# Magnolia Petroleum plc
# Annual Report
# 2011

**MAGNOLIA PETROLEUM PLC**

**ANNUAL REPORT AND FINANCIAL STATEMENTS**

**FOR THE YEAR ENDED**

**31 DECEMBER 2011**

# CONTENTS

| | |
|---|---|
| **Directors** | Dr John Malcolm Cubitt (Non-Executive Chairman)<br>Steven Otis Snead (Chief Executive Officer)<br>Rita Fern Whittington (Chief Operations Officer)<br>Gavin John Burnell (Non-Executive Director)<br>Ronald Sanford Harwood (Non-Executive Director) |
| **Secretary** | Stanley Anthony Salter |
| **Registered Office** | The Fitzpatrick Building<br>188-194 York Way<br>London N7 9AS |
| **Nominated Advisor & Broker** | Daniel Stewart & Company Plc<br>Becket House<br>36 Old Jewry<br>London EC2R 8DD |
| **Joint Broker** | Northland Capital Partners Limited<br>60 Gresham Street<br>London EC2V 7BB |
| **Legal Advisors** | Duane Morris<br>10 Chiswell Street<br>London EC1Y 4UQ<br><br>Pray Walker, P.C.<br>100 W.5th Street<br>Suite 900<br>Tulsa<br>OK 74103, USA |
| **Auditors** | Littlejohn LLP<br>Statutory Auditor<br>1 Westferry Circus<br>Canary Wharf<br>London E14 4HD |
| **Registrars** | Share Registrars Limited<br>Suite E, First Floor<br>9 Lion and Lamb Yard<br>Farnham<br>Surrey GU9 7LL |
| **Registered Number** | 05566066 |

The year under review has seen considerable progress made towards achieving our goal of transforming Magnolia into a significant US onshore oil and gas company. 2012 promises to be a year in which material increases in production and revenues attributable to the Company will be made.

Magnolia offers shareholders the opportunity to participate in the booming US onshore oil and gas industry, which has the potential to transform the US into a net exporter of oil and gas by the end of the decade. The Company's disciplined focus on proven, producing plays, where modern techniques such as horizontal drilling and fracture stimulation can be applied to improve recovery rates, lowers exploration risk and increases returns. Meanwhile, participating in numerous wells with leading operators such as Marathon Oil and ExxonMobil reduces execution risk. Finally, prioritising oil over gas plays enables higher prices and revenues to be realised.

In October 2011, the AIM Admission document laid out the Company's two pronged growth strategy: to continue to increase net production by participating in wells with established operators on our existing acreage in the Bakken and Three Forks Sanish plays in North Dakota, and the Woodford / Hunton formations in Oklahoma; and to acquire leases to drill and operate horizontal wells in the reopening Mississippi Lime formation in Oklahoma.

We have made excellent progress delivering on key objectives in order to fulfil our investment strategy. 31 out of 32 wells in which Magnolia has participated since the Company's inception in 2008 have produced a positive return on capital. This tremendous success rate goes some way towards validating our low risk / high return business model and gives us confidence for the year ahead, as we scale up our activities by increasing the number of wells in which we participate, as well as raise our average level of working interests. Magnolia now has interests in 74 producing properties and we are awaiting the results of a further three wells which are in drilling and completion phases. A number of these wells have larger working interests that Magnolia has secured historically, including the Thomason well in which Magnolia has a 9.375% net revenue interest. We expect these to add materially to our daily production and revenues in the current year.

At the same time, Magnolia remains on track to operate its first well in 2012. A licence to operate wells in Oklahoma was secured during the year, as well as exclusive rights over five prospects targeting the reopening Mississippi Lime formation in Oklahoma. Since the year end, we have acquired 3,540 net mineral acres located within the boundaries of the oil play with an average net revenue interest of 11.1%.

Around the time of our listing last year, we commissioned Moyes & Co to undertake a Competent Person's Report ('CPR') on our existing interests. The CPR assigned a Net Present Value after applying a 10% discount rate of approximately £11m to our 2P reserves at the time, a figure that stands at a premium to our current market capitalisation.

