to 18,000 bopd was achieved at minimal cost and within a timeframe of months that would not have been possible without such assistance. Your Board regards the strong relationship we enjoy with our Syrian partners as one of the Group's most important intangible assets.

I would also like to welcome Sinochem, our new Chinese partners in Block 26, and we look forward to a long and fruitful collaboration.

Against this backdrop we approach the coming year with confidence. Our overriding priority is to complete the full field development of the Khurbet East field but we are also proceeding "full ahead" in our pursuit of the remaining exploration potential of Block 26.

As this Report goes to press, there are modestly encouraging signs of a pending improvement in relations between Syria and the United States. Any progress in this direction can only be to the Company's advantage.

Our efforts to secure additional exploration opportunities in a new country in the MENA region have recently borne fruit in the form of the farm-in to two exploration licences in Tunisia, where we believe there is significant potential.

Finally, we continue to believe that our longstanding efforts in Iraq will begin to show tangible results as the obstacles to development of that country's massive oil and gas resources have at last begun to be removed. We are cautiously optimistic of being able to report positive progress in this regard during the year.

Yours sincerely,

Andrew West

Chairman

**29 March 2010**

**2010 Objectives**

Syria

- Bring Yousefieh into commercial production
- Install 22km pipeline to SPC delivery point to replace trucking operation
- Construct 2000 $m^3$ fixed roof oil storage tank at the EPF
- Manage initial phases of Central Production Facility EPC contract
- Drill 4 exploration wells and 5 production wells on Block 26
- Achieve average production of 18,000 bopd gross (9,000 bopd WI)
- Secure an additional exploration or development license in Syria

USA

- Restore production to pre-hurricane levels by year-end
- Identify additional potential reserves via drilling and work-overs
- Commence the process of divestment

Tunisia

- Complete farm-in to Chorbane and Kerkouane permits
- Acquire 3D seismic and drill two exploration wells

Business Development

- Progress Maysan project or another oil & gas exploitation project in Iraq
- Actively review opportunities to farm-in to or acquire E&P assets in elsewhere in the MENA region

## CHIEF EXECUTIVE'S REPORT

2009 was a very successful year for the Group as a whole. In Syria, the focus was primarily on increasing oil production and reserves through the drilling of the Khurbet East oil field. This resulted in a 70% increase in production over the year to approximately 17,000 bopd (gross) by year-end, exceeding our year-end target of 16,000 bopd (gross). 2P oil reserves at Khurbet East have increased by 28% to 38 mmbbls and Yousefieh 2P oil reserves have increased 42% to 8 mmbbls. After production of 2.3 mmbbls in 2009, we now have 46 mmbbls of 2P oil reserves in Syria compared with 35 mmbbls a year ago (all reserves numbers on a working interest basis).

This production performance from Syria has delivered the Group its first profit after tax of $27.8 million and has placed us in a strong financial position with net cash of $57.6 million at year-end. Assuming no unexpected surprises, we anticipate being able to meet all capital expenditure requirements in Syria and the USA throughout the forthcoming year from operating cash-flow.

### Syria

At Khurbet East, seven wells were drilled, three of which were delineation wells and four were producers. The upgrading of processing facilities at the early production facility (EPF) from 10,000 to 18,000 barrels of oil per day (bopd) capacity was completed safely in July, and tenders were issued in October for a new central production facility (CPF) with a capacity of 50,000 barrels of fluid per day (bfpd), the contract for which is expected to be awarded imminently. In addition, two appraisal wells on the Yousefieh oil field were successfully completed. Both wells flowed oil to surface on test, and approval by the Syrian Government to develop the field was received in January 2010.

A large three dimensional (3D) seismic survey of approximately 850 km² of good quality data was acquired in the first six months of the year on time, safely and within budget. In combination with seismic data acquired from a previous adjacent 3D survey, a total of approximately 1,100 km² of data has now been processed and a preliminary interpretation completed. Four exploration prospects and two leads have been identified. The exploration well on the first prospect (Zaman-1), completed in February 2010, discovered only a small non-commercial oil pool. Drilling of the second exploration well, Hanoon-1, is nearly complete and the results are anticipated in April.

A second smaller 3D seismic survey was acquired on a sole risk basis in November over the Taramish anticlinal structure located in the northeast corner of Block 26. The processed data was delivered in March 2010 and interpretation is underway.

In order to accommodate our expanding workforce in Syria, now numbering over 70 people (including contract staff), we have moved to new offices located just outside the city of Damascus and strengthened our management team with appointment of Khalid Almogharbel as Operations Manager.

A new HSE policy and management system was adopted by the Group during the year and a HSE Manager appointed to the Damascus office. I am pleased to report that Gulfsands' excellent safety record has been maintained in 2009 with no lost-time injuries being reported during the year, nor indeed since operations began in 2006.

USA

Results for the year in the USA were very disappointing from a number of perspectives. The delay in repair of third party infrastructure has been significantly more protracted than anticipated following damage incurred by Hurricanes Gustav and Ike in 2008. At the time of writing our working interest production is approximately 1,700 boepd, significantly below budget due to a number of facilities still not being fully operational. In addition, gas sales prices fell from an average of $9.4/mcf in 2008 to an average of $3.9/mcf in 2009. As a result of these and other difficulties, the US business made a loss for the year of $14.2 million before intra-group interest (2008 as restated: $0.3 million). However, we anticipate the US will make a positive contribution during 2010 assuming a reasonably trouble free hurricane season and oil and gas prices remaining at or above current levels. This will include some investment expenditure with possibly two exploration wells in addition to a number of work-overs.

The USA assets are now non-core to the Group and we intend to commence the process of divestment during 2010.

New Business Initiatives

The focus for the Group continues to be the active exploitation of potential in Block 26 in Syria. However, we are also looking to expand our footprint in Syria and are proactively seeking new opportunities.

In Iraq, participation in the Maysan Gas Project remains an objective for the Group. During the year, a thorough technical and commercial audit and review of the project, by third parties, was undertaken that has reinforced our desire to pursue the project and finalise negotiations as soon as possible. We are also looking for opportunities in Iraq that would allow direct participation in enhanced oil recovery projects that, if appropriately structured, have the potential to deliver a relatively attractive rate of return.

We have expanded our search for new business opportunities to the Middle East and North Africa region generally and recently announced a farm-in to two exploration permits in Tunisia, one onshore and one offshore, held by AUDAX Resources. This will involve us in the acquisition of 3D seismic and the drilling of two exploration wells during the course of 2010.

Objectives for 2010

We believe that a significant quantity of oil remains undiscovered in Block 26 and requires an active exploration programme to capture this potential, prior to the end of the exploration period in August 2012. We plan to drill four exploration wells in 2010 on newly defined prospects and to acquire another large 3D seismic survey in order to delineate future exploration targets.

Production for 2010 is anticipated to average approximately 18,000 bopd delivered to the export pipeline via a newly built 22 km pipeline and storage facility at the EPF. We aim to bring Yousefieh into production by mid-year.

Development drilling will continue at the Khurbet East field with four development wells and at the Yousefieh Field with one well, in preparation to ramp up oil production through the CPF once this has been brought into operation.

Outlook

2010 and 2011 will continue to be capital intensive years in Block 26 as we continue to explore aggressively and construct and commission the CPF, but all costs are anticipated to be met from cash flow. At the date of this statement, we are in a strong financial position with a cash balance of over $70 million, no debt and a forecast surplus cash flow for 2010. Thereafter, surplus cash-flows generated in Syria will be re-invested in new projects, both within Syria and elsewhere in the Middle East.

We believe that a solid foundation for the Group has now been achieved in Syria that enables Gulfsands to look to the future with great excitement and optimism and to continue to build an ever stronger E&P company by focusing on our strengths and capitalising on the opportunities that lie before us.

Richard Malcolm

**Chief Executive Officer**

29 March 2010

## Questions & Answers

### SYRIA

**How dependent is Syria on its oil & gas industry?**

Oil revenues provide a significant portion of Syria's foreign exchange earnings, and forecasting future oil revenues is a critical part of the country's economic planning process. It has been estimated that by 2020 Syria will require oil production levels of approximately 600,000 bopd to meet the country's economic growth plans, so it is important that Syria achieves exploration success to arrest declining levels of current production and ensure the country has the oil it requires to meet its economic objectives.

**What proportion of Syria's oil production is produced by international oil companies?**

It is estimated that international oil companies account for approximately 60% of the country's current production of approximately 380,000 bopd.

**How do you see Syria's oil & gas industry developing over the next few years?**

Syria is about to embark on a new round of oil field redevelopments and recently offered a number of blocks for exploration by international companies. Therefore I would expect oil and gas exploration expenditures to increase significantly in the coming years while the country also looks to bring a number of discovered gas resources into production to meet a substantial increase in local demand.

**What role can Gulfsands expect to play in that development?**

Gulfsands is keenly interested in exploring the oil potential of Block 26 in north east Syria where we have had a presence since 2003 and we have a well funded and ambitious programme underway at the moment. At the same time, we are working as quickly as we can to increase the production from our two discoveries at Khurbet East and Yousefieh in Block 26. We are also evaluating opportunities to acquire additional exploration acreage and other field redevelopment opportunities.

**How clear cut is the legal framework in Syria in terms of title to oil & gas properties?**

Syria has a well deserved reputation for honouring its production sharing contractual obligations and we are very confident that our own excellent experience in this regard will continue.

**How much more potential is there in Block 26?**

That's what we would like to know too! We expect to devote a lot of resources to exploration over the next two years and we are optimistic that we will find additional discoveries in Block 26 before our production sharing contract expires in August 2012.

**Is Gulfsands looking for new projects in Syria outside of Block 26?**

It is widely known that we are looking for opportunities to expand our portfolio with oil and gas projects outside of Block 26. We are constantly evaluating farm-in and acquisition opportunities as well as participating in new blocks offered by the government but so far we have not found additional projects that meet our objectives.

**Do you see the US sanctions regime being lifted any time soon?**

Recently there have been a number of positive developments in this regard with a number of previously imposed restrictions being removed already and the appointment of a new US ambassador to Syria. We are optimistic that, with the relationship between Syria and the US continuing to improve all the time, we will see the removal of further restrictions on trade between the two countries in the not distant future.

**Does Syria have a role to play in exporting oil & gas from Iraq when the latter's production expands as promised?**

Iraq's plans for expanding its production of oil and gas will bring significant infrastructure challenges. Iraq recognises that Syria could have a significant role to play in transporting large volumes of both oil and gas to the Mediterranean while also offering Syria access to important additional supplies of oil and gas to supplement Syria's own production.

**IRAQ**

**How do you view the situation in Iraq following the recent elections?**

The recent elections represent an important milestone in Iraq's move to become the Middle East's newest democracy. We are optimistic that once the new government is installed we will see an acceleration in the pace of progress to approve and develop energy projects in general and specifically those on which we have been working for some time.

**Are you confident the Maysan project will get the go ahead?**

I am confident that this project will eventually get the go ahead as there is a great deal of local and federal support for this critical development that will capture a huge amount of gas that is currently being flared, resulting in a great loss of wasted energy and environmental damage to a wide area in the south of the country. Now that the bid rounds for the development of super -giant oil fields in the south have been completed, we expect the government to turn its attention to the approval of this and a number of other important projects that were effectively stalled pending conclusion of those bid rounds.

**Why is a small E&P company like Gulfsands pursuing a large midstream project in Iraq?**

This is a lucrative project on its own. However we see this project as providing us with the additional opportunity to be involved in the development of a number of oil fields in the Maysan province which would then produce additional volumes of gas that could be added to our gas gathering project while providing additional revenues from the production of oil. I would stress however that this is not a project we expect to undertake alone: we intend to bring in one or more larger partners at the appropriate time, which would provide the lion's share of the funding, and indeed we have had discussions with potential candidates under way for some time.

**Iraq has become a “big oil” game: can Gulfsands really expect to prosper there given its size?**

The initial “game” in Iraq has obviously attracted many large companies, and the technical challenges and the cost of developing the oil fields already awarded will be very significant. Gulfsands is therefore pursuing projects that it considers capable of executing either on its own or in partnership with larger companies. Obviously to the extent we can form strategic partnerships with large companies our capacity to become involved in larger projects will increase. Our focus, therefore, has been on forming suitable partnerships to pursue projects where we can be appropriately rewarded for the contribution we make in the form of our local experience and relationships gained from our lengthy presence in the country.

**Why are you not looking at opportunities in Kurdistan?**

We have never “not looked” at Kurdistan because it is obviously a region of huge oil and gas potential. However, it is well known that a number of legal and commercial issues critical to the successful exploitation of oil and gas in Kurdistan remain to be resolved between the Federal government and the regional government of Kurdistan. In our view, until those issues have been reliably resolved, our efforts in Iraq will most profitably be directed towards opportunities in the south of the country, where there are a very substantial number of discovered but undeveloped fields , significant existing infrastructure, lower geological risk generally, and fewer uncertainties about how we will be compensated if our efforts are successful.

**Are you interested in looking at projects outside of Syria and Iraq?**

Our principal focus for new business has been, and remains, Syria and Iraq. However we believe that we have the capacity to take on additional projects given our financial strength, and so will continue to look for opportunities within the wider Middle East and North Africa region, seeking to leverage existing relationships as in Syria and Iraq. As part of this strategy, we announced the farm-in to two permits in Tunisia on 22 March 2010.

Mahdi Sajjad

**President**

29 March 2010

**OPERATIONS REVIEW**

**SYRIA**

Description

Gulfsands is the operator of the Block 26 Production Sharing Contract ("PSC") with a 50% working interest. The other 50% interest is held by Sinochem following its takeover of Emerald Energy in Q4 2009. Block 26 covers an area of approximately 8,300 km². The PSC grants rights to explore, develop and produce from all stratigraphic levels outside the existing field areas and the deeper stratigraphic levels below the pre-existing discovered field areas. The current exploration period expires in August 2010 but may be extended at the Contractor's option for a further two years. The minimum work commitments for the current exploration period have already been satisfied.

Gulfsands has discovered two commercial oil fields within the PSC area, Khurbet East and Yousefieh. The development and production period for the Khurbet East field expires in February 2033 (25 years after commercial approval) and that for the Yousefieh field in January 2035, but each may be extended for a further 10 years at the Contractor's option. The terms of the PSC comprise a 12.5% royalty, cost recovery allowance, and the sharing of the resultant profit oil between the contractor group and the Syrian Petroleum Company ("SPC").

The Khurbet East field was discovered in June 2007 by the KHE-1 well and was appraised by two further wells in H2 2007. Commercial development approval was granted in February 2008. The development and operation of the field is being undertaken by Dijla Petroleum Company ("DPC"), a joint operating company formed with the SPC for this purpose. The KHE-1 well was a multi-zone discovery, encountering hydrocarbons in the Cretaceous Massive formation at a depth of approximately 2000 metres and in the deeper Triassic Butmah and Kurachine Dolomite formations. The reserves attributable to Khurbet East come from the Cretaceous Massive formation only and exclude hydrocarbons in the deeper Triassic formation. Oil production commenced from the Khurbet East field in July 2008 using an early production facility ("EPF"), which had been constructed by SPC and leased to the Contractor group.

The Yousefieh field was discovered in November 2008 by the Y-1 well which was drilled to a depth of approximately 2100 metres and encountered oil in the Cretaceous aged formations. Y-1 is located approximately 3 km away from the EPF at Khurbet East. Two appraisal wells were drilled in 2009 and commercial development approval was granted in January 2010. The field is expected to be placed on production during H1 2010.

The crude oil from Khurbet East has an API gravity of approximately 25°, slightly lighter than that of Syrian Heavy crude oil. The oil is transported to the SPC operated facilities at the Souedieh-3 station, some 30km away, where it is mixed with the Syrian Heavy crude oil, and exported to the Mediterranean port of Tartous using SPC's oil handling infrastructure. Oil from Yousefieh tested variously at 23-24° API (Y-1 and Y-3) and 17° API (Y-2).

## Operations

*Production*

Gross oil production from the Khurbet East field increased by 70% during 2009: at the start of the year production was just over 10,000 bopd from five wells and by the end of the year this had risen to approximately 17,000 bopd from seven wells. Production in the first seven months of the year was constrained by the capacity of the Early Production Facility, but this was alleviated in August by the addition of another two phase separation unit, thereby increasing the throughput capacity to 18,000 bopd.

Production as at the end of March 2010 stood at approximately 17,000 bopd from seven wells. Throughout the period under review the Khurbet East field has produced oil with minimal amounts of water (less than 0.3% by volume) and with negligible pressure loss, implying the likely presence of a strong water drive from the flanks of the field. The central area of the field, where the currently producing wells are all located, exhibits exceptional reservoir quality with multi-Darcy permeability arising from the "vugular" nature of the carbonates.

To date all production has been trucked to the SPC processing facilities at the Souedieh-3 station, a distance of some 30km by road. Despite an upgrade to the road undertaken during the year, the volume of truck movements at current production levels is not sustainable in the medium term and therefore work is under way to build a 22 km 8" pipeline to replace the trucking operation. It is anticipated that this will be completed in mid 2010.

*Wells*

During the year a total of nine production and appraisal wells were drilled using a single rig: seven on Khurbet East and two on Yousefieh. The two Yousefieh wells were both vertical appraisal wells, whereas the Khurbet East wells comprised three vertical appraisal wells to delineate the southern extremities of the field and four production wells, two vertical and two horizontal. Two of the Khurbet East wells were on production by the end of 2009 and two were suspended as future producers. The depths of the wells on both fields ranged from 1986 metres to 2139 metres true vertical measured depth.

The production wells on Khurbet East drilled in 2009 cost an average of $2.7 million to drill (50% for Gulfsands' interest) and took an average of 29 days from spud to rig release. The exploration and appraisal wells cost an average of $3.5 million to drill (50% for Gulfsands' interest) and took an average of 35 days from spud to rig release (the additional time and cost being mainly due to logging and testing).

On Khurbet East, KHE-7, which was the final well drilled in 2008, was completed in January 2009. KHE-7 was a step-out appraisal well to the north intended to delineate the northern extent of the field. While oil shows were encountered the porosity was found to be much lower than in the central portion of the field. The well was suspended for further evaluation and well testing. KHE-8, a step-out appraisal well to the south, was drilled in March, and encountered a 23 metre gross (15 metre net) oil-bearing section with reasonable porosity. The well flowed 20-23° API oil to surface on test following acid stimulation and under nitrogen lift at a rate of 617 bopd, and was suspended as a potential future producer. The rig then commenced a three development well programme. KHE-9 was drilled in April as a vertical well in the central area of the field: it flowed 3,040 bopd through a

48/64" choke under an open hole drill stem test ("DST") and was placed on production in early July. KHE-10 was drilled in May/June as a horizontal producer with a bottom hole location some 700 metres northwest of KHE-9: it penetrated a 260 metre horizontal section of the reservoir and was placed on production in early August. KHE-11, another horizontal producer, was then drilled in July and penetrated a 60 metre section of the uppermost portion of the reservoir. Under test the well produced oil at a rate of 1660 bopd through a 48/64" choke, but with an associated water cut of some 30%. The well was completed as a future producer but suspended pending further testing to identify the source of the water. The rig then moved on to drill KHE-12, a far step out appraisal well some 3.2 km further south than KHE-8, aimed at delineating the southern boundary of the field and locating the field-wide oil water contact ("OWC"). Whilst the presence of residual oil was identified in a six metre section of core, the well flowed water under test leading to the interpretation that it lay beneath the field OWC. The KHE-13 vertical development well was drilled in November at a location approximately equidistant between the KHE-1 discovery well and KHE-8. The well flowed 1,020 bopd under test through a 32/64" choke with negligible amounts of water, and was placed on production in January 2010. Finally, KHE-14 was spudded in December at a location 4.9 km south of the KHE-1 discovery well, between the KHE-8 and KHE-12 locations, as an appraisal well intended to intersect the field OWC. An oil column of 14 metres gross (six metres net) was encountered, and the well flowed 27° API oil to surface under open-hole DST using nitrogen lift at a rate of 613 bopd through a 2" choke. Although a definitive OWC was not observed on wireline logs or drilling data it was established that oil was produced from a vertical depth of 1580 metres sub-surface, nine metres lower than the previous deepest oil flow observed in the field. This well result has caused the estimate of the volume of oil-in-place in Khurbet East to be revised upwards.

On Yousefieh, the Y-2 appraisal well, located 1.8km to the east of the Y-1 discovery well (drilled in November 2008), was drilled in January/February and found a gross oil column of 36 metres (16 metres net). Under a DST conducted at that time the well flowed predominantly water, which was suspected to be from a non-reservoir interval. A workover was conducted in August and after acid treatment the well flowed oil to surface at a rate of 139 bopd through a 2" choke under nitrogen lift with a water cut of 49%. The Y-1 discovery well was re-entered in August to conduct remedial cementing operations on the production liner, which was then perforated across a 14.5 metre interval and flowed 356 bopd of oil to surface through a 48/64" choke with a water cut of less than 1%. Using nitrogen lift and a 2" choke the flow rate was improved to 823 bopd. The Y-3 appraisal well, located 500 metres to the south-east of Y-1, was drilled in September/October and encountered a gross oil column of 60 metres (net 49 metres) and an OWC at 1590 metres subsurface. Under an open-hole DST the well flowed 24-25° API oil to surface at a rate of 226 bopd through a 32/64" choke with no water. It is believed that the lower flow rate compared with Y-1 is a result of formation damage sustained during drilling and coring operations. An application for commercial development of the Yousefieh field was submitted in December and approval received for this development in January 2010. First oil from the field is anticipated by mid-April 2010.

*Health & Safety*

A rigorous health & safety framework has been implemented in 2009. A detailed health & safety manual has been developed a copy of which is made available to all employees. The drilling department holds regular safety meetings, drills and inspections both on a regular scheduled basis and prior to undertaking certain tasks. No lost time incidents have been recorded since drilling

operations commenced in 2006. A full time HSE manager has been recruited and HSE training for all new recruits, as well as refresher sessions for existing staff, is being implemented.

*Exploration Programme*

850 km² of 3D seismic data over an area surrounding the Khurbet East and Yousefieh fields was acquired during H1 2009 using the Chinese firm BGP as seismic contractor. This was then processed by PGS in Cairo and the processed data was delivered to Gulfsands in September and October. The analysis of this data resulted in the identification of at least four prospects for exploration drilling in 2010, together with numerous potential leads that may evolve into prospects after further analysis and study. In addition in H2 2009 64 km² of 3D seismic was acquired on a sole-risk basis over an area known as Taramish located at the north-east corner of the block, and the processed data was delivered to Gulfsands in March 2010.

The first exploration well, Zaman-1, located approximately 4.5 km south of the Khurbet East field and targetting the same Cretaceous Massive formation as is under production at Khurbet East, was completed in February 2010. The well encountered good quality reservoir, with an interpreted four metre oil column, but flowed water under test and so has been suspended as a potential future water disposal well. The second well, Hanoon-1, targeting a smaller Cretaceous target 10km to the north of the Khurbet East field, was spudded at the end of February 2010, and the results are likely to be known in April.

Plans for 2010

In 2010 we intend to drill two further exploration wells on Block 26 after Hanoon-1, four development wells on Khurbet East and a development well on Yousefieh. In facilities terms, our key project is the construction of a permanent central production facility at Khurbet East to replace the early production facility. This will have a design capacity of 50,000 barrels of fluid per day and be capable of handling a minimum of 35,000 bopd of oil allowing for the eventuality of associated water production. We will also be tying in the Yousefieh field to the early production facility during H1 2010 via its own dedicated two phase separation unit, with a view to putting the field on production during April 2010.

We plan to acquire further 3D seismic data over at least a 500 km² area of Block 26 adjacent to the west of the 2009 seismic area, with the aim of maximising the exploration prospectivity of the Block before the final relinquishment of the exploration licence in August 2012. We intend to exercise our option in August 2010 to extend the current exploration period for a further two years, and an area comprising 25% of the original licence area has been identified for relinquishment in accordance with the terms of this extension.

**USA**

Description

Gulfsands owns a portfolio of non-operated oil & gas properties in the Gulf of Mexico, in the shallow "shelf" region offshore Texas and Louisiana. These comprise 37 leases containing 24 producing fields with over 200 wells operated by 17 different operators. Working interests range from 2% to 53%. Gulfsands also has a small interest in one onshore oil & gas field in Texas.

The assets are relatively mature, although some additional potential exists in the deeper sections. Proven & Probable reserves at year-end 2009 amounted to 4.6 million boe on a working interest basis (3.6 million boe on a net interest basis), comprised 46% of oil and 54% of gas.

The Group considers the US business to be non-core and intends to dispose of it as and when market conditions are favourable.

Operations

Operations in 2009 were dominated by the ongoing effects of Hurricanes Gustav and Ike in 2008 which caused damage both to our own facilities and to third-party infrastructure such as pipelines.

Production, which on a working interest basis had averaged 1,433 boepd and 2,575 boepd in 2008 and 2007 respectively, averaged only 1,144 boepd in 2009 because a significant element of production remained shut-in during the year pending repairs to third party pipeline infrastructure. The composition of 2009 WI production was 51% gas (3,526 mcfd), 44% oil (503 bopd) and 5% NGLs (2,217 galls/d). After tax and royalties, net interest production in 2009 was 883 boepd.

Production started the year at just over 800 boepd (working interest) having been below 400 boepd in October 2008 in the immediate aftermath of the hurricanes, and increased to 1,683 boepd in December as production from key properties, notably Eugene Island 32 and Eugene Island 57 was progressively restored. However during the year certain other non hurricane-related problems with third party infrastructure were encountered, for example at the West Delta 59 property, which caused production from this field to be shut in as of July 2009. This field returned to production during March 2010 once construction of a new oil pipeline was completed. Since year-end production has continued to increase and at the end of March was running at approximately 1,700 boepd (working interest), comprising 37% oil and 63% gas.

Total repair costs arising from the 2008 hurricanes amounted to $ 5.8 million over 2008 and 2009, of which it is estimated that at least $1.1 million is recoverable from insurance. Although damage, and subsequent repairs, to facilities occurred on numerous properties, approximately 75% of the repair and restoration expenditures were concentrated in two properties (Eugene Island 32 and Vermillion 315/332). Repairs to these facilities were undertaken quickly and production was restored during the first half of 2009.

Operational highlights include the successful installation of a caisson and compressor at West Cameron 310 leading to increased gas production, acid stimulation of several wells in the Vermillion 379 property that yielded increased oil production, and production finally re-commencing from the

Eugene Island 57 field in November. During the year 24 wells on 6 properties were plugged and abandoned and 3 structures were decommissioned.

Portfolio rationalisation continued during 2009, with the outright sale of the Galveston Island 215/186 property and the South Pass 49 Unit, and the sale with a retained over-riding royalty of the South Marsh Island 234/235 property. These transactions involving non-core assets also reduced the division's future abandonment obligations (although in present value terms the balance sheet provision has, in fact, increased).

Plans for 2010

With the hurricane recovery process nearly complete, we intend to undertake a selective re-investment programme in 2010. Plans include participating in the drilling of four additional wells within the central area (Eugene Island, South Marsh Island, Vermillion) and an aggressive work-over and re-completion programme concentrating on the Eugene Island 32 field. We will also continue to look for opportunities to rationalise the portfolio where we can harvest value or reduce future abandonment liabilities.

**Reserves and contingent resources**

The Group's reserves at 31 December 2009 are based on estimates made by management and reviewed by independent petroleum engineers. For the Syrian assets the review was performed by Senergy (2008: RPS Energy), and for the USA by Netherlands Sewell & Associates ("NSA") (2008: same).

Definitions for Proved and Probable reserves are contained in the Glossary.

Working interest reserves in Syria represent the proportion, attributable to the Group's 50% participating interest, of forecast future crude oil production during the economic life of the Block 26 PSC, including the share of that production attributable to Syrian Petroleum Company ("SPC"). In assessing the economic life it has been assumed that the option to extend the life of the PSC for a further 10 years after its initial expiry date is exercised. Working interest reserves in the USA represent the proportion, attributable to the Group's participating interests, of forecast future oil and gas production during the economic life of the properties in question, before deduction of state production taxes and overriding royalty interests. Working interest reserves have been derived from the net revenue interest reserves data contained in the NSA report, by grossing up for the percentage production tax and royalty "burden" applicable to each property. The reserves-weighted average burden at 31 December 2009 was 23%.

Entitlement reserves in Syria represent the Group's estimated share of working interest reserves after deducting the share of forecast future production attributable to SPC. This proportion is impacted by assumptions as to future development expenditure and future oil prices. For the calculation as at 31 December 2009 the average price of Brent crude was assumed to be $70/bbl in 2010, rising to $80/bbl in 2012 and constant thereafter. Entitlement reserves in the US represent the Group's estimated net revenue interest reserves after deduction of the equivalent share of oil and gas production attributable to state production taxes and overriding royalty interests.

**RESERVES TABLE**

| **Working Interest Basis** | Syria | USA | | Group Total | | |
|---|---|---|---|---|---|---|
| As at 31 December 2009 | Oil & NGLs mmbbls | Oil & NGLs mmbbls | Gas bcf | Oil & NGLs mmbbls | Gas bcf | Oil & Gas mmboe |
| Proved | 21.2 | 1.5 | 12.4 | 22.7 | 12.4 | 24.8 |
| Probable | 24.8 | 0.6 | 3.1 | 25.4 | 3.1 | 25.9 |
| Proved & Probable | 46.0 | 2.1 | 15.5 | 48.1 | 15.5 | 50.7 |
| Possible | 36.2 | 0.1 | 1.4 | 36.3 | 1.4 | 36.5 |
| Proved, Probable & Possible | 82.2 | 2.2 | 16.9 | 84.4 | 16.9 | 87.2 |

Movements in Proved & Probable reserves during year

| | Syria | USA | | Group Total | | |
|---|---|---|---|---|---|---|
| At 31 December 2008 | 35.2 | 2.4 | 16.5 | 37.6 | 16.5 | 40.4 |
| Discoveries and Additions | - | - | - | - | - | - |
| Disposals | - | (0.1) | (0.5) | (0.1) | (0.5) | (0.2) |
| Revisions | 13.1 | (0.0) | 0.8 | 13.1 | 0.8 | 13.2 |
| less Production | (2.3) | (0.2) | (1.3) | (2.5) | (1.3) | (2.7) |
| At 31 December 2009 | 46.0 | 2.1 | 15.5 | 48.1 | 15.5 | 50.7 |

| **Entitlement Basis** | Syria | USA | | Group Total | | |
|---|---|---|---|---|---|---|
| As at 31 December 2009 | Oil & NGLs mmbbls | Oil & NGLs mmbbls | Gas bcf | Oil & NGLs mmbbls | Gas bcf | Oil & Gas mmboe |
| Proved | 9.5 | 1.2 | 9.3 | 10.7 | 9.3 | 12.3 |
| Probable | 7.9 | 0.4 | 2.4 | 8.3 | 2.4 | 8.7 |
| Proved & Probable | 17.4 | 1.6 | 11.7 | 19.0 | 11.7 | 21.0 |
| Possible | 10.7 | 0.1 | 1.0 | 10.8 | 1.0 | 11.0 |
| Proved, Probable & Possible | 28.1 | 1.7 | 12.7 | 29.8 | 12.7 | 32.0 |

Movements in Proved & Probable reserves during year

| | Syria | USA | | Group Total | | |
|---|---|---|---|---|---|---|
| At 31 December 2008 | 14.3 | 1.8 | 12.6 | 16.1 | 12.6 | 18.2 |
| Discoveries and Additions | - | - | - | - | - | - |
| Disposals | - | (0.1) | (0.4) | (0.1) | (0.4) | (0.1) |
| Revisions | 4.3 | 0.1 | 0.5 | 4.4 | 0.5 | 4.5 |
| less Production | (1.2) | (0.2) | (1.0) | (1.4) | (1.0) | (1.6) |
| At 31 December 2009 | 17.4 | 1.6 | 11.7 | 19.0 | 11.7 | 21.0 |

## Financial Review

### Selected Operational and Financial Data

| | 2009 | 2008 (restated) | *Change %* |
|---|---|---|---|
| | mmboe | mmboe | |
| Production : working interest | 2.7 | 1.2 | *119%* |
| Production : entitlement | 1.6 | 0.8 | *90%* |
| | US$ MM | US$ MM | |
| Revenue | 84.4 | 53.6 | *57%* |
| Gross Profit | 46.5 | 26.2 | *77%* |
| Operating Profit / (Loss) | 28.6 | (6.9) | *n/a* |
| Net Profit /(Loss) after tax | 27.8 | (5.4) | *n/a* |
| | | | |
| Net cash provided by Operating Activities | 43.5 | 20.0 | *117%* |
| Capital Expenditures | (25.8) | (19.0) | *36%* |
| Decommissioning costs net of escrow cash released | (0.9) | (2.7) | *-66%* |
| Cash balance at end of year | 57.6 | 36.8 | *57%* |

## Market Conditions

Following the dramatic falls in energy prices in the second half of 2008, in 2009 oil prices firmed steadily over the year, with Brent finishing the year at $78/bbl having started the year at $36/bbl. US natural gas prices however continued falling to a low of $1.8/mcf in August before climbing back to finish the year at $5.8/mcf.

### Production and Sales Prices
(excludes NGLs)

| | Working Interest Production | | Entitlement Production | | Average Sales Price | | Premium / (discount) to Brent | Premium / (discount) to Henry Hub |
|---|---|---|---|---|---|---|---|---|
| | Oil | Gas | Oil | Gas | Oil | Gas | Oil | Gas |
| | bopd | mcf/d | bopd | mcf/d | US$/bbl | US$/mcf | US$/bbl | US$/mcf |
| **2009** | | | | | | | | |
| Syria | 6,249 | - | 3,367 | - | 57.3 | - | (4.4) | - |
| USA | 503 | 3,526 | 399 | 2,669 | 60.5 | 3.9 | (1.2) | (0.1) |
| Total | 6,752 | 3,526 | 3,766 | 2,669 | | | | |
| **2008** | | | | | | | | |
| Syria | 4,494 | - | 2,655 | - | 61.1 | - | (10.9) | - |
| USA | 461 | 5,262 | 352 | 4,021 | 102.3 | 9.4 | 2.6 | 0.5 |
| Total | 4,955 | 5,262 | 3,007 | 4,021 | | | | |

The Syrian production figures for 2008 are quoted from the start up of production in July 2008.

## Group

The financial statements for the year ended 31 December 2008 have been restated in order to correct the misclassification in that year and in prior years of certain items of expenditure in the US business, which were classified as capital expenditure when they should properly have been charged to the income statement as operating expenses. The net effect on the 2008 financial statements has

been to increase group profit by $4.3 million, and a fuller explanation is given below in the USA section of this review. The comparative 2008 figures referred to throughout this review are the restated numbers.

In addition to this restatement the Group has reclassified certain cash flows relating to inventory and capital expenditure from operating cash flows to investing cash flows. This reclassification has had no impact on the reported results or financial position of the Group for prior periods.

*Income Statement*

The group recorded a maiden net profit in 2009 of $27.8 million (2008: loss of $5.4 million), driven by strong production growth in Syria. As in 2008, there was a marked difference between the performance of Syria (net profit $48.4 million) and that of the USA (net loss, excluding interest owed to Group, of $14.2 million). Commentary on the results of each unit is given below.

Group revenues grew 57% to $84.4 million (2008: $53.6 million), of which $70.5 million arose from Syria and $13.9 million from the USA. Average entitlement production net to Gulfsands' interest was 4,250 boepd (3,367 bopd in Syria and 883 boepd in the USA), a 16% increase over the previous year (2008: 3,750 boepd, measuring Syrian daily production from the start of production in late July).

Cost of sales rose by 39% to $38.0 million (2008: $27.4 million), impacted inter alia by a rise in impairment charges in the USA to $6.4 million (2008: $1.7 million), and a higher depletion charge in Syria commensurate with the increase in production.

Administrative expenses fell significantly to $15.5 million from $30.3 million in 2008, but this reflected primarily the sharp drop in charges attributable to the Group's share incentive schemes ($1.1 million in 2009 vs. $12.6 million in 2008). The principal reason for the high share-based payment charge in 2008 was the options granted to incoming and existing management, a high proportion of which vested immediately and so had a disproportionate impact on the income statement. Excluding these charges and foreign exchange gains or losses the underlying group administrative expenses increased by 15% to $14.9 million (2008: $13.0 million), primarily as a result of increased staff and office costs in London and Damascus.

After deduction of hurricane repair costs of $2.3 million (2008: $2.8 million), Group operating profit came to $28.6 million, compared with a loss of $6.9 million in 2008. After crediting interest income of $0.3 million (2008: $1.2 million) and deducting a non-cash charge of $1.1 million (2008: $1.7 million) for the unwinding of the discount in the decommissioning provision, pre-tax profits amounted to $27.8 million (2008: loss of $7.3 million).

There was no material tax charge in 2009 and none is expected to arise in the next few years as all local tax obligations in Syria are settled on the Group's behalf by the Syrian Petroleum Company.

**Unit Revenues and Costs (per boe)**

| | Syria | | USA | |
|---|---|---|---|---|
| | 2009 | 2008 | 2009 | 2008 |
| | | | | (as restatec |
| | $/boe | $/boe | $/boe | $/boe |
| Gross Revenue | 57.3 | 61.1 | 41.2 | 70.1 |
| less royalties and production share | (26.4) | (25.0) | (9.4) | (16.4) |
| Net Revenue | 30.9 | 36.1 | 31.8 | 53.7 |
| Production and transport costs | (2.3) | (1.9) | (32.0) | (25.2) |
| Operating Cash Flow | 28.6 | 34.2 | (0.2) | 28.5 |
| Depletion | (4.3) | (4.0) | (4.5) | (10.2) |
| Decommissioning accrual | - | - | (2.5) | (3.2) |
| Operating profit / (loss) before G&A | 24.3 | 30.2 | (7.2) | 15.1 |

*Cash Flow*

Cash from operating activities increased by 117% to $43.5 million (2008: $20.0 million). Capital expenditure totalled $25.9 million, of which $5.4 million was spent on exploration activity, $18.1 million on development activity, $1.8 million on increases in material inventory and the balance on non oil & gas assets. In addition $0.9 million (2008: $2.7 million) was spent on decommissioning assets in the US Gulf of Mexico, net of releases of cash held in escrow as collateral.

The exercise of options yielded cash of $3.6 million.

The Group has historically invested, and intends to continue to invest, significant sums in exploration and development capital expenditure. The Group has been debt free since 2006 and has financed exploration and development investment from both cash generated from operations and equity investments since that time. The Group's current investment plans for 2010 and 2011 may be financed by cash generated from operations under all reasonably foreseeable scenarios.

*Balance Sheet*

The balance sheet remains strong with no outstanding debt and unrestricted cash balances at year-end of US$57.6 million, of which all but $14.1 million was held in US dollars. There were additional restricted cash balances of $12.0 million (2008: $13.2 million), held as collateral for decommissioning liabilities aggregating $31.6 million (2008: $26.3 million), all of which related to the US assets. The increase in decommissioning liabilities arises from an increase in future cost estimates and the use of a lower discount rate than last year. Trade and other receivables increased to $21.9 million (2008: $15.5 million), owing to timing differences in the receipt of cost recovery payments in Syria.

No hedges against oil and gas price movements were in place at year-end or during the year.

Syria

*Income Statement*

Working interest production averaged 6,249 bopd in 2009 (2008: 4,494 bopd, measured from the start up of Syrian production in July 2008), all of which was oil. Entitlement production amounted to 3,367 bopd (2008: 2,655 bopd). The average sales price was $57.3/bbl, representing a $4.4/bbl

discount over average Brent (2008: $61.1/bbl, representing a $10.9/bbl discount). Having been in excess of $12.0/bbl at the beginning of the year, the discount to Brent narrowed during 2009 and during the second half averaged $3.3/bbl, or 4.7% in percentage terms.

Revenues increased by 177% to $70.5 million (2008: $25.5 million). Cost of sales increased to $15.1 million (2008: $4.1 million), of which production costs were $2.3 million (2008: $ 0.5 million), transportation costs were $ 2.9 million (2008: $0.8 million), and depletion charges accounted for $9.9 million (2008: $2.8 million). Unit production costs per working interest barrel were $1.01/bbl, similar to 2008 ($0.71/bbl). Administrative expenses were up by 123% to $6.9 million (2008: $3.1 million), owing to higher staff and local office costs and the Group ceasing to capitalise a portion of overheads in Syria upon the declaration of commerciality of the Khurbet East field in 2008.

The Syrian operations recorded a net profit of $48.4 million, an increase of 164% over the $18.3 million recorded in 2008.

*Cash Flow*

Cash from operations was $54.4 million, and included $5.6 million in sales proceeds retained from the previous year's production pending the completion of certain assay tests on the Khurbet East oil. Capital expenditure was $22.1 million, including development and inventory expenditure of $16.5 million and exploration of $5.4 million. The net cash surplus for the Syrian operations was $32.5 million.

USA

*Income Statement*

Production in 2009 averaged 1,144 boepd on a WI basis (883 boepd on an NRI basis), compared with 1,433 boepd (1,095 boepd NRI) in 2008, a drop of 20%, owing to the continued shut-in of production for most of the year as a consequence of damage to third party infrastructure caused by the 2008 hurricanes. The composition of 2009 WI production was 51% gas (3,526 mcfd), 44% oil (503 bopd) and 5% NGLs (2,217 galls/d). Average sale prices were significantly down on 2008 levels: we received an average of $3.9/mcf for our gas (2008: $9.4/mcf) and $60.5/bbl for our oil (2008: $102.3/bbl). Gas sales prices were in line with the Henry Hub marker price but oil sales prices were $2.3/bbl below WTI because of a pipeline charge connected with the Eugene Island properties that was deducted from revenues.

As a result revenues were down by half on the prior year at $13.9 million (2008: $28.1 million). Cost of sales however reduced by only 2% to $22.8 million (2008: $23.3 million), which resulted in a gross loss, after hurricane expenses, of $11.2 million (2008: gross profit of $2.1 million).

Within cost of sales, non-cash items amounted to $8.8 million (2008: $7.0 million), comprising depletion of $2.4 million (2008: $5.4 million) and an impairment charge of $6.4 million (2008: $1.7 million). Impairment charges have occurred as a result of a combination of lower forecast gas prices in future years and increased estimates of the present value of future decommissioning liabilities. Hurricane repair costs (net of expected insurance recoveries of $1.1 million) were $2.3 million (2008: $2.8 million), other repair and workover costs were $3.5 million, decommissioning costs expensed (in excess of existing provisions) were $0.7 million (2008: $3.0 million) and the balance was general lease operating expenses.

Administrative expenses were $2.7 million (2008: $3.2 million) and the non-cash charge to unwind the discount on the decommissioning provision was $1.1 million (2008: $1.7 million), resulting in a loss for the year before interest of $14.2 million (2008 as restated: loss of $0.3 million).

*Cash Flow*

Cash flow from operations was negative to the tune of $5.1 million. $2.1 million of decommissioning costs were paid (2008: $5.6 million), which was partially funded by a release of $1.2 million (2008: $2.9 million) of cash held in escrow. Capital expenditure was $3.4 million, largely comprising $1.5 million for a recompletion on the Eugene Island 32 property and $0.9 million on drilling the B-8 Side Track on the West Cameron 498 property. The net cash deficit for the year for the US operations was $13.0 million, which was funded by an increase in the loan from the parent company.