In the CPR, a low rating was assigned to our Three Forks Sanish ("TFS") reserves due to our lack of participation in drilling this emerging play in North Dakota that, due to excellent well results, is increasingly being viewed on a par with the headline grabbing Bakken that lies above it. Aside from generating our best ever initial production rate of 2,303 bopd (received in March 2012), Skunk Creek, our first well targeting TFS, was singled out in our CPR as the trigger for an upgrade in the status of our TFS reserves. We intend to commission a follow-up CPR in the first quarter of 2013 which is expected to incorporate a TFS reserves upgrade as well as our newly acquired Mississippi Lime acreage. The directors expect this updated CPR to materially increase our net asset value.

By the end of the twelve month period, Magnolia had interests in 64 producing properties, generating revenues of approximately US$20,000 per month and $241,038 total revenues for the year as a whole. As mentioned earlier, further progress has been made since the year end, with the number of Magnolia's producing properties rising to 74. Average monthly revenues in the first three months of the year have increased to approximately $35,000 but this excludes several new wells, including the two Eckelberg wells and the Thomason well. Costs continue to be tightly managed, allowing the vast majority of additional revenues generated to be recycled into further wells or acquiring additional leases.

The current financial year is already proving to be tremendously exciting. The months ahead will continue to see Magnolia participating in wells on our existing acreage with leading operators but, crucially, we remain on track to drill our first well as operator in Oklahoma with a larger working interest than has historically been the case. We therefore expect to see a step up in production, revenues and reserves in 2012, all of which are required ingredients for Magnolia to become a significant oil and gas company.

Finally, I would like to thank the management team, directors and all our advisors for their dedication and hard work over the last twelve months and also our shareholders for their active and continued support. The year just passed has seen much activity and the year ahead promises much of the same.

Steven Snead
Chief Executive Officer

21 May 2012

**The Bakken / Three Forks Sanish Formations, North Dakota**

During the year under review, the Company elected to participate in seven wells targeting the Bakken and TFS formations, North Dakota, bringing the total number of wells in which Magnolia has an interest in these two formations to 21, all of which are now producing.

Oil was first discovered in the Bakken shale in 1951. The advent of horizontal drilling in the 1980s, together with improved hydraulic fracturing techniques, led to the shale becoming a significant target for oil and gas, and post 2000, activity has significantly increased. Daily production is estimated to exceed 700,000 bopd by 2013 and to top 1.2 MMbopd by 2019. The 2008 US Geological Survey ('USGS') estimates that mean undiscovered recoverable volumes of 3.65 Bbbls and 1.85 Tcf are contained in the Bakken Shale of Montana and North Dakota. The latter is the main centre of Bakken Shale activity, where there are over 4,000 active wells.

The results of our participated wells targeting the Bakken have highlighted the potential prolific nature of this formation. For example, in November 2011, we received the initial production rates for the Drone#1 - 34H well, which came in at 1,199 bopd and 441mcf per day, resulting in a major uplift in net daily production. Post year end, we reported an initial production rate of 1,263 bopd and 625 mcf for the Eckelberg 14-23H also targeting the Bakken.

The period under review also saw Magnolia participate in a first well, the Skunk Creek 15H, targeting the TFS. A state study evaluating oil reserves in this formation in western North Dakota concluded that there could be as much as 2 billion barrels of recoverable oil in the TFS. The projection is based on more than 200 well measurement logs and 85 sets of testimony from technical experts. At 2,303 bopd, the Skunk Creek 15H well reported the best ever initial production rate for the Company. Significantly, Skunk Creek is expected to lead to a TFS reserves upgrade in an updated CPR to be commissioned in Q1 2013.

Magnolia holds leases in respect of 33,920 gross acres across 28 sections, equating to 557 net mineral acres within the boundaries of the Bakken / TFS formations. The Company's acreage includes 197 proven development locations, 92 on the Bakken and the remaining 105 on the TFS acreage.

**Mississippi Lime Formation, Oklahoma**

The directors identified the Mississippi Lime formation in Oklahoma as having the potential to be the next big US onshore oil play. The Mississippi is a proven commercial oil and gas system that has been producing at shallow depths ranging from 4,500 to 7,000 feet below the surface from several thousand vertical wells for more than 50 years. New technology and horizontal drilling has reopened the oil play. Due to the relatively shallow depths and less tight rock formation, drilling costs at between \$2.4 and \$3.5 million are considerably lower than those in the Bakken. Horizontal wells generally have shorter lateral lengths of between 2,500ft and 5,000ft and are fracture stimulated in 6-12 stages – less than those in the Bakken play. Drilling times are relatively short at between 17 and 28 days from spud to total depth.

In October 2011, the Company executed an agreement with a local geologist to develop five prospects covering an area of approximately 80 square miles. Post year end, Magnolia has acquired 3,540 net mineral acres in the play with average net revenue interests of 11.1%, considerably higher than historical levels. One of the five prospects identified by the geologist is included in this acreage.

During the year, Magnolia was granted a licence to operate wells in Oklahoma, which confers to the Company control of timing the proposing, drilling, and producing of wells. Among the acreage acquired post year end in the play are leases with working interests of up to 100% which have the right to operate wells. The Company intends to drill and operate its first well on this acreage in the current year.

Since the year end, Magnolia has elected to participate in nine wells targeting the Mississippi formation. On one of these, the Thomason operated by Chesapeake Energy, Magnolia holds a 12.5% working interest. The well has been completed and is currently producing with initial production rates awaited. Three more are in drilling and five are waiting to spud.

**Woodford / Hunton Formations, Oklahoma**

Like the Bakken, the Woodford / Hunton formations in Oklahoma are established reservoirs that have been reopened following the introduction of horizontal drilling and stimulation technology. As a result the Woodford oil play in particular is increasingly being drilled by leading operators. Magnolia holds leases in respect of approximately 57,600 gross mineral acres (702 net mineral acres), giving rights to participate in the drilling of wells in 87 sections located in 26 counties in central Oklahoma.

During the year under review, Magnolia participated in the drilling of five wells in the formation, bringing the overall total to 19. Since the year end, five new wells were completed and the company has elected to participate in a further two wells with Cimarex.

**Summary**

In total the Company has 74 producing wells, for which the Company hope to announce average production rates in the second quarter 2012, with three wells in drilling / awaiting completion and seven wells waiting to spud. The Company is reviewing a large number of additional well proposals which, if the Company elected participate, could result in the company achieving its target of 100 producing wells by the end of 2012.

Rita Whittington
Chief Operations Officer

21 May 2012

The Directors present their Annual Report and the Financial Statements for the year ended 31 December 2011.

**Principal activities and review of the business**

The principal activity of the Group is onshore oil and gas exploration and production in the United States of America. The Company acts as a holding company and provides technical and other services to its subsidiary.

The Company subsidiary is Magnolia Petroleum Inc. (“Magnolia”), an independent oil and gas exploration and production company based near Tulsa, Oklahoma, USA. Magnolia’s core area of business is in the Bakken/Three Forks Sanish area in North Dakota, the emerging Mississippi Formation in Oklahoma and the Woodford/Hunton oil and gas formations in Oklahoma, United States.

A business and financial review of operations for the financial year 2011 as well as the future developments of the Group are included in the Chief Executive Officer’s and Chief Operations Officer’s Statement.

**Results and dividends**

The loss for the year after taxation was $342,447(2010 – loss $59,114).

The Directors do not recommend the payment of a dividend.

**Political and charitable contributions**

During the period the Company did not make any payments for charitable or political purposes.

**Going Concern**

The Directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future and, therefore, continue to adopt the going concern basis in preparing the Annual Report and Financial Statements. Further details on their assumptions and their conclusion thereon are included in the statement on going concern included in Note 2 to the Financial Statements.

**Risks and uncertainties**

The Group’s activities expose it to a variety of risks and uncertainties.

*Market risk*

The Group operates in an international market for hydrocarbons and is exposed to risk arising from variations in the demand for and price of the hydrocarbons. Oil and gas prices historically have fluctuated widely and are affected by numerous factors over which the Group does not have any control, including world production levels, international economic trends, currency exchange fluctuations, inflation, speculative activity, consumption patterns and global or regional political events.

**Risks and uncertainties (continued)**

*Non-operator risk*

On non-operated interests, the Group has no influence on the timing of drilling of the oil and gas wells in which it participates and will depend on operators to initiate and supervise the drilling and operation of such wells. As such the Group cannot accurately predict the timing of the cash flows associated with the drilling of these wells. If the Group is unable or unwilling to comply with its payment obligations, it would seek to negotiate a wellbore assignment of the lease, thus retaining the right to participate in future wells that may be drilled on that acreage. If an assignment could not be negotiated, the Group would lose the right to participate in the acreage if it does not participate in the original well. This could have an adverse affect on the Group's future revenues and earnings.