*Prior Year Restatement*

Following the prior year restatements contained in the 2008 financial statements, a full internal assessment was undertaken in 2009 of the accounting systems and processes of Gulfsands USA, involving external consultants. This has resulted in a number of changes to the accounting software and to internal processes and procedures, and certain staff changes within the accounts department. As part of this process it came to light that over a number of years up to 2008, certain items of expenditure had been erroneously classified as capital items when they should have been charged to the income statement as operating expenses. The aggregate amount so misclassified over the years was $9.7 million, most of which related to financial years up to and including 2007. The restatement of prior years' accounts has resulted in reductions to fixed assets (and thereby to depletion and impairment charges) and a corresponding increase in operating expenses. Because of certain timing differences, the reduction in impairment charges in 2008 more than offset the increase in operating expenses, resulting in a $4.3 million reduction in the 2008 loss before interest and tax to a loss of $1.1 million (previously reported a loss of $5.4 million).

Financial Risk Management

The financial risks concerning the group comprise pricing risk, currency risk, liquidity risk and access to capital.

Pricing risk arises because all of the Group's oil and gas production is sold under short term pricing arrangements and so the Group is exposed to movements in oil and gas prices. To date this exposure has not been hedged since the Board has taken the view that the Group's cash flow is sufficient to bear any reasonably foreseeable downturn in prices without affecting our core business. However this policy is kept under frequent review.

Currency risk arises because the Group's sales are denominated in US dollars but a proportion of its expenses are in euro (some procurement costs) and sterling (head office costs). The risk is mitigated by retaining a proportion of our cash resources in these currencies.

Liquidity risk concerns the Group's ability to access funds to meet its obligations as they fall due. Our policy is to maintain sufficient cash balances and readily realisable investments for this purpose, given that the Group has no bank lines of credit available to it. Sums in excess of what is needed to meet near-term obligations are invested in a money market fund which holds a diverse portfolio of short-term financial instruments rated A1 or better, resulting in a greater spread of risk and an improved return compared with what we would otherwise be able to achieve. It is the Board's

intention to seek to put in place one or more bank credit lines as and when Syrian country risk becomes more readily acceptable in the international banking market.

Access to capital depends on conditions prevailing in the equity market for independent E & P companies generally and the sentiment among the Group's shareholders in particular. Considerable efforts have been devoted in 2009 to communicate with our shareholders, to cultivate new investors and to build relationships with research analysts and equity sales desks at brokerage houses, in order to widen the following of Gulfsands by the investment community generally.

Andrew Rose

**Chief Financial Officer**

29 March 2010

## Principal Risks and Uncertainties

The Board places a high priority on managing and mitigating risk in all its forms. A comprehensive assessment of risks facing the Group is undertaken annually using a matrix approach which assesses each risk in terms of its financial impact, probability of occurrence, shareholder tolerance and cost of mitigation, and reviewed by the Board. Subsequent reviews are carried out as often as necessary during the year.

The following summarises the principal risks and uncertainties facing the Group and the measures which have been taken to mitigate them

| **Risk** | **Mitigation** |
|---|---|
| **External** | |
| Political Interference<br>The risk of authorities in the host country seeking to expropriate assets or change the terms of existing contracts | This can only effectively be mitigated by developing close relationships at high level in the country in question. In the case of Syria we have successfully developed such relationships through Mahdi Sajjad as a result of our longstanding presence in the country and our active community programmes. |
| Act of War or Terrorism<br>The risk of an act of war or terrorism in Syria, as a result of Middle East tensions generally, impacting the Group's operations or strategy | We maintain insurance providing for the medical treatment and evacuation of personnel in the event of an act of war or terrorism. Corporately we do not currently insure against such events in view of the costs of doing so, considering this as a risk that investors are prepared to take if they invest in the Company |
| Price and Currency Movements<br>The risk of movements in oil and gas prices or currencies adversely impacting profits and cash flow | The Group sells all its oil and gas production on the spot market : there are no long term price contracts in place. The Board considers that investors in the Company wish to retain exposure to oil and gas price movements, so will only undertake price hedging if available funds would be insufficient to finance planned expenditure in the event of a material price downturn<br>The Group maintains some cash balances in currencies other than US dollars to cover expenditure commitments in these currencies |
| Retention of Key Staff<br>The risk of defection of key staff as a result of higher financial inducement | The Group aims to pay competitively and undertakes an annual benchmarking exercise to ensure that remuneration is in line with market rates. Remuneration includes a significant performance-based component and participation in share incentive schemes extends throughout the Group.<br>We also aim to provide a challenging but fulfilling working environment so that pay is not the only determinant of job satisfaction |
| | |
| **Operational** | |
| Oilfield Accident<br>The risk of a blow-out or other control-of-well incident leading to damage to people, property or environment | The Group has implemented comprehensive health and safety procedures in Syria and has recently hired a full-time HSE manager. To date no lost-time incidents have occurred. Insurance is maintained for repair to structures and for the control and redrill of wells, as well as for third party liabilities |

| | |
|---|---|
| <u>Natural Disaster</u><br>The principle risk is that of hurricanes in the Gulf of Mexico impacting our US business as occurred in 2008 | Until 2009 the Group insured its Gulf of Mexico properties against damage from hurricanes, but in the wake of the 2008 hurricane season the cost of such insurance became prohibitively high and so the Group did not insure against windstorm risk in 2009<br>In any event, the majority of the economic cost to the Group from the 2008 hurricanes arose because damage to third party infrastructure caused production to be shut in for an extended period : a risk against which it is impossible to insure at an economic cost. |
| <u>Exploration Failure</u><br>The risk that an exploration well is found not to contain commercial quantities of hydrocarbons | Exploration is an inherently risky business, where the risk of failure on any one well is usually significantly greater than the chance of success. Risk is mitigated by careful geological and petrophysical analysis prior to drilling, often involving the acquisition of 3D seismic data.<br>The cost of failure is mitigated in Syria by the fact that operations are land-based so the cost of a well is comparatively low, as well as by the fact that exploration costs within Block 26 are recoverable against existing production under the terms of the PSC, meaning that the net cost of a well to the Contractor group is only 35% of its gross cost. |
| <u>Partner Approval</u><br>The risk that the a joint venture partner does not approve the Group's operational or budgetary plans | In Syria the Group has a 50% interest in the Block 26 joint venture and acts as operator, with the other 50% being held by Sinochem. Because the Group does not hold outright majority voting powers it is possible in certain circumstances for a partner to block decisions. This is mitigated by intensive efforts to communicate our strategy and plans to our partner and to address their concerns, with the fall-back that we retain the option to carry out an operation on a sole-risk basis if approval is not forthcoming. |
| <u>Equipment Availability</u><br>The risk of necessary equipment such as rigs not being available when required | The US sanctions regime against Syria has resulted in the Group not being able to source goods and services from US companies. However, to date this has not proved a constraint as we have always been able to procure from non-US sources. For key equipment such as drilling rigs the procurement process is begun well in advance of the need crystallising, in order to minimise any delays. |
| | |
| **Financial** | |
| <u>Cost control</u><br>The risk of costs exceeding budget through inadequate cost control | A detailed expenditure control framework is in place involving clear limits on expenditure authority and frequent reporting of costs and commitments against budget. Particular emphasis is placed on controlling expenditure at the pre-commitment stage. |
| <u>Liquidity and Funding</u><br>The risk of insufficient short term funds being available to meet commitments or long term funds to finance capital projects | The Group maintains significant balances in cash or short term money market funds. At present there are no bank lines of credit available to the Group given that the appetite for Syrian country exposure among international banks remains limited, but it is our intention to put in place such lines of credit as and when the situation eases.<br>We place great importance on cultivating relations with the investor community and with research analysts in order to ensure that the market is receptive to our story should the need to raise further equity arise. |

| **Reputational** | |
|---|---|
| <u>Fraud and Corruption</u><br>The risk that actions by an employee or business associate damage the Group's reputation or result in a financial cost | The Group has a detailed policy on Conduct of Business and Ethics which establishes clear guidelines for relationships with officials and suppliers, and which has been circulated internally. In addition a whistleblowing policy is in place allowing employees who become aware of an incident of fraud or corruption to report it safely to the appropriate person. |

## BOARD OF DIRECTORS

**Andrew West**
**Non-Executive Chairman**

Andrew West (52) has been Chairman of Gulfsands since July 2006. An investment banker specialising in mergers and acquisitions by career, he has worked for Smith Barney (1981 - 85), Lehman Brothers (1985 – 90), Guinness Mahon (1990 – 97) and from 1997 to 1999 was Managing Director of Strand Partners, a privately owned investment banking firm specialising in energy and natural resources. He is currently a non-executive director of numerous companies, and has had considerable experience as both a financial adviser and a non-executive director in the oil and gas sector.

**Richard Malcolm**
**Chief Executive**

Ric Malcolm (57) joined Gulfsands as Chief Executive in October 2008. A professional geoscientist with over 30 years of oil and gas experience, he began his career as a Petroleum Geologist with Woodside in Australia. He then spent 10 years with Ampolex, an Australian independent E&P company, latterly as Exploration Manager, followed by three years with Mobil as Manager for Papua New Guinea. In 1999 he joined OMV as Exploration Manager for Australia and New Zealand, going on to become Exploration Manager in Libya, General Manager in Norway and finally in 2006 Managing Director for OMV UK.

**Mahdi Sajjad**
**Executive Director and President**

Mahdi Sajjad (51) is an Iraqi national who was educated in the UK, and was one of the founders of Gulfsands in 1998. Having worked from 1981–88 with a consortium of British engineering companies in the Middle East and Africa, in 1988 he joined International Development Corporation in Dubai where he became Managing Director. From 1988 – 95 he was also a director of Oil & Minerals Development Corporation in Dubai. He has also established a number of companies with interests in the Middle East in different industry sectors but with particular emphasis on the energy and mining sectors.

**Andrew Rose**
**Chief Financial Officer**

Andrew Rose (53) joined Gulfsands as Chief Financial Officer in June 2008. He was formerly CFO of Burren Energy, the UK independent E&P company which he joined in 2001, helped to list on the London Stock Exchange in December 2003 and oversaw its sale to ENI in January 2008. Prior to this he had spent his career in investment banking, working in advisory, capital markets and financing roles, latterly as head of Corporate Finance for Eastern Europe, Middle East and Africa at Société Générale.

**Ken Judge**
**Director of Corporate Development & Communications**

Ken Judge (54) was one of the founder shareholders of Gulfsands but only joined the Board in 2006 as a Non-Executive Director, becoming an executive Director in 2008. A former corporate lawyer in Australia, he has held numerous public company directorships and has been engaged in the establishment or corporate development of oil and gas, mining and technology companies in the United Kingdom, Middle East, USA, Australia, Europe, Canada, Latin America and South East Asia.

**David Cowan**
**Non-Executive Director**

David Cowan (55) has been a Director of Gulfsands since 2006. A practicing solicitor, he is a partner with Lang Michener LLP based in Vancouver, Canada, and practices primarily in the area of corporate and securities law. He represents numerous publicly traded companies and has been involved in the drafting of British Columbia's securities legislation. He is a past Chairman of both the Securities and Natural Resources subsections, and the National Natural Resources subsection of the Canadian Bar Association. His specific Middle East experience includes ventures in Syria, Iraq and Algeria.

## CORPORATE SOCIAL RESPONSIBILITY

### Corporate Social Responsibility is among the core values of the Group and protecting those values is a key business priority.

Gulfsands has a policy of promoting high standards of corporate social responsibility ("CSR") and the Group is well recognised for its efforts in supporting the communities in which we operate.

The Directors interact on a regular basis with the Company's shareholders and we are pleased to acknowledge their backing for our initiatives to support the interests of our other stakeholders in the communities in which we operate. We believe that the combination of responsible corporate policies, the support of local social development programmes and the conduct of our operations in a manner that ensures a sustainable business and social environment, will help us create a thriving business. Through these activities we strive to earn the respect of the host governments and the people of the communities in which we operate, which can only assist us in lowering the Group's risk profile generally and in achieving our overall business development objectives.

Working within this framework, Gulfsands has achieved recognition for its business ethics and social responsibility and for providing a safe, reliable and enjoyable working environment for our employees.

### Health and Safety

We continue to focus management and financial resources on extending our excellent Health, Safety and Environment ("HSE") record. During 2009, a very busy period in our history, we completed the expansion of the early production facility at the Khurbet East field and over 21,000 metres of drilling carried out over almost 300 days, all with zero lost time incidents. This excellent record is a reflection of our commitment to preparation, training and inspection programmes designed to ensure our staff are able to work with the level of safety and efficiency that we and our stakeholders expect from our operations.

### Community and Labour Relations

Our interaction with the communities of the regions in which we operate has assisted us to quickly identify newly emerging local risks affecting our business. For example, at our operations on Block 26, Syria, this has been reflected in the construction of the new oil transport pipeline that will shortly replace our existing trucking operation, resulting in a safer and more efficient means of transportation. This is a good example of how we've been able to take an initiative that helps the local community and, with support from the Syrian government, the General Petroleum Corporation and the Syrian Petroleum Company, deliver a good outcome for the local community which has the added benefit of improving the overall efficiency and profitability of our operations.

Wherever sensibly possible to do so, we draw upon the skills available within the local communities

in which we operate, and we have also been especially successful in attracting experienced and foreign trained expatriate Syrians to return to Syria to work with us and pass on their skills and experience. Consequently the vast majority of the people who work for our Group, whether in Syria or elsewhere, are nationals of the respective country in which we are operating.

## Employee Training

Our employees are provided with access and encouragement to undertake technical training to the highest international standards and during the course of 2009 various members of our staff, particularly those working for us in Syria, have participated in advanced training programmes in many countries including the UK, the US, France, China, Croatia and Egypt. Gulfsands is well recognised locally for the efforts it has made to train local Syrians and is considered an employer of choice by for those graduating from Syria's universities.

We have recently begun to work with the General Petroleum Corporation, the Syrian Government's organisation charged with the responsibility of regulating and administering the oil and gas sector, to engage, and where appropriate, train a number of Syrian graduate geologists and engineers who have commenced working with the Syrian Petroleum Company. This joint programme has already provided our Group with a number of skilled employees and as the pool of highly trained technical staff continues to expand through this initiative, we expect to be able to hire many more of these talented individuals.

## Support for Charitable Causes

During 2009 Gulfsands expanded its commitment to support financially a number of social and charitable organisations active in the national, regional and local communities where we operate. As the principal focus of our operations is in Syria, we have focussed the majority of our effort in supporting programmes that are directed at improving the lives of children and disadvantaged members of Syrian society.

Syria is a relatively young nation with approximately 22% of the population between the ages of 15 and 24, either in the latter stages of their education or seeking employment for the first time. Following the President's well regarded initiative to expand public sector investment in education through the establishment of private secondary and tertiary institutions, there has been significant growth in the number of children attending and going on to graduate from secondary schools and universities throughout the country. The government is therefore targeting initiatives in partnership with the private sector to help reduce unemployment levels among skilled young people.

### *Education*

Gulfsands is working with a number of private sector sponsored organisations whose principal objectives are the provision of education support for the young and disadvantaged members of Syria's society and the development of business and life skills. These programmes will help young people stay in the education system longer so that they graduate with the kind of higher level skills required for better paid jobs or for starting their own businesses.

Many of these initiatives such as **FIRDOS**, **BIDAYA**, **SHABAB** and the **Syrian Young Scholars Programme** are directed at providing access to education and educational infrastructure. Examples include mobile libraries, computers and internet connectivity for rural communities, micro finance and technical and mentoring assistance for the development of self sustaining micro-businesses for young people and women in rural communities. These programmes have been shown to be effective in reducing poverty levels that currently average about 15%.

Gulfsands encourages its staff to personally volunteer their assistance and financial support for these organisations, most of which have developed extensive networks of volunteers. This personal support provides additional leverage for the financial contributions provided by Gulfsands.

*Handicapped Children*

Gulfsands and its management and staff also support other organisations working to improve the lives of sick and handicapped children, especially in the countryside areas outside Damascus.

We currently provide financial support for **BANA**, which educates and provides support for blind children, **AAMAL**, the Syrian association for the disabled, the **Syrian Association for Autistic Children,** which provides teaching and support facilities for children with learning difficulties, the **Light and Flowers Centre for Cerebral Palsy**, which provides education and teaching facilities for children, and the **Syria Trust for Development** which provides infrastructure and offers professional support to approximately 80 NGO's working in Syria, as well as a number of other worthy organisations.

*Child Healthcare*

Gulfsands is a significant supporter of **BASMA**, a voluntary organisation dedicated to providing support for children with cancer, particularly among the under-privileged. Gulfsands was the principal financial sponsor for the 16 bed **BASMA** paediatric oncology wing of the Al-Buruni University Hospital in Damascus, Syria's first paediatric oncology unit, which was officially opened by BASMA's patron and Syria's First Lady, Mrs Asma Al-Asaad, in September 2009. The facility had been accepting patients since April 2009 and is manned by 38 medical professionals. In 2009 it accepted 96 children as inpatients, handled almost 500 admissions and dealt with almost 1,000 outpatient visits, providing a level and quality of medical support and treatment for children that was previously unavailable in the country.

Gulfsands' financial assistance coupled with the tireless efforts of a team of volunteers that includes a number of Gulfsands employees, has enabled BASMA to expand its support for children with cancer to the Haematology and Oncology Unit at the larger Children's Hospital in Damascus. It also subsidises the oncology drugs that BASMA imports into Syria and makes available through its pharmacies now established at the Al-Buruni facility and at the Children's Hospital.

Through these initiatives approximately 430 children received treatment during 2009, bringing the number to almost 1,700 who have received BASMA supported treatment, including 50 children treated outside of Syria, since the organisation was established three years ago.

## Summary

We are delighted that the financial contribution we have made to these organisations has enabled them to make significant progress with their ambitions to improve the lives of Syria's people. Combined with the volunteering efforts and personal financial contributions of many of our staff, these initiatives have enhanced the reputation that the Group enjoys in Syria for corporate citizenship, responsiveness to issues affecting the communities in which we operate, and respect for the privileged position we enjoy as operators of Block 26 in Northeast Syria.

In expanding our business activities within Syria and beyond, we will look to build on our strong record of corporate social responsibility. Gulfsands' Board of Directors is committed to building on our early initiatives in Syria and Iraq so as to create a legacy from our presence in Syria and eventually Iraq that includes the sustainable long term economic development of the local communities where we operate.

Maintaining a strong record of achievement for corporate social responsibility will ensure we remain welcome operators in Syria while also providing an important reference of our record in this area of increasing importance to the governments we are dealing with in seeking new business opportunities in Iraq and other countries in the region.

The Directors present their report together with the audited financial statements of Gulfsands Petroleum plc and its subsidiary undertakings ("the Group" or "the Company" or "Gulfsands") for the year ended 31 December 2009.

**PRINCIPAL ACTIVITY**

The Group was established in October 1997. The Company was incorporated in England on 2 December 2004 as a public company limited by shares, and became the parent company of the Group in March 2005 as a result of a corporate reorganisation. In April 2005 the Company was listed on the Alternative Investment Market ("AIM") of the London Stock Exchange.

The Group's principal activity is that of oil and gas production, exploration and development. The Group has development and exploration projects in the Syrian Arab Republic and a non-operated portfolio of producing oil and gas properties in the USA (offshore Gulf of Mexico and onshore Gulf Coast). The Group also has business development activities in Iraq. In March 2010 the Group announced farm-in agreements to two permits in and offshore Tunisia.

**REVIEW OF THE BUSINESS AND FUTURE PROSPECTS**

The Group is required by the Companies Act 2006 to set out in this report a review of the business for the year ended 31 December 2009. A full review of the Group's operations, performance and prospects is set out in the following sections of this report:


| | Pages |
|---|---|
| The Chairman's statement | 6 – 7 |
| The Chief Executive's statement | 9 – 11 |
| The Operations review | 15 – 20 |
| The Financial review | 23 – 28 |
| The Corporate social responsibility review | 34 – 37 |
| The Directors remuneration Report | 45 – 47 |


**KEY PERFORMANCE INDICATORS**

During the year ended 31 December 2009 the Directors adopted certain financial and non-financial Key Performance Indicators ("KPIs") for 2009 with which to measure performance of the Group during the current financial year. Definitions of these KPIs plus the outcome for the year are contained in the section "Key Performance Indicators" on page 5.

## RESULTS AND DIVIDENDS

The Group made a profit after taxation for the year ended 31 December 2009 of $27.8 million (2008 as restated: $5.4 million loss). Earnings before interest, taxation, depreciation, impairment and share based payment charges was $48.9 million (2008 as restated: $15.7 million). The Directors do not recommend payment of a dividend.

## GROUP STRUCTURE AND CHANGES IN SHARE CAPITAL

There were no changes in the Group structure during 2009. Details of movements in the Company's share capital during the year are set out in note 21 to the financial statements.

## DIRECTORS AND THEIR INTERESTS

The Directors who served during the year and their interests in the Company's shares were as follows:

| | **At 31 December 2009** | | At 31 December 2008 | |
|---|---|---|---|---|
| | **Number of ordinary shares** | **Number of share options** | Number of ordinary shares | Number of share options |
| A T West | **-** | **1,200,000** | - | 1,200,000 |
| M Sajjad [1] | **8,205,268** | **1,450,000** | 9,588,601 | 1,450,000 |
| R Malcolm | **-** | **1,500,000** | - | 1,500,000 |
| A Rose | **400,000** | **1,000,000** | 300,000 | 1,000,000 |
| K Judge [2] | **3,966,750** | **1,000,000** | 3,966,750 | 1,000,000 |
| D Cowan | **441,750** | **525,000** | 441,750 | 525,000 |

(1) The interest for Mr Sajjad disclosed above includes shares held by Nordman Continental S.A., a company owned by a trust of which Mr Sajjad's children are potential beneficiaries.

(2) The interest for Mr Judge disclosed above includes shares held by Hamilton Capital Partners Limited, a company of which Mr Judge is a director.

## ISSUE OF SHARE OPTIONS

Details of share options issued, lapsed and exercised during the year ended 31 December 2009 are set out in note 21 to the financial statements.

## DIRECTORS' INTEREST IN TRANSACTIONS

Details of transactions with Directors for the year ended 31 December 2009 are set out in note 27 to the financial statements.