*Oil and gas exploration and production risks*

The Group is primarily a non-operator working interest owner and is reliant on the operator for managing all aspects of its exploration and production activities in its non-operated interests. There are significant risks and hazards inherent in the exploration and production of oil and gas, including environmental hazards, industrial incidents, labour disputes, fire, drought, flooding and other acts of God. The occurrence of any of these hazards can delay or interrupt production and increase production costs. There is no guarantee that oil and/or gas will be discovered in any of the Group's existing or future licences/permitted acreage or that commercial quantities of oil and/or gas can be recovered.

The Group currently holds less than a 100 per cent working interest in its completed wells and in wells which are being drilled. It is also likely to hold less than 100 per cent in wells which may be drilled in the future. The Group could be held liable for the joint activity obligations of the other working interest owners, such as non-payment of costs and liabilities arising from the actions of those other working interest owners. In the event that other working interest owners do not pay their share of such costs, the Group would be likely to have to pay those costs.

*Environmental risk*

The Group's operations are subject to environmental regulation in all the jurisdictions in which it operates. The Group is unable to predict the effect of additional environmental laws and regulations which may be adopted in the future, including whether any such laws or regulations would adversely affect the Group's operations. There can be no assurance that such new environmental legislation once implemented will not oblige the Group to incur significant expenses and undertake significant investments.

*Licences and title*

The leases in which the Group has or is seeking to have an interest will be subject to termination after the primary term of such leases unless there is current production of oil and/or gas in commercial quantities. If a lease is not extended after the primary term, the Group may lose the opportunity to develop and discover any hydrocarbon resources on that lease area. In taking an assignment of an oil and/or gas lease, the Group would, in accordance with industry practice, rely on the warranty provisions and would not perform a title check in respect of previous assignments or the title of the original mineral rights lessor. Other parties may therefore dispute the Group's title to its properties.

**Risks and uncertainties (continued)**

*Decommissioning*

The full extent to which the decommissioning provision is required depends on the legal requirements at the time of decommissioning, the costs, location and timing of any decommissioning works and the discount rate applied to such costs.

Financial risk management disclosures are included in Note 3 of the Financial Statements.

**Directors and Directors' interests**

The Directors who held office during the year to the date of approval of these Financial Statements, together with their beneficial interests in the ordinary shares of the Company, are shown below.

| | 31 December 2011 | | 01 January 2011 | |
|---|---|---|---|---|
| | **Ordinary Shares** | **Options and warrants** | **Ordinary Shares** | **Options and warrants** |
| Gavin J Burnell (1) | 13,950,503 | 11,220,768 | 12,132,323 | 11,220,768 |
| Dr John M Cubitt | 384,614 | 4,400,000 | 384,614 | 4,400,000 |
| Steven Otis Snead (2) | 197,436,360 | 14,110,000 | 193,800,000 | 28,220,000 |
| Rita Fern Whittington | 11,400,000 | 10,126,000 | 11,400,000 | 1,660,000 |
| Ronald Sanford Harwood (3) | 24,618,180 | 1,660,000 | 22,800,000 | 3,320,000 |

(1) Figures at 1 January and 31 December 2011 included 830,000 ordinary shares owned by Elizabeth Burnell, the wife of Gavin Burnell.

(2) Includes 91,200,000 ordinary shares owned by the Snead Family LLC and 11,400,000 ordinary shares owned by R. Sterling Snead.

(3) Ronald Sanford Harwood's shares are held by the Ronald S. Harwood Trust.

**Dr John Malcolm Cubitt, Non-Executive Chairman**

Dr John Cubitt has more than 30 years' commercial experience in the oil exploration and production industry, following a period in academic research and graduate/post-graduate education in the UK and USA. He is a registered Chartered Geologist (CGeol) and has a BSc and PhD in geology. His experience has included asset evaluation and project management, as well as board-level strategic and operational direction. Until December 2011 he was Managing Director of Woburn Energy Plc (formerly Black Rock Oil and Gas Plc), an AIM-listed oil and gas exploration company whose primary assets are in the United Kingdom and Colombia. He is also a director of ES Information & Consultancy Limited, an exploration and production consultancy, and of Terrasciences Inc, an oil industry software house.