## INTERNAL CONTROLS

The Board is responsible for identifying and evaluating the major business risks faced by the Group and for determining and monitoring the appropriate course of action to manage these risks. Further information relating to the Group's Corporate Governance policies is shown on pages 43 and 44.

## SUBSTANTIAL SHAREHOLDERS

The Company has been notified, in accordance with Chapter 5 of the FSA's Disclosure and Transparency Rules, of the following interests in its ordinary shares as at 23 March 2010 of 3% shareholders and above.

| Name | Number of shares | % of shares in isssue | % of shares in isssue |
|---|---|---|---|
| Schroder Investment Management | 25,901,311 | **21.40%** | 17.96% |
| Abdul Rahman Mohdabdullah Kayed | 11,500,000 | **9.50%** | 9.70% |
| Nordman Continental S.A. (1) | 8,655,268 | **7.15%** | 8.09% |
| Al-Mashrek Global Invest Ltd | 7,000,000 | **5.78%** | 7.68% |
| Hugh Sloan | 5,007,240 | **4.14%** | 5.91% |
| George Robinson | 5,000,000 | **4.13%** | 4.61% |
| Hamilton Capital Partners Limited (2) | 3,966,750 | **3.28%** | 4.36% |

(1) Nordman Continental S.A. is owned by discretionary trusts of which Mr Sajjad's children are potential beneficiaries.
(2) Hamilton Capital Partners Limited is an associated company of Mr Judge.

## PRINCIPAL RISKS AND UNCERTAINTIES FACING THE GROUP

The business of oil and gas exploration involves a high degree of risk which a combination of experience, knowledge and careful evaluation may not be able to prevent. The Board has established a process for identifying and evaluating the principal risks and uncertainties facing the Group and a summary of these risks and uncertainties, together with measures taken to mitigate them, is contained on pages 29 - 31.

## SUPPLIERS' PAYMENT POLICY

It is the Group's policy that payments to suppliers are made in accordance with those terms and conditions agreed between the Group and its suppliers, provided that all trading terms and conditions have been complied with. The Group's average creditors' payment period at 31 December 2009 was 34 days.

## RISK MANAGEMENT OBJECTIVES AND POLICIES

Gulfsands' approach to financial risk management is described in the Financial Review on pages 23 – 28 and in the Principal Risks and Uncertainties section on pages 29 -31. Further disclosure is made in note 26 to the Financial Statements including the Group's exposure to price, credit, liquidity and currency risk.

## POLITICAL AND CHARITABLE CONTRIBUTIONS

There were no political contributions made by the Group during the years ended 31 December 2009 and 2008. The Group has a policy of making social contributions in its areas of operations where it will impact directly in the local communities. Further details are included in the Corporate social responsibility report on pages 34 - 37. Approximately $238,000 was provided to community programmes undertaken in Syria during 2009 (2008: $175,000).

## ANNUAL GENERAL MEETING

The Company's Annual General Meeting will be held on 27 May 2010 at 11am. The Notice of the Meeting, which sets out the resolutions to be proposed, accompanies this Annual Report and Financial Statements.

## GOING CONCERN

The Group's business activities, financial performance, financial position and risks are set out in the Operations review and the Financial Review. The financial position of the Group, its cash flows, liquidity position and resources are detailed in these reviews and further details are included in the financial statements. The Group has significant cash resources, no debt and forecasts surplus cash being generated in 2010 and the first half of 2011. After making appropriate enquiries and examining those areas which could give rise to financial exposure the Directors are satisfied that no material or significant exposures exist and that the Group and Company has adequate resources to continue its operations for the foreseeable future, despite the current uncertain economic environment. For this reason the Directors continue to adopt the going concern basis in preparing the financial statements.

## INFORMATION TO SHAREHOLDERS

The Group has its own website (www.gulfsands.com) for the purposes of improving information flow to shareholders and potential investors.

## STATEMENT OF RESPONSIBILITIES OF THOSE CHARGED WITH GOVERNANCE

The Directors are responsible for preparing the financial statements in accordance with applicable laws and International Financial Reporting Standards ("IFRSs") as adopted by the European Union.

Company law requires the Directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company and Group and of the profit or loss of the Group for that year. In preparing those financial statements, the directors are required to:

- properly select and apply accounting policies;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements in IFRSs are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Group's financial position and financial performance; and
- make an assessment of the Company's ability to continue as a going concern.

The Directors confirm that the financial statements comply with the above requirements.

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

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

**STATEMENT OF DISCLOSURES TO THE AUDITORS**

So far as the Directors, at the time of approval of their report, are aware:

- there is no relevant audit information of which the Company's auditors are unaware; and
- each Director has taken steps that they ought to have taken to make themselves aware of any relevant audit information and to establish that the auditors are aware of that information.

This confirmation is given and should be interpreted in accordance with Section 418 of the Companies Act 2006.

**AUDITORS**

During the year the Directors appointed Deloitte LLP as auditors of the Company to replace UHY Hacker Young. A resolution to reappoint Deloitte LLP as auditors and that the Directors be authorised to fix their remuneration will be put to shareholders at the Annual General Meeting.

By order of the Board

Richard Malcolm

**Chief Executive Officer**

Andrew Rose

**Chief Financial Officer**

29 March 2010

## DIRECTORS' CORPORATE GOVERNANCE REPORT FOR THE YEAR ENDED 31 DECEMBER 2009

Gulfsands Petroleum plc is committed to meeting high standards of corporate governance and acting responsibly in all the Company's business activities. The Company is committed to maintaining throughout the Group the highest standards of business conduct and ethics, as well as full compliance with all applicable government laws, rules and regulations, corporate reporting and disclosure, accounting practices, accounting controls, auditing practices and other matters relating to fraud against shareholders.

The Company has established appropriate subcommittees, adopted an Audit Committee Charter, a Code of Business Conduct and Ethics, a Whistleblower Policy and has also established a formal Health, Safety & Environment ("HSE") Policy.

### AUDIT COMMITTEE

The Audit Committee meets at least twice each year to discuss the review of the interim financial statements and the audit of the year-end Financial Statements. For the annual results the independent auditors are invited to discuss the conclusions arising from their audit and their assessment of the Group's internal controls. The Audit Committee also reviews annually, in detail, the risks and uncertainties facing the Group prior to the submission of the annual risk report to the Board. The Chairman of the Audit Committee is Andrew West and the other participating members of the committee are David Cowan and Kenneth Judge.

The activities of the Audit Committee are governed by an Audit Committee Charter which addresses the mandate of the Committee, its composition, independence and expertise of the members, frequency of meetings, roles and responsibilities which include oversight of the external audit function, internal controls, financial reporting, and the provision by the auditors of non-audit services. The Audit Committee has the power to engage such external advisers as it deems necessary to discharge its responsibilities.

### REMUNERATION COMMITTEE

The Remuneration Committee meets at least once per year and is responsible for setting the remuneration of the Board of Directors, including any pension and share incentive plan awards, and for establishing guidelines for the remuneration of staff in general, with closer scrutiny of the remuneration of senior management. The Chairman of the Remuneration Committee is David Cowan and the other participating member is Andrew West.

### CODE OF BUSINESS CONDUCT AND ETHICS

The Company has adopted a Code of Business Conduct and Ethics which addresses the workplace environment (including non-discrimination, harassment, substance abuse, violence and employment of family members), HSE, relationships with third parties (including conflicts of interest, gifts and entertainment, competitive practices, supplier and contractor relationships, public relations and governmental relations), legal compliance, information and records, use and misuse of company assets and reporting of violations.

## WHISTLEBLOWER POLICY

The Company has adopted a Whistleblower Policy. Pursuant to its charter, the Audit Committee is responsible for ensuring that a confidential and anonymous process exists whereby persons can report any matter relating to the Company and its subsidiaries which, in the view of the complainant, is illegal, unethical, contrary to the policies of the Company or in some other manner not right or proper.

All Directors, officers, employees, consultants and contractors of the Company and its subsidiaries are made aware of the Policy and a copy of the Policy has been distributed to Directors, officers and employees. All Directors, officers and employees will be informed whenever significant changes are made and new Directors, officers and employees will be provided with a copy of this Policy and educated about its importance.

## HEALTH, SAFETY & ENVIRONMENT ("HSE") POLICY

A primary goal of the Group is the protection of Health, Safety and Environment ("HSE"). The Group is dedicated to continuous efforts to make its operations compatible with protecting people, property and the environment.

This policy, whose implementation is overseen by the Chief Executive Officer, governs the Group's operations and is specifically designed to:

- comply with and exceed relevant HSE legislation, regulations and other requirements;
- maintain and develop systems to identify, assess, monitor, review and control HSE issues;
- set HSE objectives and targets;
- implement mechanisms to communicate with and to obtain input from employees, contractors, partners and associates;
- coordinate HSE policy, including the HSE management systems of contractors, to provide a unified system to guide operations; and
- institute a site-specific Emergency Response Procedure ("ERP") so that immediate actions are taken, without delay, to minimize danger to personnel, the environment and property. ERPs will be rehearsed prior to commencing operations to ensure that personnel make the appropriate responses in the event of emergency.

It is the policy of the Group to consider the health and welfare of employees by maintaining a safe place and system of work as required by the Safety, Health and Welfare at Work Act, 1989.

The Group closely monitors activities to ensure to the best of its knowledge there is not potential for any such breach. There have been no convictions in relation to breaches of these Acts recorded against the Group during the reporting year.

## REGULAR BOARD MEETINGS

The Board of Directors holds scheduled Board Meetings approximately six times per year plus such other ad-hoc meetings as are deemed necessary to deal with urgent business matters.

## DIRECTORS' REMUNERATION REPORT FOR THE YEAR ENDED 31 DECEMBER 2009

This report has been prepared having regard to Schedule 8 to the Accounting Regulations under the Companies Act 2006, which requires the Auditors to report to a company's shareholders on the auditable part of the Directors' Remuneration Report and to state whether in their opinion that part of the report has been properly prepared. The report has therefore been divided into separate sections for audited and unaudited information.

The report has been prepared by the Remuneration Committee and has been approved by the Board for submission to shareholders.

### Unaudited Information

Remuneration Policy

Up to and including the end of the 2008 financial year no remuneration policy was in place for Directors or staff. No formal appraisals of staff performance were carried out, and no formal studies had been undertaken to ensure that the remuneration of key staff was competitive with their industry peer group.

Bonuses paid to Directors in 2009 represented contractually agreed amounts upon the completion of one year's service. There are no further such bonuses payable.

During 2009 the Board engaged Hewitt New Bridge Street as remuneration consultants to review the Group's remuneration structure generally, to undertake a benchmarking exercise for Directors and senior staff, and to make recommendations regarding bonus and share incentive plan structure and policy going forward.

A new Remuneration Policy was adopted during the year, which provided for, inter alia, formal annual reviews of individual staff performance and goal-setting, the establishment of bands of eligible bonus and share plan awards relative to salary for each separate grade of employee (with the actual award within these bands being determined on merit), and the benchmarking of remuneration against peer group comparables at least once every two years.

A new Restricted Share Plan ("RSP") was established to complement the existing Share Option Plan ("SOP"): the intention being that future share incentive awards for all but the most senior staff should be in the form of restricted (deferred) shares and that share option awards be confined only to directors and the most senior staff. This will reduce the dilution to shareholders arising from future share incentive awards. Whereas the Company's general practice in the past had been for all share incentive awards to vest immediately, under the Remuneration Policy future awards under the RSP or SOP will have a vesting period except in exceptional circumstances.

**Audited Information**

Remuneration of Directors

The remuneration of the Directors for the year ended 31 December 2009 was as follows:

| | Annual remuneration ($000) | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Salary and fees | | Bonuses | | Benefits in kind | | Compensation for loss of office | | Total | |
| | **2009** | 2008 | **2009** | 2008 | **2009** | 2008 | **2009** | 2008 | **2009** | 2008 |
| A T West | **195** | 268 | **-** | 49 | **-** | - | **-** | - | **195** | 317 |
| M Sajjad | **538** | 519 | **-** | 1,681 | **25** | 53 | **-** | - | **563** | 2,253 |
| R Malcolm (1) | **428** | 97 | **208** | - | **5** | - | **-** | - | **641** | 97 |
| A Rose (2) | **338** | 160 | **165** | - | **8** | 4 | **-** | - | **511** | 164 |
| K Judge | **264** | 284 | **-** | 19 | **-** | - | **-** | - | **264** | 303 |
| D Cowan (3) | **77** | 91 | **-** | - | **-** | - | **-** | - | **77** | 91 |
| J Dorrier (4) | **-** | 96 | **-** | - | **-** | 25 | **-** | 444 | **-** | 565 |
| D DeCort (4) | **-** | 83 | **-** | - | **-** | 45 | **-** | 399 | **-** | 527 |
| | **1,840** | 1,598 | **373** | 1,749 | **38** | 127 | **-** | 843 | **2,251** | 4,317 |

(1) Appointed as a director on 15 October 2008
(2) Appointed as a director on 1 June 2008
(3) Non-executive director
(4) Resigned on 23 April 2008

In addition to the above, in 2005 the Group entered into an agreement with Mr Dorrier and Mr DeCort to bear the interest payable to the Internal Revenue Service of the United States of America ("IRS") on taxable gains arising as a result of the acquisition of Gulfsands Petroleum Limited by Gulfsands Petroleum Plc prior to the listing of the Company on the AIM market, but rolled over as permitted under the IRS rules. This interest became payable upon the disposal by Mr Dorrier and Mr DeCort of shares in Gulfsands Petroleum Plc, which occurred during 2009. This interest, and the tax thereon, equates to approximately $427,000 in respect of Mr Dorrier and $313,000 in respect of Mr DeCort and was paid in January 2010.

In addition to the remuneration shown above the Group incurred share based payment charges of $824,000 (2008 - $10,725,000) in respect of the above named Directors.

## Share options

The interests of the Directors in options over the Company's shares are set out in the table below:

| | Number of options | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | At 1 January 2009 | Granted | Exercised | Lapsed | At 31 December 2009 | Exercise price (£) | Market price at date of exercise (£) | Gain on exercise of options ($000) | Date from which exercisable | Expiry date |
| AT West | 125,000 | | | | 125,000 | 1.45 | | | 14/02/2006 | 13/02/2011 |
| | 75,000 | - | - | - | 75,000 | 1.04 | - | - | 25/07/2006 | 24/07/2011 |
| | 1,000,000 | | | | 1,000,000 | 1.88 | | | 13/05/2008 | 12/05/2013 |
| M Sajjad [(1)] | 450,000 | - | - | - | 450,000 | 1.30 | - | - | 05/04/2005 | 04/04/2010 |
| | 1,000,000 | | | | 1,000,000 | 1.88 | | | 13/05/2008 | 12/05/2013 |
| R Malcolm | 750,000 | | | | 750,000 | 1.86 | | | 15/10/2008 | 14/10/2013 |
| | 375,000 | - | - | - | 375,000 | 1.86 | - | - | 15/10/2009 | 14/10/2013 |
| | 375,000 | | | | 375,000 | 1.86 | | | 15/10/2010 | 14/10/2013 |
| A Rose | 500,000 | | | | 500,000 | 1.80 | | | 08/05/2008 | 07/05/2013 |
| | 250,000 | - | - | - | 250,000 | 1.80 | - | - | 08/05/2009 | 07/05/2013 |
| | 250,000 | | | | 250,000 | 1.80 | | | 08/05/2010 | 07/05/2013 |
| K Judge | 400,000 | - | - | - | 400,000 | 0.96 | - | - | 18/10/2006 | 17/10/2011 |
| | 600,000 | | | | 600,000 | 1.88 | | | 13/05/2008 | 12/05/2013 |
| D Cowan | 125,000 | - | - | - | 125,000 | 1.45 | - | - | 14/02/2006 | 13/02/2011 |
| | 400,000 | | | | 400,000 | 1.88 | | | 13/05/2008 | 12/05/2013 |

(1) Share option details shown above include options granted to Nordman Continental S.A., a company owned by discretionary trusts of which Mr Sajjad's children are potential beneficiaries.

This report was approved by the Board of Directors on 29 March 2010.

David Cowan

Chairman of the Remuneration Committee

29 March 2010

## INDEPENDENT AUDITORS' REPORT

## TO THE SHAREHOLDERS OF GULFSANDS PETROLEUM PLC

We have audited the financial statements of Gulfsands Petroleum Plc for the year ended 31 December 2009 which comprise the Consolidated income statement, the Consolidated and Company balance sheets, the Consolidated and Company cash flow statements, the Consolidated and Company statements of changes in equity and the related notes 1 to 30. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards ("IFRSs") as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006.

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

### Respective responsibilities of directors and auditors

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

### Scope of the audit of the financial statements

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

### Opinion on financial statements

In our opinion:

- the financial statements give a true and fair view of the state of the Group's and the Parent Company's affairs as at 31 December 2009 and of the Group's profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union;

- the Parent Company financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

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

In our opinion:

- the part of the Directors' remuneration report to be audited has been properly prepared in accordance with the provisions of the Companies Act 2006 that would have applied were the company a quoted company; and
- the information given in the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements.

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

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

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

David Paterson (Senior Statutory Auditor)

for and on behalf of Deloitte LLP

Chartered Accountants and Statutory Auditors

London, United Kingdom

29 March 2010

## CONSOLIDATED INCOME STATEMENT
## FOR THE YEAR ENDED 31 DECEMBER 2009

| | Notes | 2009 $' 000 | 2008 (restated) $' 000 |
|---|---|---|---|
| **Revenue** | 6 | **84,415** | 53,600 |
| Cost of sales | | | |
| Depletion | | **(12,289)** | (8,165) |
| Impairment | | **(6,420)** | (1,655) |
| Other cost of sales | | **(19,250)** | (17,567) |
| Total cost of sales | | **(37,959)** | (27,387) |
| **Gross profit** | | **46,456** | 26,213 |
| General administrative expenses | | **(14,947)** | (13,033) |
| Foreign exchange gains / (losses) | | **538** | (4,729) |
| Share based payments | 7 | **(1,124)** | (12,572) |
| Total administrative expenses | | **(15,533)** | (30,334) |
| Other operating expenses - hurricane repairs | 8 | **(2,316)** | (2,750) |
| **Operating profit / (loss)** | 9 | **28,607** | (6,871) |
| Discount expense on decommissioning provision | 20 | **(1,056)** | (1,667) |
| Net interest income | 10 | **293** | 1,229 |
| **Profit / (loss) before taxation** | | **27,844** | (7,309) |
| Taxation | 11 | **(12)** | 1,932 |
| **PROFIT / (LOSS) FOR THE YEAR - attributable to equity holders of the Company** | | **27,832** | (5,377) |
| **Earnings / (Loss) per share (cents):** | | | |
| Basic | 12 | **23.32** | (4.65) |
| Diluted | 12 | **23.06** | (4.65) |

The profit and loss for 2009 and 2008 relate entirely to continuing operations. There are no items of comprehensive income not included in the income statement.

Comparatives have been adjusted in accordance with IAS 1 "Presentation of Financial Statements – Revised", as described in notes 2 and 30.

## CONSOLIDATED BALANCE SHEET
## AS AT 31 DECEMBER 2009

| | Notes | **2009** $'000 | 2008 (restated) $'000 | 2007 (restated) $'000 |
|---|---|---|---|---|
| **ASSETS** | | | | |
| **Non-current assets** | | | | |
| Property, plant and equipment | 13 | **82,569** | 77,055 | 42,631 |
| Intangible assets | 14 | **7,091** | 343 | 28,593 |
| Long term financial assets | 17 | **11,990** | 13,167 | 16,078 |
| | | **101,650** | 90,565 | 87,302 |
| **Current assets** | | | | |
| Inventory - materials | | **4,165** | 2,401 | - |
| Trade and other receivables | 16 | **21,867** | 15,536 | 11,154 |
| Cash and cash equivalents | 17 | **57,623** | 36,812 | 18,533 |
| | | **83,655** | 54,749 | 29,687 |
| **Total Assets** | | **185,305** | 145,314 | 116,989 |
| **LIABILITIES** | | | | |
| **Current liabilities** | | | | |
| Trade and other payables | 18 | **13,411** | 11,245 | 6,672 |
| Provision for decommissioning | 20 | **3,683** | 5,877 | 10,952 |
| | | **17,094** | 17,122 | 17,624 |
| **Non-current liabilities** | | | | |
| Deferred tax liabilities | 19 | **-** | - | 1,932 |
| Provision for decommissioning | 20 | **27,937** | 20,430 | 16,824 |
| | | **27,937** | 20,430 | 18,756 |
| **Total Liabilities** | | **45,031** | 37,552 | 36,380 |
| **NET ASSETS** | | **140,274** | 107,762 | 80,609 |
| **EQUITY** | | | | |
| **Capital and reserves attributable to equity holders** | | | | |
| Share capital | 21 | **12,971** | 12,814 | 11,997 |
| Share premium | | **101,929** | 98,530 | 79,389 |
| Share-based payments reserve | | **15,429** | 14,305 | 1,733 |
| Merger reserve | | **11,709** | 11,709 | 11,709 |
| Retained losses | | **(1,764)** | (29,596) | (24,219) |
| **TOTAL EQUITY** | | **140,274** | 107,762 | 80,609 |

Comparatives have been adjusted in accordance with IAS 1 "Presentation of Financial Statements – Revised", as described in notes 2 and 30.

These financial statements were approved by the Board of Directors on 29 March 2010 and signed on its behalf by:

Richard Malcolm
**Chief Executive Officer**

Andrew Rose
**Chief Financial Officer**

## COMPANY BALANCE SHEET
## AS AT 31 DECEMBER 2009

| | Notes | **2009 $'000** | 2008 $'000 |
|---|---|---|---|
| **ASSETS** | | | |
| **Non-current assets** | | | |
| Property, plant and equipment | 13 | **196** | 145 |
| Intangible assets | 14 | **121** | - |
| Investments in and loans to subsidiaries | 15 | **59,741** | 50,136 |
| | | **60,058** | 50,281 |
| **Current assets** | | | |
| Trade and other receivables | 16 | **4,485** | 33,911 |
| Cash and cash equivalents | 17 | **45,578** | 28,339 |
| | | **50,063** | 62,250 |
| **Total Assets** | | **110,121** | 112,531 |
| **LIABILITIES** | | | |
| **Current liabilities** | | | |
| Trade and other payables | 18 | **1,122** | 4,467 |
| **Total Liabilities** | | **1,122** | 4,467 |
| **NET ASSETS** | | **108,999** | 108,064 |
| **EQUITY** | | | |
| **Capital and reserves attributable to equity holders** | | | |
| Share capital | 21 | **12,971** | 12,814 |
| Share premium | | **101,929** | 98,530 |
| Share-based payments reserve | | **15,429** | 14,305 |
| Retained losses | | **(21,330)** | (17,585) |
| **TOTAL EQUITY** | | **108,999** | 108,064 |

The financial statements of Gulfsands Petroleum Plc (registered number: 05302880) were approved by the Board of Directors on 29 March 2010 and signed on its behalf by:

Richard Malcolm
**Chief Executive Officer**

Andrew Rose
**Chief Financial Officer**

**CONSOLIDATED STATEMENT OF CHANGES IN EQUITY**
**FOR THE YEAR ENDED 31 DECEMBER 2009**

| | Share capital $'000 | Share premium $'000 | Share based payments reserve $'000 | Merger reserve $'000 | Retained losses $'000 | Total equity $'000 |
|---|---|---|---|---|---|---|
| **Year ended 31 December 2009** | | | | | | |
| At 1 January 2009 | 12,814 | 98,530 | 14,305 | 11,709 | (29,596) | 107,762 |
| Options exercised | 157 | 3,399 | - | - | - | 3,556 |
| Share -based payment charge | - | - | 1,124 | - | - | 1,124 |
| Profit for 2009 | - | - | - | - | 27,832 | 27,832 |
| At 31 December 2009 | 12,971 | 101,929 | 15,429 | 11,709 | (1,764) | 140,274 |
| **Year ended 31 December 2008** | | | | | | |
| At 1 January 2008 (restated) | 11,997 | 79,389 | 1,733 | 11,709 | (24,219) | 80,609 |
| Options exercised | 194 | 1,224 | - | - | - | 1,418 |
| Shares issued | 623 | 17,917 | - | - | - | 18,540 |
| Share -based payment charge | - | - | 12,572 | - | - | 12,572 |
| Loss for 2008 (restated) | - | - | - | - | (5,377) | (5,377) |
| At 31 December 2008 (restated) | 12,814 | 98,530 | 14,305 | 11,709 | (29,596) | 107,762 |

The merger reserve arose on the acquisition of Gulfsands Petroleum Ltd and its subsidiaries by the Company by way of share-for-share exchange in April 2005, in conjunction with the flotation of the Company on the Alternative Investment Market of the London Stock Exchange.

**COMPANY STATEMENT OF CHANGES IN EQUITY**
**FOR THE YEAR ENDED 31 DECEMBER 2009**

| | Share capital $'000 | Share premium $'000 | Share based payments reserve $'000 | Merger reserve $'000 | Retained (losses) / earnings $'000 | Total equity $'000 |
|---|---|---|---|---|---|---|
| **Year ended 31 December 2009** | | | | | | |
| At 1 January 2009 | 12,814 | 98,530 | 14,305 | - | (17,585) | 108,064 |
| Options exercised | 157 | 3,399 | - | - | - | 3,556 |
| Share -based payment charge | - | - | 1,124 | - | - | 1,124 |
| Loss for 2009 | - | - | - | - | (3,745) | (3,745) |
| At 31 December 2009 | 12,971 | 101,929 | 15,429 | - | (21,330) | 108,999 |
| | | | | | | |
| **Year ended 31 December 2008** | | | | | | |
| At 1 January 2008 | 11,997 | 79,389 | 1,733 | - | 1,790 | 94,909 |
| Options exercised | 194 | 1,224 | - | - | - | 1,418 |
| Shares issued | 623 | 17,917 | - | - | - | 18,540 |
| Share -based payment charge | - | - | 12,572 | - | - | 12,572 |
| Loss for 2008 | - | - | - | - | (19,375) | (19,375) |
| At 31 December 2008 | 12,814 | 98,530 | 14,305 | - | (17,585) | 108,064 |

## CONSOLIDATED CASH FLOW STATEMENT
## FOR THE YEAR ENDED 31 DECEMBER 2009

| | *Notes* | **2009 $' 000** | 2008 (restated) $' 000 |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Operating profit / (loss) | | **28,607** | (6,871) |
| Depreciation, depletion and amortisation | 13 & 14 | **12,781** | 8,351 |
| Impairment charge | 13 | **6,420** | 1,655 |
| Decommissioning costs paid in excess of provision | 20 | **696** | 2,987 |
| Share-based payment charge | 7 | **1,124** | 12,572 |
| (Profit) / Loss on disposal of assets | | **(284)** | 9 |
| Increase in receivables | | **(6,239)** | (4,066) |
| Increase in payables | | **198** | 4,672 |
| **Net cash provided by operations** | | **43,303** | 19,309 |
| Interest received | | **293** | 1,229 |
| Taxation paid | | **(66)** | (524) |
| **Net cash provided by operating activities** | | **43,530** | 20,014 |
| **Investing activities** | | | |
| Exploration and evaluation expenditure | | **(5,358)** | (1,762) |
| Oil and gas properties expenditure | | **(18,082)** | (13,952) |
| Increase in inventory | | **(1,764)** | (2,401) |
| Disposal of oil and gas assets | | **455** | - |
| Other capital expenditures | | **(630)** | (923) |
| Change in long term financial assets | 17 | **1,177** | 2,911 |
| Decommissioning costs paid | 20 | **(2,073)** | (5,566) |
| **Net cash used in investing activties** | | **(26,275)** | (21,693) |
| **Financing activities** | | | |
| Cash proceeds from issue of shares | | **3,556** | 19,958 |
| **Net cash provided by financing activities** | | **3,556** | 19,958 |
| **Increase in cash and cash equivalents** | | **20,811** | 18,279 |
| Cash and cash equivalents at beginning of year | | **36,812** | 18,533 |
| Cash and cash equivalents at end of year | 17 | **57,623** | 36,812 |

Comparatives have been adjusted in accordance with IAS 1 “Presentation of Financial Statements – Revised”, as described in notes 2 and 30.

## COMPANY CASH FLOW STATEMENT
## FOR THE YEAR ENDED 31 DECEMBER 2009

| | *Notes* | **2009 $' 000** | 2008 $' 000 |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Operating loss | | **(7,827)** | (23,627) |
| Depreciation and amortisation | 13 & 14 | **141** | 17 |
| Share-based payment charge | 7 | **1,124** | 12,572 |
| Loss on disposal of assets | | **-** | 9 |
| Decrease / (increase) in receivables | | **29,426** | (26) |
| (Decrease) / increase in payables | | **(3,345)** | 4,397 |
| **Net cash provided by / (used in) operations** | | **19,519** | (6,658) |
| Interest received | | **4,082** | 4,252 |
| Taxation paid | | **-** | (413) |
| **Net cash provided by / (used in) operating activities** | | **23,601** | (2,819) |
| **Investing activities** | | | |
| Other capital expenditures | | **(313)** | (158) |
| Loans to subsidiaries | 15 | **(9,605)** | (3,473) |
| **Net cash used in investing activties** | | **(9,918)** | (3,631) |
| **Financing activities** | | | |
| Cash proceeds from issue of shares | | **3,556** | 19,958 |
| **Net cash provided by financing activities** | | **3,556** | 19,958 |
| **Increase in cash and cash equivalents** | | **17,239** | 13,508 |
| Cash and cash equivalents at beginning of year | | **28,339** | 14,831 |
| Cash and cash equivalents at end of year | 17 | **45,578** | 28,339 |

## 1. Authorisation of financial statements and statement of compliance with IFRSs

Gulfsands Petroleum plc is a public limited company listed on the Alternative Investment Market (AIM) of the London Stock Exchange and incorporated in the United Kingdom. The principal activities of the Company and its subsidiaries (the Group) is that of oil and gas production, exploration, and development.

The Group's financial statements for the year ended 31 December 2009 were authorised for issue by the Board of Directors on 29 March 2010 and the balance sheets were signed on the Board's behalf by Richard Malcolm and Andrew Rose.

The Company's and Group's financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as adopted by the European Union. The principal accounting policies adopted are set out in note 3 below.

## 2. Adoption of International Financial Reporting Standards and correction of errors in prior periods

The Company's and Group's financial statements for the year ended 31 December 2009 and for the comparative year ended 31 December 2008 have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union and IFRIC (International Financial Reporting Interpretations Committee) interpretations and with those parts of the Companies Act 2006 applicable to companies reporting under IFRS.

The Group has restated the Income statements, Balance sheets and Cash flow statements as reported for prior periods. In prior periods the Group had erroneously classified certain repair costs as capital expenditure for its Gulf of Mexico assets for the periods ended 31 December 2006 to 31 December 2008. As a consequence depletion, impairment costs and other costs of sales recorded in these periods have been misstated. Further details of these restatements are shown in note 30. In addition the Group has restated certain cash flows relating to capital investments from operating activities to investing activities within the Consolidated cash flow statement.

## 3. Significant accounting policies

### 3.1 Basis of preparation and accounting standards

The Group's significant accounting policies used in the preparation of the financial statements are set out below.

The consolidated financial statements have been prepared in accordance with applicable International Financial Reporting Standards as adopted by the European Union and, except for share-based payments, under the historical cost convention. They have also been prepared on the going concern basis of accounting, for the reasons set out in the 'Going concern' section of the Directors report.

These financial statements consolidate the accounts of Gulfsands Petroleum plc and all its subsidiary undertakings drawn up to 31 December each year.

In the Group financial statements, merged subsidiary undertakings are treated as if they had always been a member of the Group. The results of such subsidiaries are included for the whole year in the year they join the Group.

### 3.2 Basis of consolidation

Intra-group sales, profits and balances are eliminated fully on consolidation.

The results of other subsidiaries acquired or sold are consolidated for the periods from or to the date when control passed. Acquisitions are accounted for under the purchase method, under which purchase consideration is allocated to the assets and liabilities on the basis of fair value at the date of acquisition.

The consolidated financial statements include the accounts of subsidiary undertakings when the Company has the power to exercise, or actually exercises, dominant influence or control over the undertaking.

The Group is engaged in oil and gas exploration, development and production through incorporated and unincorporated joint ventures (together “Jointly Controlled Entities”). The Group accounts for its share of the results and net assets of these Jointly Controlled Entities using the proportional consolidation method.

No individual income statement is presented in respect of the Company as permitted by section 408 of the Companies Act 2006. The Company’s loss for the year was $3,745,000 (2008 – loss of $19,375,000). There are no items of comprehensive income of the Company not included in the loss noted above.

### 3.3 Reporting currency

These financial statements are presented in U.S. Dollars. The Company’s operations and the majority of all costs associated with foreign operations are paid in U.S. Dollars and not the local currency of the operations. Therefore the presentational and functional currency of the Company and of the Group, and the functional currency of all subsidiaries, is the U.S. Dollar. Gains and losses from foreign currency transactions, if any, are recognised in the income statement for the year. The effective exchange rate to the Pound Sterling at 31 December 2009 was £1: US $1.66 (2008 – £1: US $1.45).

### 3.4 Oil and gas assets

The Group applies the requirements of IFRS 6 ’Exploration for and Evaluation of Mineral Resources’ and where additional guidance is needed IAS 16 ’Property, Plant and Equipment’ and IAS 36 ’Impairment of Assets’ noting that several items in the latter two standards are exempted for assets at the exploration and evaluation stage due to the application of IFRS 6. Set out below is our interpretation of the principles set out in IFRS 6 and other IFRSs.

There are two categories of oil and gas assets, exploration and evaluation assets which are included in Intangible assets, and development and production assets which are included in Property, plant and equipment.

***Oil and gas assets: exploration and evaluation***

*Recognition and measurement*

Exploration and evaluation (E&E) assets consist of costs of license acquisition, exploration, evaluation, appraisal and development activities and evaluating oil and gas properties. The cost of E&E assets includes capitalised overheads relevant to the exploration and evaluation up to the point of commercial discovery. Costs incurred prior to having obtained the legal rights to explore an area (pre-license costs) are expensed directly to the income statement as they are incurred and are not included in E&E assets. E&E costs are accumulated and capitalised into cost pools and added to Intangible assets pending determination of commercial reserves.

E&E assets relating to each exploration license/prospect are not amortised but are carried forward until the existence or otherwise of commercial reserves has been determined. If commercial reserves have been discovered, the related E&E assets are assessed for impairment on a cash generating unit basis as set out below and any impairment loss is recognised in the income statement. The carrying value of the E&E assets, after any impairment loss, is then reclassified as development and production assets in Property, plant and equipment.

*Impairment*

E&E assets are assessed for impairment when facts and circumstances suggest that the carrying amount may exceed its recoverable amount. Such indicators include the point at which a determination is made as to whether commercial reserves exist.

Where the E&E assets concerned fall within the scope of a cash generating unit, the E&E assets are tested for impairment together with all development and production assets associated within the cash generating unit. The aggregate carrying value is compared against the expected recoverable amount of the pool, generally by reference to the present value of the future net cash flows expected to be derived from production of commercial reserves. Where the E&E assets to be tested fall outside the scope of a cash generating unit, there will generally be no commercial reserves and the E&E assets concerned will generally be written off in full.

Any impairment loss is recognised in the income statement and is separately disclosed. In the balance sheet it is recorded against the carrying value of the related E&E asset.

***Oil and gas assets: development and production***

Tangible oil and gas assets are grouped into a cash generating unit or groups of units for purposes of impairment testing and for depreciating the development and production assets. A cash generating unit is the smallest unit that does not have inter-related revenues and may be a well, field, area, block, region, or other defined area as appropriate. Inter-relationships can be measured by oil and gas production agreements, geological analysis, or other documentation showing such relationships. The only limitation in the size of a cash generating unit is that it cannot be larger than an operating segment of the Group.

*Recognition and measurement*

Development and production assets are accumulated on a cash generating unit basis and represent the cost of developing the commercial reserves discovered and bringing them into production, together with the E&E expenditures incurred in finding commercial reserves transferred from intangible E&E assets.

The cost of development and production assets also includes the cost of acquisitions and purchases of such assets, directly attributable overheads, and the cost of recognising provisions for future restoration and decommissioning.

*Depletion of producing assets*
Expenditure within each cash generating unit is depleted by a unit of production method using the ratio of oil and gas production in the year compared to the estimated quantity of commercial reserves at the beginning of the year. Costs used in the unit of production calculation comprise the net book value of capitalised costs plus the estimated future field development costs for proved and probable reserves. Changes in estimates of commercial reserves or future development costs are dealt with prospectively.

*Impairment*
An impairment test is performed whenever events and circumstances arising during the development or production phase indicate that the carrying value of a development or production asset may exceed its recoverable amount. The aggregate carrying value is compared against the recoverable amount of the cash generating unit, generally by reference to the present value of the future net cash flows expected to be derived from production of commercial reserves.

**3.5 Decommissioning**
Where a material liability for the removal of 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. A fixed asset of an amount equivalent to the provision is also created (included in development and production assets) and depleted on a unit of production basis. Changes in estimates are recognised prospectively, with corresponding adjustments to the provision and the associated fixed asset.

**3.6 Definition of reserves**
The Group's definition of reserves is in accordance and consistent with the 2007 Petroleum Resources management System, as prepared by the Oil and Gas Reserves Committee of the Society of Petroleum Engineers ("SPE") and reviewed and jointly sponsored by the World Petroleum Council ("WPC"), the American Association of Petroleum Geologists and the Society of Petroleum Evaluation Engineers. The estimation of Proved (1P), Proved plus Probable (2P) and Proved plus Probable plus Possible (3P) commercially recoverable reserves are performed utilising relevant geological, geophysical and engineering data and with reference to the use of the probabilistic methodology as approved by SPE / WPC. The reserves are verified by a certified independent expert.

Proved plus Probable (2P) entitlement reserves are utilised as the basis for the Group's calculations of depletion and impairment as these represent the Group's estimate of the most likely commercially recoverable reserves as per the approved probabilistic methodology.

**3.7 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, less estimated residual value, of assets on a straight-line basis over their useful lives of between two and five years.

### 3.8 Intangible assets other than oil and gas assets

Intangible assets other than oil and gas assets are stated at cost less accumulated amortisation and any provision for impairment. Amortisation is charged so as to write off the cost, less estimated residual value, of assets on a straight-line basis over their useful lives of between two and five years. Amortisation is included with depreciation and classified as cost of sales or administrative expenses as appropriate. No intangible assets other than oil and gas assets have indefinite lives.

### 3.9 Revenue recognition

Sales revenue represents amounts invoiced exclusive of sales related taxes and royalties for the Group's share of oil and gas sales in the year. Oil and gas sales are recognised when goods are delivered and title has passed.

Interest income is accrued on a time basis, by reference to the principal outstanding and at the effective rate applicable.

### 3.10 Operating leases

Rentals payable under operating leases are charged to the income statement on a straight line basis over the lease term.

### 3.11 Taxation

Current tax, including UK corporation tax 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.

The liability method is used in accounting for deferred income taxes. Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted, or substantively enacted, tax rates and laws that will be in effect when the differences are expected to reverse. The recoverability of deferred tax assets is evaluated annually and an impairment provision is provided if it is more likely than not that the deferred tax asset will not give rise to future benefits in the Group's tax returns.

### 3.12 Derivative financial instruments

The Group has in the past used forward crude oil and gas sales contracts and swaps to reduce exposure to fluctuations in the price of crude oil and natural gas in order to reduce the volatility of the cash flows of the Group. Contracts are only entered into to hedge physical positions related to the Group's crude oil and natural gas production and are accordingly accounted for as hedge transactions. The Group has not entered into any such contracts during any of the periods presented.

### 3.13 Share based payments

The Company has made equity-settled share-based payments to certain employees and directors by way of issues of share options. The fair value of these payments is calculated at grant date by the Company using the Black-Scholes option pricing model excluding the effect of non market-based vesting conditions. The expense is recognised on a straight line basis over the period from the date of award to the date of vesting, based on the Company's best estimate of the number of options that will eventually vest. At each balance sheet date, the Company revises its estimates of the number of options expected to vest as a result of the effect of non market-based vesting

conditions. The impact of the revision of the original estimates, if any, is recognised in profit or loss such that the cumulative expense reflects the revised estimate, with a corresponding adjustment to the share based payments reserve.

**3.14 Cash and cash equivalents**

Cash and cash equivalents are carried in the balance sheet at cost and comprise cash in hand and deposits repayable on demand by banks and other short term investments with original maturities of three months or less. Balances held in bank accounts subject to escrow agreements as collateral for performance bonds issued are excluded from cash and cash equivalents and are shown as long term financial assets.

**3.15 Foreign currency**

Foreign currency transactions of individual companies within the Group are translated to the functional and reporting currency of US Dollars at the rates prevailing when the transactions occurred. Monetary assets and liabilities denominated in foreign currencies are translated at the rate of exchange at the balance sheet date. All differences are taken to the Income statement.

**3.16 Investments**

The Parent Company's investments in subsidiary companies are included in the Company Balance sheet at cost, less provision for any impairment.

**3.17 Inventories**

Inventories comprise materials and equipment, which are stated at the lower of cost and net realisable value. Cost includes all costs incurred in bringing the materials and equipment to its present condition and location.

**3.18 Trade receivables**

Trade receivables are carried at original invoice amounts less any provision made for impairment of receivables. A provision for impairment of trade receivables is made when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the debt.

**3.19 Trade payables**

Trade payables are not interest-bearing and are stated at their nominal values.

**3.20 Equity instruments**

Equity instruments issued by the Company, being any instruments with a residual interest in the assets of the Company after deducting all its liabilities, are recorded at the proceeds received, net of direct issue costs.

## 4. New IFRS standards and interpretations

In preparing the financial statements of the Group for the current year, the Group has adopted the following pronouncements of the IASB for the first time. These pronouncements have not had a material impact on the results or net assets of the Group.

- IFRS 8 'Operating Segments' was issued in October 2006 and defines operating segments as components of an entity about which separate financial information is available and is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. The new standard sets out the required disclosures for operating segments and is effective for annual periods beginning on or after 1 January 2009. The new standard has had no impact on the Group's reported income or net assets. The required disclosures are set out in note 6.
- In September 2007 the IASB issued Amendments to IAS 1 'Presentation of Financial Statements' – A Revised Presentation, which requires separate presentation of owner and non-owner changes in equity by introducing the statement of comprehensive income. Whenever there is a restatement or reclassification, an additional balance sheet, as at the beginning of the earliest period presented, will be required to be published. The revised standard is effective for annual periods beginning on or after 1 January 2009. There has been no effect on the Group's reported income or net assets from the adoption of IAS 1 Revised.

The financial statements have been prepared after adopting the following pronouncements from the IASB which have no effect on either the reported results and financial position or the presentation or disclosure within the financial statements.

| | |
|---|---|
| IAS 23 (revised 2007) Borrowing Costs | The principal change to the Standard was to eliminate the option to expense all borrowing costs when incurred. This change has had no impact on these financial statements because the Group has no material borrowing costs. |
| Amendments to IAS 32 Financial Instruments: Presentation and IAS 1 Presentation of Financial Statements – Puttable Financial Instruments and Obligations Arising on Liquidation | The revisions to IAS 32 amend the criteria for debt / equity classification. The Group has no such financial instruments. |
| Amendments to IAS 39 Financial Instruments: Recognition and Measurement – Eligible Hedged Items | The amendments provide clarification on two aspects of hedge accounting. The Group has no such hedged items. |
| Embedded Derivatives (Amendments to IFRIC 9 Reassessment of Embedded Derivatives and IAS 39 Financial Instruments: Recognition and Measurement) | The amendments clarify the accounting for embedded derivatives in light of IAS 39. The Group has no such embedded derivatives. |

| | |
|---|---|
| IFRIC 16 Hedges of a Net Investment in a Foreign Operation | The interpretation provides guidance on detailed requirements for net investment hedging. The Group has no such hedging. |

The following pronouncements from the IASB will become effective for future financial reporting periods and have not yet been adopted by the Group.

- In January 2008 the IASB issued a revised version of IFRS 3 'Business Combinations'. The revised standard still requires the purchase method of accounting to be applied to business combinations but will introduce some changes to existing accounting treatment. For example, contingent consideration is measured at fair value at the date of acquisition and subsequently remeasured to fair value with changes recognised in profit or loss. Goodwill may be calculated based on the parent's share of net assets or it may include goodwill related to the minority interest. All transaction costs are expensed. The standard is applicable to business combinations occurring in accounting periods beginning on or after 1 July 2009 and the Group plans to adopt it with effect from 1 January 2010. Assets and liabilities arising from business combinations occurring before the date of adoption by the Group will not be restated and thus there will be no effect on the Group's reported income or net assets on adoption.

- Also in January 2008 the IASB issued an amended version of IAS 27 'Consolidated and Separate Financial Statements'. This requires the effects of all transactions with non-controlling interests to be recorded in equity if there is no change in control. Such transactions will no longer result in goodwill or gains or losses. When control is lost, any remaining interest in the entity is remeasured to fair value and a gain or loss recognised in profit or loss. The amendment is effective for annual periods beginning on or after 1 July 2009 and is to be applied retrospectively, with certain exceptions. The Group plans to adopt the amendment with effect from 1 January 2010 and does not expect there to be any effect on the Group's reported income or net assets.

There are no other standards and interpretations in issue but not yet adopted that the Directors anticipate will have a material effect on the reported income or net assets of the Group.

**5. Critical accounting estimates and assumptions**

In the process of applying the Group's accounting policies, which are set out in note 3, the Directors have made the following judgements and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a risk of causing material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

*a) Intangible oil and gas exploration and evaluation costs*
Costs capitalised as intangible assets are assessed for impairment when circumstances suggest that the carrying value may exceed its recoverable value. This assessment involves judgement as to the

(i) likely commerciality of the assets, and (ii) future revenues and costs pertaining and the discount rate to be applied for the purpose of deriving a recoverable value.

*b) Decommissioning*

The Group has decommissioning obligations in respect of its producing interests in the Gulf of Mexico. 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. The Group has received a report from external specialist decommissioning experts regarding the cost of future works. The timing of these works is inherently uncertain and depends upon the determination of the end of commercial production. The Group has utilised the expected useful lives in the year end reserves report to estimate the timing of decommissioning liabilities. A risk free interest rate of 4% (2008 – 6%) has been used to discount the expected costs of decommissioning.

*c) Oil and gas development and production assets and reserves*

Oil and gas development and production assets held in property, plant and equipment are depleted on a unit of production basis calculated by reference to Proved and Probable (“2P”) reserves. The Group’s 2P reserves take the estimated future cost of developing and extracting those reserves into account.

Future forecast capital expenditure associated with developing proved and probable reserves is included in the cost base for the purposes of calculating depletion charges. 2P reserves are determined using estimates of oil and gas in place, recovery factors and future oil and gas prices. The carrying amount of oil and gas assets therefore depends upon a number of estimates at year end.

The level of 2P reserves is also a key determinant in assessing whether the carrying value of any of the Group’s oil and gas assets have been impaired.

**6. Total revenue and segmental information**

The total revenue of the Group, as defined by IAS 18, for 2009 was $84,741,000 (2008: $54,833,000) comprising sales of hydrocarbons and incidental income of $84,415,000 (2008: $53,600,000) and interest income of $326,000 (2008: $1,233,000).

As described in note 4, the Group adopted IFRS 8 ‘Operating Segments’ during the year. The adoption of IFRS 8 did not result in any changes to the segments required to be disclosed.

For management purposes, the Group operates in two geographical areas, the USA and Syria. Both segments are involved with production and exploration of oil and gas.

The Group revenue and results for the year is analysed by reportable segment as follows:

| | 2009 | | | |
|---|---|---|---|---|
| | **USA** | **Syria** | **Other** | **Total** |
| | **$' 000** | **$' 000** | **$' 000** | **$' 000** |
| Revenues from external parties | **13,962** | **70,453** | **-** | **84,415** |
| Inter-segment revenue | **648** | **-** | **382** | **1,030** |
| Total segment revenue | **14,610** | **70,453** | **382** | **85,445** |
| Depletion charges | **(2,372)** | **(9,917)** | **-** | **(12,289)** |
| Impairment | **(6,420)** | **-** | **-** | **(6,420)** |
| Hurricane repairs | **(2,316)** | **-** | **-** | **(2,316)** |
| Other cost of sales | **(14,023)** | **(5,227)** | **-** | **(19,250)** |
| General administrative expenses before depreciation | **(2,670)** | **(5,467)** | **(6,317)** | **(14,454)** |
| Inter-segment administrative expense | **-** | **(1,030)** | **-** | **(1,030)** |
| Depreciation and amortisation | **(16)** | **(329)** | **(148)** | **(493)** |
| Foreign exchange gains / (losses) | **-** | **(98)** | **636** | **538** |
| Share based payments | **-** | **-** | **(1,124)** | **(1,124)** |
| Profit / (loss) before interest and taxation | **(13,207)** | **48,385** | **(6,571)** | **28,607** |
| Interest expense and unwinding of discount | **(1,056)** | **-** | **(33)** | **(1,089)** |
| Interest income from external parties | **82** | **38** | **206** | **326** |
| Inter-segment interest | **(3,910)** | **-** | **3,910** | **-** |
| Taxation | **(10)** | **(2)** | **-** | **(12)** |
| Profit / (loss) for the year | **(18,101)** | **48,421** | **(2,488)** | **27,832** |

| | 2008 (restated) | | | |
|---|---|---|---|---|
| | USA | Syria | Other | Total |
| | $' 000 | $' 000 | $' 000 | $' 000 |
| Revenues from external parties | 28,121 | 25,479 | - | 53,600 |
| Inter-segment revenue | 127 | - | - | 127 |
| Total segment revenue | 28,248 | 25,479 | - | 53,727 |
| Depletion charges | (5,359) | (2,806) | - | (8,165) |
| Impairment | (1,655) | - | - | (1,655) |
| Hurricane repairs | (2,750) | - | - | (2,750) |
| Other cost of sales | (16,249) | (1,318) | - | (17,567) |
| General administrative expenses before depreciation | (3,208) | (3,026) | (6,603) | (12,837) |
| Inter-segment administrative expense | - | (127) | - | (127) |
| Depreciation and amortisation | (49) | (124) | (23) | (196) |
| Foreign exchange gains / (losses) | - | 74 | (4,803) | (4,729) |
| Share based payments | - | - | (12,572) | (12,572) |
| (Loss) / profit before interest and taxation | (1,022) | 18,152 | (24,001) | (6,871) |
| Interest expense and unwinding of discount | (1,668) | - | (3) | (1,671) |
| Interest income from external parties | 464 | 133 | 636 | 1,233 |
| Inter-segment interest | (3,618) | - | 3,618 | - |
| Taxation | 1,932 | - | - | 1,932 |
| (Loss) / profit for the year | (3,912) | 18,285 | (19,750) | (5,377) |

Central costs have not been apportioned to the reportable segments and are included within 'Other' above.

All external revenues are derived from production in, and sales to, the segments above. See the credit risk section of note 26 for details on major customers.

The segment assets and liabilities as at 31 December and the segment capital expenditure during the year ended 31 December were as follows:

| | 2009 | | | |
|---|---|---|---|---|
| | **USA** | **Syria** | **Other** | **Total** |
| | **$' 000** | **$' 000** | **$' 000** | **$' 000** |
| Assets | **58,072** | **82,004** | **45,229** | **185,305** |
| Liabilities | **(36,405)** | **(7,579)** | **(1,047)** | **(45,031)** |
| Inter-segment balances | **(47,370)** | **(8,823)** | **56,193** | **-** |
| Capital expenditure | **3,376** | **20,340** | **349** | **24,065** |

| | 2008 (restated) | | | |
|---|---|---|---|---|
| | USA | Syria | Other | Total |
| | $' 000 | $' 000 | $' 000 | $' 000 |
| Assets | 66,260 | 52,475 | 26,579 | 145,314 |
| Liabilities | (33,397) | (3,757) | (398) | (37,552) |
| Inter-segment balances | (40,466) | (32,466) | 72,932 | - |
| Capital expenditure | 4,951 | 11,125 | 156 | 16,232 |

Transactions between segments include management fees and are charged at estimated prevailing market prices.

## 7. Share based payments

The charge for the period is based upon the requirements of IFRS 2 regarding share based payments. For this purpose, the weighted average estimated fair value of the share options granted was calculated using a Black-Scholes option pricing model. The expected average option life was assumed to be four years. No dividends were factored into the model.

The fair value of options issued in 2009 was $313,000 (2008: $12,587,000). Details of option grants made during the year and assumptions included in the calculation of the charge to the income statement are as follows:

| Grant date | Year options vest | Stock price at date of grant | Exercise price | Number of options issued | Risk free interest rate | Volatity |
|---|---|---|---|---|---|---|
| 9 February 2009 | 2009 and 2010 | £1.58 | £1.86 | 40,000 | 2.6% | 57.8% |
| 16 February 2009 | 2009 - 2011 | £1.37 | £1.86 | 250,000 | 2.2% | 57.8% |
| 27 April 2009 | 2009 and 2010 | £1.99 | £1.99 | 20,000 | 2.3% | 62.5% |
| 08 July 2009 | 2009 and 2010 | £1.75 | £1.88 | 75,000 | 2.7% | 35.5% |

The estimated fair value of options with a deferred vesting period is charged to the income statement over the vesting period of the options concerned. The estimated fair value of options exercisable immediately is expensed at the time of issuance of the options. Further details are provided in note 21.

## 8. Hurricane repairs

In 2008 Hurricanes Gustav and Ike caused damage to several of the Group's oil and gas properties and supporting infrastructure in the Gulf of Mexico. A charge has been made in these accounts for the full amount of any damage notified by the operators less insurance claim refunds that the directors are satisfied are virtually certain to be recoverable. The income statement charge in 2009 reflects increased cost notifications from operators received during the year. The amount charged to the Income Statement in the year end 31 December 2009 was $2,316,000 (2008: $2,750,000).

## 9. Operating profit / (loss)

The Group's operating profit / (loss) is stated after charging / (crediting):

| | **2009** | 2008 (restated) |
|---|---|---|
| | **$' 000** | $' 000 |
| Foreign exchange (gain) / loss | **(538)** | 4,729 |
| Share based payment charges (note 7) | **1,124** | 12,572 |
| Hurricane repairs (note 8) | **2,316** | 2,750 |
| Depletion of oil and gas properties (note 13) | **12,289** | 8,165 |
| Depreciation and amortisation of other fixed assets (notes 13 & 14) | **493** | 186 |
| Impairment of development and production assets (note 13) | **6,420** | 1,655 |
| Staff costs excluding share based payments (note 22) | **8,177** | 6,176 |
| Operating lease rentals: | | |
| Buildings | **1,268** | 232 |
| Vehicles and equipment | **4,420** | 2,614 |

The operating lease rentals shown for 2009 include $3,463,000 (2008: $2,523,000) in respect of the hire of drilling rigs and operating staff.

Details of the auditors' remuneration is set out in the table below:

| | **2009** | 2008 |
|---|---|---|
| | **$' 000** | $' 000 |
| **Deloitte (2008: UHY Hacker Young)** | | |
| Fees payable to the Company's auditors for the audit of the Company's annual accounts | **216** | 203 |
| Fees payable to the Company's auditors and their associates for the audit of the Company's subsidiaries pursuant to legislation | **23** | - |
| Fees payable to the Company's auditors and their associates for the audit of the Company's joint ventures pursuant to legislation | **27** | - |
| **Total audit fees** | **266** | 203 |
| **Deloitte (2008: UHY Hacker Young)** | | |
| Other services pursuant to legislation - interim review | **66** | 12 |
| Taxtion services | **33** | 8 |
| Other services | **-** | 1 |
| **Total non-audit fees** | **99** | 21 |

## 10. Net Interest receivable

| Group | **2009** | 2008 |
|---|---|---|
| | **$' 000** | $' 000 |
| Short-term bank deposit interest | **326** | 1,233 |
| Overdraft and similar interest charges | **(33)** | (4) |
| | **293** | 1,229 |

## 11. Taxation charge

**Group**

| | **2009** | 2008 |
|---|---|---|
| | **$' 000** | $' 000 |
| Current Corporation Tax: | | |
| UK Corporation Tax | **-** | - |
| Overseas Corporation Tax | **12** | - |
| Deferred Taxation: | | |
| Tax losses carried forward | **-** | 1,725 |
| Timing differences | **-** | (3,657) |
| Total charge / (credit) | **12** | (1,932) |

The Group's effective tax rate differs from the theoretical amount that would arise using the UK domestic corporation tax rate applicable to profits of the consolidated companies as follows:

| Group | | 2008 |
|---|---|---|
| | **2009** | (restated) |
| | **$' 000** | $' 000 |
| Profit / (loss) before tax | **27,844** | (7,309) |
| Tax calculated at domestic rate of 28% (2008: 28.5%) | **7,796** | (2,083) |
| Effects of: | | |
| Expenses not deductible for taxation purposes | **15** | 19 |
| Share based payments | **315** | 3,583 |
| Tax losses for which no deferred taxation asset was recognised | **4,488** | 8,032 |
| Effect of prior period adjustment | **98** | (5,838) |
| Impact of local tax rates | **(12,553)** | (5,808) |
| Other tax adjustments | **(147)** | 163 |
| | **12** | (1,932) |

The Group's tax liability in Syria is settled on its behalf by the Syrian Petroleum Company out of the latter's share of royalties and profit oil and, as such, is not reflected in the Group's tax charge for the year.

## 12. Earnings per share

The basic and diluted earnings per share have been calculated using the earnings for the year ended 31 December 2009 of $27,832,000 (2008 loss (restated): $5,377,000). The basic earnings per share was calculated using a weighted average number of shares in issue of 119,334,527 (2008: 115,520,651). The weighted average number of ordinary shares, allowing for the exercise of share options, for the purposes of calculating the diluted earnings per share was 120,681,343 (2008: 115,520,651).

## 13. Property, plant and equipment

| Group | Oil and gas properties | | | |
|---|---|---|---|---|
| | USA $' 000 | Syria $' 000 | Other fixed assets $' 000 | Total $' 000 |
| *Cost:* | | | | |
| At 1 January 2008 (restated) | 73,228 | - | 310 | 73,538 |
| Additions (restated) | 4,621 | 10,000 | 596 | 15,217 |
| Transfer from Intangible assets | - | 29,221 | - | 29,221 |
| Disposals | - | - | (33) | (33) |
| At 31 December 2008 (restated) | 77,849 | 39,221 | 873 | 117,943 |
| Additions | 9,010 | 15,308 | 428 | 24,746 |
| Disposals | (1,625) | - | - | (1,625) |
| At 31 December 2009 | 85,234 | 54,529 | 1,301 | 141,064 |
| *Accumulated depreciation and depletion:* | | | | |
| At 1 January 2008 (restated) | (24,687) | - | (166) | (24,853) |
| Charge for 2008 (restated) | (5,359) | (2,806) | (185) | (8,350) |
| Disposals | - | - | 24 | 24 |
| At 31 December 2008 (restated) | (30,046) | (2,806) | (327) | (33,179) |
| Charge for 2009 | (2,372) | (9,917) | (314) | (12,603) |
| Disposals | 1,087 | - | - | 1,087 |
| At 31 December 2009 | (31,331) | (12,723) | (641) | (44,695) |
| *Accumulated impairment:* | | | | |
| At 1 January 2008 (restated) | (6,054) | - | - | (6,054) |
| Impairment charge for 2008 (restated) | (3,482) | - | - | (3,482) |
| Reversal of impairment charges from prior years | 1,827 | - | - | 1,827 |
| At 31 December 2008 | (7,709) | - | - | (7,709) |
| Impairment charge for 2009 | (7,218) | - | - | (7,218) |
| Reversal of impairment charges from prior years | 798 | - | - | 798 |
| Disposals | 329 | - | - | 329 |
| At 31 December 2009 | (13,800) | - | - | (13,800) |
| **Net book value at 31 December 2009** | **40,103** | **41,806** | **660** | **82,569** |
| Net book value at 31 December 2008 (restated) | 40,094 | 36,415 | 546 | 77,055 |
| Net book value at 31 December 2007 (restated) | 42,487 | - | 144 | 42,631 |

The depletion for the US oil and gas properties is stated after depletion reversals of $2,317,000 (2008: $415,000). These depletion reversals occur on properties that have been substantially depleted in prior years and where subsequent downward revisions to decommissioning estimates have been made in years before the actual decommissioning has commenced.

The impairment charges and reversals of impairment charges for 2009 and 2008 relate to provisions against the Group's carrying values of its USA producing assets, following a review of reserves and prevailing oil and gas prices at the year ends. The changes in the market price of oil and gas, together with movements in the Proved and Probable reserves on certain fields, has led to a reappraisal of the economics of certain fields in the USA.

Impairment has been assessed, based on a value in use calculation, and using a discount rate of 6% for assets (2008: 6% ), a long-term oil price of $80/bbl (2008: $70/bbl) and a long term gas price of $6.00/mcf (2008: $7.00/mcf). In determining the appropriate discount rate to be used consideration is given to the risk incorporated in the underlying cash flows.

**Company**

| | Office equipment, fixtures and fittings $' 000 | Total $' 000 |
|---|---|---|
| *Cost:* | | |
| At 1 January 2008 | 33 | 33 |
| Additions | 158 | 158 |
| Disposals | (33) | (33) |
| At 31 December 2008 | 158 | 158 |
| Additions | 140 | 140 |
| At 31 December 2009 | 298 | 298 |
| *Accumulated depreciation:* | | |
| At 1 January 2008 | (20) | (20) |
| Charge for 2008 | (17) | (17) |
| Disposals | 24 | 24 |
| At 31 December 2008 | (13) | (13) |
| Charge for 2009 | (89) | (89) |
| At 31 December 2009 | (102) | (102) |
| **Net book value at 31 December 2009** | **196** | **196** |
| Net book value at 31 December 2008 | 145 | 145 |

## 14. Intangible assets

**Group**

| | Exploration and evaluation assets $' 000 | Computer software $' 000 | Total $' 000 |
|---|---|---|---|
| *Cost:* | | | |
| At 1 January 2008 | 28,576 | 50 | 28,626 |
| Additions | 645 | 327 | 972 |
| Transfer to Property, plant & equipment | (29,221) | - | (29,221) |
| At 31 December 2008 | - | 377 | 377 |
| Additions | 6,724 | 202 | 6,926 |
| At 31 December 2009 | 6,724 | 579 | 7,303 |
| *Accumulated amortisation:* | | | |
| At 1 January 2008 | - | (33) | (33) |
| Charge for 2008 | - | (1) | (1) |
| At 31 December 2008 | - | (34) | (34) |
| Charge for 2009 | - | (178) | (178) |
| At 31 December 2009 | - | (212) | (212) |
| **Net book value at 31 December 2009** | **6,724** | **367** | **7,091** |
| Net book value at 31 December 2008 | - | 343 | 343 |

Intangible E&E assets of $29,221,000, representing the cumulative cost of exploration work in Block 26 in Syria, were transferred to development and production assets within tangible fixed assets upon the successful declaration of commerciality for the Khurbet East field in the second half of 2008. At 31 December 2009 E&E assets represents the costs to date of the Group's share of the acquisition of 3D seismic data over 850km2 of Block 26 plus the sole risk costs of 64km2 of 3D seismic data over the Taramish area of Block 26 in Syria acquired during 2009.

$645,000 of overhead expense was capitalised during the year ended 31 December 2008 in respect of general and administrative costs prior to discovery of commercial reserves.

**Company**

| | Computer software $' 000 | Total $' 000 |
|---|---|---|
| *Cost:* | | |
| At 1 January 2009 | - | - |
| Additions | 173 | 173 |
| At 31 December 2009 | 173 | 173 |
| *Accumulated amortisation:* | | |
| At 1 January 2009 | - | - |
| Amortisation charge for 2009 | (52) | (52) |
| At 31 December 2009 | (52) | (52) |
| **Net book value at 31 December 2009** | **121** | **121** |
| Net book value at 31 December 2008 | - | - |

## 15. Investments

### Company

| | **2009 $' 000** | 2008 $' 000 |
|---|---|---|
| Cost of shares in Gulfsands Petroleum Ltd. | **7,306** | 7,306 |
| Loans to subsidiaries | **52,435** | 42,830 |
| | **59,741** | 50,136 |

The Company's fixed asset investment of $7,306,000 represents the historic cost of acquisition of the entire share capital of Gulfsands Petroleum Ltd. by means of a share for share exchange in 2005, less any required provision for impairment.

Loans to subsidiary undertakings comprise a revolving loan from the Company to Gulfsands Petroleum USA, Inc. for $52,435,000 (2008: $42,830,000) including accrued interest. Interest is charged at 8.5% per annum on the outstanding principal and is payable in full on 31 December annually. The principal balance may be paid in part or in full at anytime with no penalty. On 1 January 2011 the loan converts to a term loan and the payments will be made in 4 instalments over the next 4 years.

The Company's investments in subsidiary undertakings are shown below. All investments are in ordinary shares and are directly or indirectly owned by the Company as stated below:

| ***Name of Company*** | ***Proportion of voting shares at 31 December 2009*** | ***Nature of business*** | ***Country of incorporation*** |
|---|---|---|---|
| *Directly held by the Company:* | | | |
| Gulfsands Petroleum Ltd. | 100% | Holding company | Cayman Islands |
| *Indirectly held by the Company:* | | | |
| Gulfsands Petroleum Holdings | 100% | Holding company | Cayman Islands |
| Gulfsands Petroleum Colombia Ltd. | 100% | Dormant | Cayman Islands |
| Gulfsands Petroleum Syria Ltd. | 100% | Oil & gas exploration | Cayman Islands |
| Gulfsands Petroleum Iraq Ltd. | 100% | Oil & gas exploration | Cayman Islands |
| Gulfsands Petroleum USA, Inc. | 100% | Oil & gas exploration | US |
| Darcy Energy LLC | 100% | Oil & gas exploration | US |

Gulfsands Petroleum Syria Limited owns a 50% interest in a contractor group exploring for hydrocarbons in Block 26 in Syria. The results and net assets of the contractor group are proportionally consolidated within the Group accounts.

Gulfsands Petroleum Syria Limited owns 25% of the voting shares in Dijla Petroleum Company ("DPC"), a company incorporated in Syria. DPC is a joint venture undertaking between the Syrian Petroleum Company and the other parties participating in the production of hydrocarbons from Block 26 in Syria. All costs of DPC are ultimately borne equally between the Group and its joint venture partner, Emerald Energy plc. In the Group accounts the results and net assets of DPC are proportionally consolidated.

The Group's share of the summarised aggregated balance sheet of jointly controlled entities is set out below:

| | **$' 000** | $' 000 |
|---|---|---|
| Long term assets | **52,831** | 28,973 |
| Current assets | **47,032** | 16,958 |
| Current liabilities | **(22,197)** | (36,223) |

The Group's share of the summarised aggregated income statement of jointly controlled entities is set out below:

| | **2009** | 2008 |
|---|---|---|
| | **$' 000** | $' 000 |
| Income | **70,453** | 25,479 |
| Expenses | **(18,216)** | (7,193) |

## 16. Trade and other receivables

| | Group | | Company | |
|---|---|---|---|---|
| | **2009** | 2008 | **2009** | 2008 |
| | **$' 000** | $' 000 | **$' 000** | $' 000 |
| Trade receivables | **15,213** | 8,266 | **-** | - |
| Other receivables | **-** | 28 | **-** | - |
| Insurance receivable (note 8) | **1,128** | - | **-** | - |
| Underlift | **502** | 919 | **-** | - |
| Corporation tax recoverable | **408** | 316 | **354** | 262 |
| Prepayments and accrued income | **1,427** | 1,378 | **209** | 134 |
| Amounts due from oil and gas partnerships | **3,189** | 4,629 | **-** | - |
| Amounts due from subsidiaries | **-** | - | **3,922** | 33,515 |
| | **21,867** | 15,536 | **4,485** | 33,911 |

Included in trade receivables at 31 December 2008 was an amount of $5,096,000 that represented a retention of 20% on the oil sales to the Oil Marketing Bureau of the Government of the Syrian Arab Republic. This retention was released during September 2009 upon completion of certain assay tests on the quality of the crude oil delivered from the Khurbet East field.

No significant trade receivables are classified as past due or considered impaired.

Underlift at 31 December 2009 and 2008 represents the rights to gas revenue receivable as a result of the acquisition of oil and gas properties in the Gulf of Mexico in May 2004. Underlift represents a right to future economic benefits (through entitlement to receive equivalent future production), which constitutes an asset. During the year ended 31 December 2009 certain underlift balances were sold to external parties.

Amounts due from oil and gas partnerships represents the excess of the Group's loans and advances to jointly controlled entities over its share of the assets less liabilities of those entities.

## 17. Cash and cash equivalents

| | Group | | Company | |
|---|---|---|---|---|
| | **2009** | 2008 | **2009** | 2008 |
| | **$' 000** | $' 000 | **$' 000** | $' 000 |
| Cash at bank and in hand | **57,623** | 36,812 | **45,578** | 28,339 |
| Restricted cash balances | **11,990** | 13,167 | **-** | - |
| | **69,613** | 49,979 | **45,578** | 28,339 |
| Included in long term financial assets | **11,990** | 13,167 | **-** | - |
| Total cash and cash equivalents | **57,623** | 36,812 | **45,578** | 28,339 |

The restricted cash balances comprise (i) amounts held in escrow to cover decommissioning expenditures under the requirements of the regulatory authorities that manage the oil and gas and other mineral resources in the Gulf of Mexico and (ii) a bank guarantee that is required under the terms of the Production Sharing Contract with the Syrian Petroleum Company and which is reduced quarterly as the obligations under the required work programmes are completed.

## 18. Trade and other payables

| | Group | | Company | |
|---|---|---|---|---|
| | **2009** | 2008 | **2009** | 2008 |
| | **$' 000** | $' 000 | **$' 000** | $' 000 |
| Trade payables | **6,732** | 9,266 | **316** | 251 |
| Accruals and other payables | **6,679** | 1,979 | **731** | 144 |
| Amounts due to subsidiaries | **-** | - | **75** | 4,072 |
| | **13,411** | 11,245 | **1,122** | 4,467 |

## 19. Deferred tax assets / (liabilities)

| | Group | | Company | |
|---|---|---|---|---|
| | **2009** | 2008 | **2009** | 2008 |
| | **$' 000** | $' 000 | **$' 000** | $' 000 |
| DD&A and impairment in excess of tax allowances | **2,980** | 767 | **-** | - |
| Other short term temporary differences | **2,330** | 943 | **-** | - |
| Tax losses carried forward | **10,810** | 6,322 | **2,423** | 2,328 |
| Unprovided deferred tax asset | **(16,120)** | (8,032) | **(2,423)** | (2,328) |
| Deferred tax asset / (liability) at 31 December | **-** | - | **-** | - |

The tax effect of amounts for which no deferred tax asset has been recognised is as follows:

| | Group | | Company | |
|---|---|---|---|---|
| | **2009** | 2008 | **2009** | 2008 |
| | **$' 000** | $' 000 | **$' 000** | $' 000 |
| Unutilised tax losses | **10,810** | 6,755 | **2,423** | 2,328 |
| Other short term temporary differences | **5,310** | 1,277 | **-** | - |
| | **16,120** | 8,032 | **2,423** | 2,328 |

$24 million (2008: $14 million) of the Group's unutilised tax losses have expiry dates between 2024 and 2029. The remaining tax losses of the Group and the tax losses of the Company have no expiry date.

Deferred tax assets are not provided where the Group does not consider it probable that sufficient future taxable profits will be made to offset the deductions represented by those deferred tax assets. In performing this calculation the Group considers deferred tax balances relating to each tax authority separately.

## 20. Provision for decommissioning

The provision for decommissioning relates to the expected present value of costs of plugging and abandoning the oil and gas properties held by Gulfsands Petroleum USA, Inc and Darcy Energy LLC. The provision for decommissioning is estimated after taking account of inflation, years to abandonment and an appropriate discount rate. At 31 December 2009, the oil and gas properties have estimated plugging and abandonment dates between 2009 and 2024.

The portion of the provision for decommissioning expected to be settled in 2010, totalling approximately $3.7 million, is included in current liabilities and the remainder, totalling approximately $27.9 million, is included in non-current liabilities in the consolidated balance sheet at 31 December 2009.

Actual decommissioning costs will ultimately depend upon future market prices for the decommissioning work required, which will reflect market conditions at the relevant time. Furthermore, the timing of decommissioning is likely to depend on when the fields cease to produce at economically viable rates. This in turn will depend upon future oil and gas prices, which are inherently uncertain.

The actual amounts paid for decommissioning may ultimately vary significantly from the provision at 31 December 2009 requiring potentially material adjustments to the carrying value of the obligations.

The movement in the provision for decommissioning was as follows:

| | $' 000 |
|---|---|
| At 1 January 2008 | 27,776 |
| Changes in estimates | (557) |
| Additions | - |
| Costs in excess of provision | 2,987 |
| Decommissioning costs paid | (5,566) |
| Discount expense | 1,667 |
| At 31 December 2008 | 26,307 |
| Less: current portion | 5,877 |
| Non-current portion | 20,430 |
| At 1 January 2009 | 26,307 |
| Changes in estimates | 5,542 |
| Additions | 92 |
| Costs in excess of provision | 696 |
| Decommissioning costs paid | (2,073) |
| Discount expense | 1,056 |
| At 31 December 2009 | 31,620 |
| Less: current portion | 3,683 |
| Non-current portion | 27,937 |

## 21. Share capital

### Group and Company

| | **2009 Number** | 2008 Number |
|---|---|---|
| *Authorised:* | | |
| Ordinary shares of 5.714 pence each | **175,000,000** | 175,000,000 |

| | **2009 $' 000** | 2008 $' 000 |
|---|---|---|
| *Allotted, called up and fully paid:* | | |
| 120,222,500 (2008 - 118,522,500) ordinary shares of 5.714 pence each | **12,971** | 12,814 |

The movements in share capital and share options were:

| | Weighted average exercise price of options | Number of share options | Number of ordinary shares |
|---|---|---|---|
| At 1 January 2009 | £1.64 | 10,165,000 | 118,522,500 |
| Share options exercised for cash | £1.31 | (1,700,000) | 1,700,000 |
| Share options lapsed | £1.86 | (40,000) | - |
| Share options issued | £1.87 | 385,000 | - |
| At 31 December 2009 | £1.71 | 8,810,000 | 120,222,500 |

The detail of the share options outstanding at 31 December 2009 are as follows:

| Exercise period | Year options vest | Weighted average exercise price | Number of options |
|---|---|---|---|
| 5 April 2005 - 4 April 2010 | 2005 | £1.30 | 535,000 |
| 13 February 2006 - 18 October 2011 | 2006 | £1.18 | 855,000 |
| 19 February 2007 - 3 June 2012 | 2007 | £1.13 | 530,000 |
| 8 May 2008 - 8 December 2013 | 2008 | £1.86 | 5,175,000 |
| 8 May 2009 - 27 November 2013 | 2009 | £1.82 | 675,000 |
| 9 February 2009 - 10 June 2014 | 2009 | £1.87 | 192,500 |
| 8 May 2010 - 27 November 2013 | 2010 | £1.82 | 675,000 |
| 16 February 2010 - 10 June 2014 | 2010 | £1.88 | 110,000 |
| 16 February 2011 - 16 February 2014 | 2011 | £1.86 | 62,500 |
| | | £1.71 | 8,810,000 |

Options are exercisable at prices from £0.96 to £1.99 per share and have a weighted estimated remaining contractual life of 3.8 years.

Of the total outstanding options at 31 December 2009, the options granted to the Directors numbered 6,675,000 (2008: 6,675,000) and those granted to other staff numbered 2,040,000 (2008: 1,845,000). The remaining 95,000 (2008: 1,645,000) were granted to ex-employees and ex-directors or consultants who are currently involved with or have performed work for the Group.

The average share price during 2009 was £1.95. The highest share price during the year was £2.54 and the lowest price was £1.25.

## 22. Staff costs

The aggregate payroll costs of staff and Directors were as follows:

| | **2009** | 2008 |
|---|---|---|
| | **$' 000** | $' 000 |
| Wages and salaries | **6,891** | 5,858 |
| Social security costs | **373** | 175 |
| Share based payment charges | **1,124** | 12,572 |
| Other benefits in kind | **913** | 143 |
| | **9,301** | 18,748 |

Included in other benefits in kind above is a sum of $740,000 in respect of benefits paid to former directors (2008: nil), see the Directors' remuneration report on pages 45 – 47 for further details.

The average monthly number of persons employed by the Group, including Directors was as follows:

| | **2009** | 2008 |
|---|---|---|
| | **Number** | Number |
| Operational and technical | **12** | 6 |
| Administrative | **20** | 15 |
| | **32** | 21 |

Staff numbers and costs recorded above include the Group's proportionate share of staff employed by jointly controlled entities.

Details of the remuneration of Directors are included in the Directors' remuneration report on pages 45 to 47. No employees other than Directors are determined to be key management personnel.

## 23. Obligations under operating leases

At the end of the year the Group had commitments for future minimum lease payments under non-cancellable operating leases as follows:

| | **2009** | | 2008 | |
|---|---|---|---|---|
| | **Land & Buildings** | **Other** | Land & Buildings | Other |
| | **$' 000** | **$' 000** | $' 000 | $' 000 |
| Amounts payable on leases: | | | | |
| Within one year | **612** | **472** | 539 | 395 |
| In two to five years | **986** | **-** | 1,462 | 7 |
| After more than five years | **-** | **-** | - | - |
| | **1,598** | **472** | 2,001 | 402 |

In addition to the items mentioned above the Group had commitments to make payments under a non-cancellable lease for the provision of an oil rig. This lease expires in 2010. At 31 December 2009 the Group had a commitment to make further payments totalling approximately $2.7 million (2008: $7.5 million) for the provision of the rig and operating staff. The ultimate timing of these payments will depend upon the Group's drilling programme.

At the end of the year the Company had commitments for future minimum lease payments under non-cancellable operating leases in respect of land and buildings of $438,000 (2008: $381,000) within one year and $986,000 (2008: $1,238,000) between two and five years. This lease is due to expire in 2013.

## 24. Commitments

At 31 December 2009 all exploration expenditure and work programme commitments pertaining to the current exploration period (ending August 2010) in Block 26 in Syria had been satisfied in full.

There were no other material obligations or contracts outstanding in relation to ongoing projects not provided for at 31 December 2009 or 2008.

## 25. Contingent liabilities

Due to the nature of the Group's business, some contamination of the real estate property owned or leased by the Group is possible. Environmental site assessments of the property would be necessary to adequately determine remediation costs, if any. The Directors do not consider the amounts that would result from any environmental site assessments to be significant to the financial position or results of operations of the Group. Accordingly, except for the provision made against decommissioning costs (note 20), no further provision for potential remediation costs is required.

## 26. Financial instruments, derivatives and capital management of the Group

*Risk assessment*
The Group's oil and gas activities are subject to a range of financial risks, as described below, which can significantly impact its performance.

*Liquidity risk*
At 31 December 2009 the Group had sufficient funds available to progress its exploration portfolio and projected requirements for the development of existing reserves. At the end of the year the Group had cash in hand of $57.6 million, and further bank balances of $12.0 million held in escrow to cover expected decommissioning liabilities.

Cash forecasts identifying the liquidity requirements of the Group are produced frequently. These are reviewed regularly by management and the Board to ensure that sufficient financial headroom exists for at least 12 months. At present the Group has no loan facilities in place and has no obvious need for such facilities based upon its current projects in hand and its available cash resources. However this position will continually be reviewed in the light of developments with existing projects and new project opportunities as they arise.

*Currency risk*
The Group has currency exposure arising from transactions denominated in currencies other than the functional currency of the Company and all its subsidiaries, US Dollars. These transactions relate predominantly to certain costs of its Syrian operations which are denominated in Syrian Pounds and Euro, and its head office costs which are denominated in Pounds Sterling.

Although sales of crude oil by the Group's Syrian operations are invoiced in US Dollars payment is made in Euro according to the exchange rate pertaining between US Dollars and Euro shortly before the payment is made. The Group manages any further risk through the use of short term

foreign currency forward contracts of not more than ten days duration. Each contract is entered into with the aim of exactly covering any foreign currency risk on Euro receivables. There was no significant contract in place as at 31 December 2009 or 2008.

Costs incurred in Euro in the Syrian operations are recoverable under the terms of the Production Sharing Contract at the rate of exchange between US Dollars and Euro at the date of payment.

The Group maintains part of its cash balances in Pounds Sterling to defray head office costs.

The following table demonstrates the sensitivity to changes in the US Dollar exchange rate, with all other variables held constant, on the Group's profit before tax and the Group's equity.

| | Change in US Dollar rate | Effect on (loss) / profit before tax $000 |
|---|---|---|
| **2009** | **(+ or -) 5%** | 505 |
| 2008 | (+ or -) 5% | 660 |

*Credit risk*
In the USA the Group trades only with recognised, creditworthy third parties. The Group manages the exposures to credit risk by performing credit evaluations on all of their major customers requiring credit.

In Syria, the Group's share of crude oil is sold to the Oil Marketing Bureau of the Government of the Syrian Arab Republic. Management believe that the counterparty risk is low and similar to the sovereign risk of Syria.

*Capital risk management*
The Group's objectives when managing capital are to safeguard the Group'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. In order to maintain or adjust the capital structure, the Group may return capital to shareholders, issue new shares or sell assets to reduce debt.

The Group considers capital to be its equity reserves. At the current stage of the Group's life cycle, the Group's objective in managing its capital is to ensure funds raised meet the exploration expenditure commitments.

The Group ensures it is meeting its objectives by reviewing its KPIs and other management information to ensure its activities are progressing in line with expectations, controlling costs and placing unused funds on deposit to conserve resources and increase returns on surplus cash held.

*Financial assets*
The Group's financial assets consist of long term financial assets, cash at bank and receivables. The interest rate profile at 31 December for these assets at US dollar equivalents was as follows:

| | Financial assets on which interest is earned $' 000 | Financial assets on which no interest is earned $' 000 | Total $' 000 |
|---|---|---|---|
| **2009** | | | |
| US Dollar | **41,725** | **38,816** | **80,541** |
| UK Sterling | **7,129** | **559** | **7,688** |
| Euro | **6,628** | **10** | **6,638** |
| Syrian Pounds | **167** | **7** | **174** |
| | **55,649** | **39,392** | **95,041** |
| **2008** | | | |
| US Dollar | 35,780 | 16,042 | 51,822 |
| UK Sterling | 12,656 | 149 | 12,805 |
| Euro | 698 | - | 698 |
| Syrian Pounds | 185 | 5 | 190 |
| | 49,319 | 16,196 | 65,515 |

The UK Sterling, Euro and Syrian Pound assets principally comprise cash on hand, cash in instant access accounts and short term money market deposits. The US Dollar assets represent cash on call accounts, money market accounts, and short term receivables. The Group earned interest on its interest bearing financial assets at rates between 0.1% and 4.75%. All financial assets are considered immediately available to turn into cash on demand.

In the current economic climate with exceptionally low interest rates, the Group is not sensitive to fluctuations in the interest rate received on bank and money market deposits and accordingly no sensitivity analysis is published.

Included in US Dollar financial assets are amounts of $15,213,000 (2008: $8,266,000) of trade receivables. The Group considers that $13,217,000 (2008: $7,015,000) carries the risk of the sovereign debt of the Syrian Arab Republic. The remaining trade receivables consist of amounts receivable from various counter-parties where the Group considers the credit risk to be low. This risk is monitored by the Group. No significant assets included in trade receivables are past due or considered impaired.

*Financial liabilities*

The Group’s financial liabilities consist of short term payables. None of these liabilities bear interest to external parties.

At 31 December financial liabilities are classified as shown below:

| | Financial liabilities on which no interest is charged $' 000 |
|---|---|
| **2009** | |
| US Dollar | **9,869** |
| UK Sterling | **1,073** |
| Euro | **1,637** |
| Syrian Pounds | **832** |
| | **13,411** |
| **2008** | |
| US Dollar | 10,755 |
| UK Sterling | 395 |
| Euro | - |
| Syrian Pounds | 95 |
| | 11,245 |

The Group's short term creditors liabilities are considered to be payable on demand.

*Derivatives*

The Group has exposure to changes in oil and gas prices. In the past the Group utilised derivative financial instruments to reduce exposure to market risks resulting from fluctuations in oil and gas prices in order to reduce the volatility of the cash flows of the Group. The derivative contracts expired in May 2007 and no such contracts are currently outstanding. The future use of derivatives will be kept under review should the Group feel that the exposure to commodity price risk significantly impacts the liquidity risk of the Group. The Group incurred no expense in respect of oil and gas price derivatives in 2009 or 2008.

*Fair values*

At 31 December 2009 and 2008, the Directors considered the fair values and book values of the Group's financial assets and liabilities to be materially the same.

### 27. Financial instruments, derivatives and capital management of the Company

The financial risks of the Company are principally in respect of balances held in bank accounts and on deposit, and balances owed to, or owed by, subsidiary undertakings. These balances are all denominated in US Dollars. Other risks are managed on a unified basis with the Group and a full disclosure of these risks is made in note 26.

A summary of the financial assets and financial liabilities of the Company is set out below:

| | Financial assets on which interest is earned $' 000 | Financial assets on which no interest is earned $' 000 | Total $' 000 |
|---|---|---|---|
| **2009** | | | |
| US Dollar | **78,295** | **16,295** | **94,590** |
| UK Sterling | **7,129** | **559** | **7,688** |
| Euro | **-** | **9** | **9** |
| | **85,424** | **16,863** | **102,287** |
| **2008** | | | |
| US Dollar | 58,339 | 29,603 | 87,942 |
| UK Sterling | 12,805 | 262 | 13,067 |
| Euro | - | - | - |
| | 71,144 | 29,865 | 101,009 |

| | Financial liabilities on which no interest is charged $' 000 |
|---|---|
| **2009** | |
| US Dollar | **75** |
| UK Sterling | **1,047** |
| | **1,122** |
| **2008** | |
| US Dollar | - |
| UK Sterling | 395 |
| | 395 |

## 28. Related party transactions and key management

Key management of the Group are considered to be the Directors of the Company. There were no transactions with Directors, other than interests in shares and their remuneration and share options as disclosed in the Directors' remuneration report on pages 45 to 47.

The remuneration of Directors is set out below in aggregate for each of the categories specified in IAS 24 'Related Party Disclosures'.

| | **2009 $' 000** | 2008 $' 000 |
|---|---|---|
| Short-term employee benefits | **2,251** | 3,424 |
| Post-employment benefits | **-** | 50 |
| Termination benefits | **-** | 843 |
| Share-based payments | **824** | 10,725 |
| | **3,075** | 15,042 |

There were no other related party transactions during the year ended 31 December 2009.

## 29. Events after the balance sheet date

On 18 March 2010 the Company announced that it had received a preliminary approach that may, or may not, lead to an offer for the Company. On 19 March 2010 the Board of Directors of the Company announced that it had rejected the preliminary approach as it considered the proposal to be wholly inadequate and materially undervaluing the Company. The Board also considered the approach to be unsolicited, highly conditional, subject to due diligence and other pre-conditions.

On 22 March 2010 the Group announced that it had reached an agreement to acquire working interests in two exploration permits in Tunisia and one in Southern Italy. The terms of the acquisition of the interests in these permits will require the Group to pay for a percentage of certain 3D seismic work and exploration drilling.

## 30. Restatement of previous period financial statements

The Group has identified corrections required to certain balances in the financial statements of prior periods. The Group has chosen to restate the Consolidated balance sheets, Consolidated income statements and Consolidated statements of cash flows as at, and for the periods ended, 31 December 2008, 2007 and 2006.

In prior periods certain expenditure of an operating nature incurred in the Gulf of Mexico had been erroneously classified as capital expenditure. The amounts misclassified were $979,000, $2,375,000 and $6,388,000 for 2008, 2007 and 2006 respectively. The corrections of the misclassifications have led to various adjustments to the calculated depletion and impairment charges for each period.

The Group has reclassified cash flows relating to inventory purchases and certain accounts payable as investing activities where these relate to development and exploration activities.

The effect of these restatements to the Consolidated balance sheets, Consolidated income statements and Consolidated statements of cash flows is set out below:

**CONSOLIDATED INCOME STATEMENT**
**FOR THE YEAR ENDED 31 DECEMBER 2008**

| | As stated in 2008 Annual Report $' 000 | Restatement $' 000 | As restated $' 000 |
|---|---|---|---|
| **Revenue** | 53,600 | - | 53,600 |
| Cost of sales | | | |
| Depletion | (8,767) | 602 | (8,165) |
| Impairment | (6,327) | 4,672 | (1,655) |
| Other cost of sales | (16,588) | (979) | (17,567) |
| Total cost of sales | (31,682) | 4,295 | (27,387) |
| **Gross profit** | 21,918 | 4,295 | 26,213 |
| General administrative expenses | (13,033) | - | (13,033) |
| Foreign exchange losses | (4,729) | - | (4,729) |
| Share based payments | (12,572) | - | (12,572) |
| Total administrative expenses | (30,334) | - | (30,334) |
| Hurricane repairs | (2,750) | - | (2,750) |
| **Operating loss** | (11,166) | 4,295 | (6,871) |
| Discount expense on decommissioning provision | (1,667) | - | (1,667) |
| Net interest income | 1,229 | - | 1,229 |
| **Loss before taxation** | (11,604) | 4,295 | (7,309) |
| Taxation | 1,932 | - | 1,932 |
| **LOSS FOR THE YEAR - attributable to equity holders of the Company** | (9,672) | 4,295 | (5,377) |
| **Loss per share (cents):** | | | |
| Basic | (8.37) | | (4.65) |
| Diluted | (8.37) | | (4.65) |

**CONSOLIDATED INCOME STATEMENT**
**FOR THE YEAR ENDED 31 DECEMBER 2007**

| | As stated in 2008 Annual Report $' 000 | Restatement $' 000 | As restated $' 000 |
|---|---|---|---|
| **Revenue** | 37,309 | - | 37,309 |
| Cost of sales | | | |
| Depletion | (6,541) | 687 | (5,854) |
| Impairment | (1,418) | 217 | (1,201) |
| Other cost of sales | (17,425) | (2,375) | (19,800) |
| Total cost of sales | (25,384) | (1,471) | (26,855) |
| **Gross profit** | 11,925 | (1,471) | 10,454 |
| General administrative expenses | (7,204) | - | (7,204) |
| Share based payments | (882) | - | (882) |
| Total administrative expenses | (8,086) | - | (8,086) |
| Hurricane repairs | (1,856) | - | (1,856) |
| **Operating profit** | 1,983 | (1,471) | 512 |
| Discount expense on decommissioning provision | (1,828) | - | (1,828) |
| Net interest income | 1,190 | - | 1,190 |
| **Profit / (loss) before taxation** | 1,345 | (1,471) | (126) |
| Taxation | (2,557) | - | (2,557) |
| **LOSS FOR THE YEAR - attributable to equity holders of the Company** | (1,212) | (1,471) | (2,683) |
| | | | |
| **Loss per share (cents):** | | | |
| Basic | (1.13) | | (2.50) |
| Diluted | (1.13) | | (2.50) |

**CONSOLIDATED INCOME STATEMENT**
**FOR THE YEAR ENDED 31 DECEMBER 2006**

| | As stated in 2008 Annual Report $' 000 | Restatement $' 000 | As restated $' 000 |
|---|---|---|---|
| **Revenue** | 33,934 | - | 33,934 |
| Cost of sales | | | |
| Depletion | (11,693) | 534 | (11,159) |
| Impairment | (4,135) | 424 | (3,711) |
| Other cost of sales | (15,434) | (6,388) | (21,822) |
| Total cost of sales | (31,262) | (5,430) | (36,692) |
| **Gross profit / (loss)** | 2,672 | (5,430) | (2,758) |
| | | | |
| General administrative expenses | (4,455) | - | (4,455) |
| Share based payments | (851) | - | (851) |
| Total administrative expenses | (5,306) | - | (5,306) |
| Hurricane repairs | (2,573) | - | (2,573) |
| **Operating loss** | (5,207) | (5,430) | (10,637) |
| Discount expense on decommissioning provision | (785) | - | (785) |
| Net interest income | 1,193 | - | 1,193 |
| **Loss before taxation** | (4,799) | (5,430) | (10,229) |
| Taxation | (2,433) | - | (2,433) |
| **LOSS FOR THE YEAR - attributable to equity holders of the Company** | (7,232) | (5,430) | (12,662) |
| | | | |
| **Loss per share (cents):** | | | |
| Basic | (7.57) | | (13.25) |
| Diluted | (7.57) | | (13.25) |

**CONSOLIDATED BALANCE SHEET**
**AS AT 31 DECEMBER 2008**

| | As stated in 2008 Annual Report $' 000 | Restatement $' 000 | As restated $' 000 |
|---|---|---|---|
| **ASSETS** | | | |
| **Non-current assets** | | | |
| Property, plant and equipment | 79,661 | (2,606) | 77,055 |
| Intangible assets | 343 | - | 343 |
| Long term financial assets | 13,167 | - | 13,167 |
| | 93,171 | (2,606) | 90,565 |
| **Current assets** | | | |
| Inventory | 2,401 | - | 2,401 |
| Trade and other receivables | 15,536 | - | 15,536 |
| Cash and cash equivalents | 36,812 | - | 36,812 |
| | 54,749 | - | 54,749 |
| **Total Assets** | 147,920 | (2,606) | 145,314 |
| **LIABILITIES** | | | |
| **Current liabilities** | | | |
| Trade and other payables | 11,245 | - | 11,245 |
| Provision for decommissioning | 5,877 | - | 5,877 |
| | 17,122 | - | 17,122 |
| **Non-current liabilities** | | | |
| Provision for decommissioning | 20,430 | - | 20,430 |
| | 20,430 | - | 20,430 |
| **Total liabilities** | 37,552 | - | 37,552 |
| **NET ASSETS** | 110,368 | (2,606) | 107,762 |
| **EQUITY** | | | |
| **Capital and reserves attributable to equity holders** | | | |
| Share capital | 12,814 | - | 12,814 |
| Share premium | 98,530 | - | 98,530 |
| Share-based payments reserve | 14,305 | - | 14,305 |
| Merger reserve | 11,709 | - | 11,709 |
| Retained losses | (26,990) | (2,606) | (29,596) |
| **TOTAL EQUITY** | 110,368 | (2,606) | 107,762 |

**CONSOLIDATED BALANCE SHEET**
**AS AT 31 DECEMBER 2007**

| | As stated in 2008 Annual Report $' 000 | Restatement $' 000 | As restated $' 000 |
|---|---|---|---|
| **ASSETS** | | | |
| **Non-current assets** | | | |
| Property, plant and equipment | 49,532 | (6,901) | 42,631 |
| Intangible assets | 28,593 | - | 28,593 |
| Long term financial assets | 16,078 | - | 16,078 |
| | 94,203 | (6,901) | 87,302 |
| **Current assets** | | | |
| Trade and other receivables | 11,154 | - | 11,154 |
| Cash and cash equivalents | 18,533 | - | 18,533 |
| | 29,687 | - | 29,687 |
| **Total Assets** | 123,890 | (6,901) | 116,989 |
| **LIABILITIES** | | | |
| **Current liabilities** | | | |
| Trade and other payables | 6,672 | - | 6,672 |
| Provision for decommissioning | 10,952 | - | 10,952 |
| | 17,624 | - | 17,624 |
| **Non-current liabilities** | | | |
| Deferred tax liabilities | 1,932 | - | 1,932 |
| Provision for decommissioning | 16,824 | - | 16,824 |
| | 18,756 | - | 18,756 |
| **Total liabilities** | 36,380 | - | 36,380 |
| **NET ASSETS** | 87,510 | (6,901) | 80,609 |
| **EQUITY** | | | |
| **Capital and reserves attributable to equity holders** | | | |
| Share capital | 11,997 | - | 11,997 |
| Share premium | 79,389 | - | 79,389 |
| Share-based payments reserve | 1,733 | - | 1,733 |
| Merger reserve | 11,709 | - | 11,709 |
| Retained losses | (17,318) | (6,901) | (24,219) |
| **TOTAL EQUITY** | 87,510 | (6,901) | 80,609 |

**CONSOLIDATED BALANCE SHEET**
**AS AT 31 DECEMBER 2006**

| | As stated in 2008 Annual Report $' 000 | Restatement $' 000 | As restated $' 000 |
|---|---|---|---|
| **ASSETS** | | | |
| **Non-current assets** | | | |
| Property, plant and equipment | 51,340 | (5,430) | 45,910 |
| Intangible assets | 15,097 | - | 15,097 |
| Long term financial assets | 12,897 | - | 12,897 |
| Deferred tax asset | 176 | - | 176 |
| | 79,510 | (5,430) | 74,080 |
| **Current assets** | | | |
| Trade and other receivables | 9,629 | - | 9,629 |
| Cash and cash equivalents | 13,827 | - | 13,827 |
| | 23,456 | - | 23,456 |
| **Total Assets** | 102,966 | (5,430) | 97,536 |
| **LIABILITIES** | | | |
| **Current liabilities** | | | |
| Trade and other payables | 12,717 | - | 12,717 |
| Provision for decommissioning | 7,627 | - | 7,627 |
| Oil and gas price derivatives | 101 | - | 101 |
| | 20,445 | - | 20,445 |
| **Non-current liabilities** | | | |
| Provision for decommissioning | 18,514 | - | 18,514 |
| | 18,514 | - | 18,514 |
| **Total liabilities** | 38,959 | - | 38,959 |
| **NET ASSETS** | 64,007 | (5,430) | 58,577 |
| **EQUITY** | | | |
| **Capital and reserves attributable to equity holders** | | | |
| Share capital | 11,047 | - | 11,047 |
| Share premium | 56,506 | - | 56,506 |
| Share-based payments reserve | 851 | - | 851 |
| Merger reserve | 11,709 | - | 11,709 |
| Retained losses | (16,106) | (5,430) | (21,536) |
| **TOTAL EQUITY** | 64,007 | (5,430) | 58,577 |

**CONSOLIDATED CASH FLOW STATEMENT**
**FOR THE YEAR ENDED 31 DECEMBER 2008**

| | As stated in 2008 Annual Report $'000 | Restatement $'000 | As restated $'000 |
|---|---|---|---|
| **Cash flows from operating activities:** | | | |
| Operating loss | (11,166) | 4,295 | (6,871) |
| Depreciation, depletion and amortisation | 8,953 | (602) | 8,351 |
| Impairment charge | 6,327 | (4,672) | 1,655 |
| Decommissioning costs paid in excess of provision | 2,987 | - | 2,987 |
| Share-based payment charge | 12,572 | - | 12,572 |
| Loss on disposal of assets | 9 | - | 9 |
| Increase in receivables | (4,066) | - | (4,066) |
| Increase in payables | 4,781 | (109) | 4,672 |
| Increase in inventory | (2,401) | 2,401 | - |
| **Net cash from operations** | 17,996 | 1,313 | 19,309 |
| Interest received | 1,229 | - | 1,229 |
| Taxation paid | (524) | - | (524) |
| **Net cash from operating activities** | 18,701 | 1,313 | 20,014 |
| **Investing activities** | | | |
| Exploration and evaluation expenditure | (645) | (1,117) | (1,762) |
| Oil and gas properties expenditure | (16,157) | 2,205 | (13,952) |
| Increase in inventory | - | (2,401) | (2,401) |
| Other capital expenditures | (923) | - | (923) |
| Change in long term financial assets | 2,911 | - | 2,911 |
| Decommissioning costs paid | (5,566) | - | (5,566) |
| **Net cash used in investing activties** | (20,380) | (1,313) | (21,693) |
| **Financing activities** | | | |
| Cash proceeds from issue of shares | 19,958 | - | 19,958 |
| **Net cash from financing activities** | 19,958 | - | 19,958 |
| **Increase in cash and cash equivalents** | 18,279 | - | 18,279 |
| Cash and cash equivalents at beginning of year | 18,533 | - | 18,533 |
| Cash and cash equivalents at end of year | 36,812 | - | 36,812 |

**CONSOLIDATED CASH FLOW STATEMENT**
**FOR THE YEAR ENDED 31 DECEMBER 2007**

| | As stated in 2008 Annual Report $'000 | Restatement $'000 | As restated $'000 |
|---|---|---|---|
| **Cash flows from operating activities:** | | | |
| Operating profit | 1,983 | (1,471) | 512 |
| Depreciation, depletion and amortisation | 6,541 | (687) | 5,854 |
| Impairment charge | 1,418 | (217) | 1,201 |
| Decommissioning costs paid in excess of provision | 1,640 | - | 1,640 |
| Share-based payment charge | 882 | - | 882 |
| Non-cash bonus | 252 | - | 252 |
| Loss on disposal of assets | 2 | - | 2 |
| Increase in receivables | (2,265) | - | (2,265) |
| Decrease in payables | (5,398) | (774) | (6,172) |
| **Net cash from operations** | 5,055 | (3,149) | 1,906 |
| Interest received | 1,190 | - | 1,190 |
| Taxation paid | (356) | - | (356) |
| **Net cash from operating activities** | 5,889 | (3,149) | 2,740 |
| **Investing activities** | | | |
| Exploration and evaluation expenditure | (13,510) | 675 | (12,835) |
| Oil and gas properties expenditure | (5,275) | 2,474 | (2,801) |
| Other capital expenditures | (46) | - | (46) |
| Change in long term financial assets | (3,181) | - | (3,181) |
| Decommissioning costs paid | (2,752) | - | (2,752) |
| **Net cash used in investing activties** | (24,764) | 3,149 | (21,615) |
| **Financing activities** | | | |
| Cash proceeds from issue of shares | 23,831 | - | 23,831 |
| Share issue costs | (250) | - | (250) |
| **Net cash from financing activities** | 23,581 | - | 23,581 |
| **Increase in cash and cash equivalents** | 4,706 | - | 4,706 |
| Cash and cash equivalents at beginning of year | 13,827 | - | 13,827 |
| Cash and cash equivalents at end of year | 18,533 | - | 18,533 |

**CONSOLIDATED CASH FLOW STATEMENT**
**FOR THE YEAR ENDED 31 DECEMBER 2006**

| | As stated in 2008 Annual Report $' 000 | Restatement $' 000 | As restated $' 000 |
|---|---|---|---|
| **Cash flows from operating activities:** | | | |
| Operating loss | (5,207) | (5,430) | (10,637) |
| Depreciation, depletion and amortisation | 11,693 | (534) | 11,159 |
| Impairment charge | 4,135 | (424) | 3,711 |
| Decommissioning costs paid in excess of provision | 969 | - | 969 |
| Share-based payment charge | 851 | - | 851 |
| Increase in receivables | (3,888) | - | (3,888) |
| Increase in payables | 7,441 | 718 | 8,159 |
| **Net cash from operations** | 15,994 | (5,670) | 10,324 |
| Interest received | 1,193 | - | 1,193 |
| Taxation paid | (1,111) | - | (1,111) |
| **Net cash from operating activities** | 16,076 | (5,670) | 10,406 |
| **Investing activities** | | | |
| Exploration and evaluation expenditure | (9,375) | 839 | (8,536) |
| Oil and gas properties expenditure | (17,896) | 4,831 | (13,065) |
| Purchase of minority interest | (277) | - | (277) |
| Other capital expenditures | (234) | - | (234) |
| Change in long term financial assets | 1,691 | - | 1,691 |
| Decommissioning costs paid | (2,062) | - | (2,062) |
| **Net cash used in investing activities** | (28,153) | 5,670 | (22,483) |
| **Financing activities** | | | |
| Cash proceeds from issue of shares | 3,931 | - | 3,931 |
| **Net cash from financing activities** | 3,931 | - | 3,931 |
| **Decrease in cash and cash equivalents** | (8,146) | - | (8,146) |
| Cash and cash equivalents at beginning of year | 21,973 | - | 21,973 |
| Cash and cash equivalents at end of year | 13,827 | - | 13,827 |

**Four Year Summary**

| | | 2009 | 2008 (restated) | 2007 (restated) | 2006 (restated) |
|---|---|---|---|---|---|
| Production | | | | | |
| Production - Working Interest | mmboe | 2.7 | 1.2 | 0.8 | 0.8 |
| Production - Entitlement | mmboe | 1.6 | 0.8 | 0.7 | 0.6 |
| | | | | | |
| Summary income statement | | | | | |
| Revenue | $ MM | 84.4 | 53.6 | 37.3 | 33.9 |
| Operating profit / (loss) | $ MM | 28.6 | (6.9) | 0.5 | (10.6) |
| Net profit / (loss) to shareholders | $ MM | 27.8 | (5.4) | (2.7) | (12.7) |
| Basic earnings / (loss) per share | US cents | 23.32 | (4.65) | (2.50) | (13.25) |
| | | | | | |
| Summary cash flow statement | | | | | |
| Net cash from operating activities | $ MM | 43.5 | 20.0 | 2.7 | 10.4 |
| Net cash used in investing activities | $ MM | (26.3) | (21.7) | (21.5) | (22.5) |
| Net cash from financing activities | $ MM | 3.6 | 20.0 | 23.6 | 3.9 |
| Net increase in cash & cash equivalents | $ MM | 20.8 | 18.3 | 4.7 | (8.2) |
| | | | | | |
| Summary balance sheet | | | | | |
| Total assets | $ MM | 185.3 | 145.3 | 117.0 | 97.5 |
| Shareholders equity | $ MM | 140.3 | 107.8 | 80.6 | 58.6 |
| Cash and cash equivalents less debt | $ MM | 57.6 | 36.8 | 18.5 | 13.8 |

# Gulfsands Petroleum plc

## Glossary of terms

| | |
|---|---|
| 2D seismic | Seismic data, obtained using a sound source and receivers placed in a straight line on the surface of the earth, that is processed to provide a graphic representation of a vertical cross-section through the subsurface rock layers (“seismic line”). In a 2D seismic survey, several seismic lines are recorded and the cross-sections are interpolated to yield subsurface maps on which exploration prospects can be delineated |
| 2P | Proved and probable reserves |
| 3D seismic | In a 3D seismic survey, multiple closely spaced seismic lines are recorded and the high density of cross sections are interpolated to yield detailed subsurface maps on which exploration prospects can be delineated |
| Appraisal well | An appraisal well is drilled to assess the characteristics (e.g. flow rate) of a proven oil and gas accumulation |
| bbl | Barrel of oil |
| bcf | Billion cubic feet of gas |
| bfpd | Barrels of fluid per day |
| boe | Barrels of oil equivalent where the gas component is converted into an equivalent amount of oil using a conversion rate of 6mcf to one barrel of oil |
| boepd | Barrels of oil equivalent per day |
| bopd | Barrels of oil per day |
| CPF | Central Production Facility |
| CSR | Corporate Social Responsibility |
| Development well | A development well is drilled within the proved area of an oil or gas reservoir to the depth of the stratigraphic horizon known to be productive. |
| DPC | Dijla Petroleum Company |
| E&P | Exploration and Production |
| EPF | Early Production Facility |
| Exploration well | An exploration well is drilled to find and produce oil or gas in an unproved area, to find a reservoir in a field previously found to be productive of oil or gas in another reservoir, or to extend a known reservoir |
| HSE | Health, Safety and Environment |
| GPC | General Petroleum Company |
| $Km^2$ | Square kilometres |
| KPI | Key Performance Indicators |
| mcf | Thousand cubic feet of gas |
| MENA | Middle East and North Africa |
| mmbbl | Millions of barrels of oil |
| mmboe | Millions of barrels of oil equivalent |
| NGLs | Natural Gas Liquids |
| NGO | Non-governmental organisation |
| NRI | Net revenue Interest |
| OMB | The Oil Marketing Bureau of the Government of the Syrian Arab Republic |
| P+P | Proved and Probable reserves |
| Probable reserves | Probable reserves are those unproved reserves which analysis of geological and engineering data suggests are more likely than not to be recoverable. In this context, when probabilistic methods are used, there should be more than a 50% probability that the quantities actually recovered will equal or exceed the sum of estimated proved plus probable reserves |

| | |
|---|---|
| Proved reserves | Proved reserves are those quantities of petroleum which, by analysis of geological and engineering data, can be estimated with reasonable certainty (normally over 90% if measured on a probabilistic basis) to be commercially recoverable, from a given date forward, from known reservoirs and under current economic conditions, operating methods, and government regulations |
| PSC | Production Sharing Contract |
| psi | Pounds per square inch (pressure) |
| SPC | Syrian Petroleum Company |
| SPE | Society of Petroleum Engineers |
| WI | Working Interest |
| WPC | World Petroleum Congress |

# Gulfsands Petroleum plc

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**COMPANY NUMBER**

5302880

**STOCK EXCHANGE LISTING**

AIM market of London Stock Exchange
Symbol : GPX