**Steven Otis Snead, Chief Executive Officer**

Mr Snead is a Certified Professional Landman with 34 years' experience in the oil and gas industry. In 1980 he founded Energy Land Services Inc., an oil and gas service company that was contracted by small and medium-sized oil companies to perform title research, determine owners of mineral interests in a prospective drilling area, and then purchase leases from those mineral owners or negotiate agreements with other exploration companies. Energy Land Services also obtained permits or regulatory agency approvals, and secured necessary title curative to ensure clear title to ownership of wells. Energy Land Services, which employed up to 32 landmen and support staff, was sold to its employees in 1989, and still operates today.

**Directors and Directors' interests (continued)**

**Steven Otis Snead, Chief Executive Officer (continued)**

In 1984, he founded (and still owns and operates) Enerlex Inc. ("Enerlex") for the purpose of purchasing and managing royalty interests. In 1987, he acquired Magnolia Petroleum Limited, an exploration and production company which at that time had over 30 operated wells in Oklahoma. By 1999, when the properties were profitably sold, Magnolia Petroleum Limited had acquired, drilled and managed working interests (operated and non-operated) in over 200 wells. The company was then liquidated solvently, but Mr Snead retained the rights to the name "Magnolia Petroleum".

In 1988 he co-founded International Searchers Inc. ("ISI"), a research company that located and recovered unpaid royalties or uncollected assets. ISI recovered significant royalties and assets for its clients and had a research process that allowed it to identify royalty owners in wells throughout the United States. In 2000, Enerlex acquired ISI's research process and its proprietary database of 2.25 million names and addresses of royalty owners which is used by Enerlex to identify royalty interests available for acquisition.

**Rita Fern Whittington, Chief Operating Officer**

Mrs Whittington is a petroleum landman with more than 30 years' experience in acquisition, operations and management of oil and gas properties.

She began her career in 1977 working for an Oklahoma based oil exploration company where she became a prospect manager. In 1985, she joined Kaiser-Francis Oil Company in Oklahoma as a land supervisor. Between 1987 and 1989, she acted as a title analyst for Terra Resources Inc. specialising in Gulf Coast, Texas and Louisiana properties. In 1989, she joined Enerlex Inc. as vice president where she spent nine years negotiating and purchasing thousands of mineral acres. From 1998 to 2001, she was land administrator for Brighton Energy LLC, focusing on building the company's portfolio through acquisitions and disposals. In 2001, she joined Primary Natural Resources, Inc as a primary member of the asset management team, developing and expanding the company until it sold its assets in 2003. It commenced business again in 2004 and sold its assets in 2008.

**Gavin John Burnell, Non-Executive Director**

Mr Burnell has specialised in advising smaller capitalised companies for the last eleven years having joined Ruegg & Co in 2001, which was later purchased by Astaire Group plc. He is now a director of corporate finance at Northland Capital Partners, responsible for maintaining client relationships with a number of AIM-quoted corporate clients. He was a founder shareholder and non-executive director of Stratex International Plc, an AIM-traded resources company with gold exploration properties in Turkey and Ethiopia and a non-executive director of Iceni Oil and Gas Limited, a private company with North Sea oil and gas exploration projects which was acquired by Bridge Resources Corp., a company listed on the Toronto Stock Exchange. He was a founder and non-executive director of Silvrex Limited a gold exploration company active in Senegal, West Africa sold to Stratex International Plc in 2011. He is also a founder and non-executive director of Hot Rocks Investments Plc and Hellenic Capital Plc, both PLUS-quoted companies and a non-executive director of Globo Plc, an AIM-listed software company.

**Ronald Sanford Harwood, Non-Executive Director**

Mr Harwood graduated in 1957 from Wharton School of Finance and Commerce, University of Pennsylvania, with a Bachelor of Science degree in Economics. During the course of his extensive business career, he has had active involvement in originating and developing projects in a wide range of sectors, mainly in oil and gas exploration and production (since 1981) but also in financial and business development services, telecommunications, computer software, power generation and specialty chemicals.

**Directors and Directors' interests (continued)**

**Ronald Sanford Harwood, Non-Executive Director (continued)**

In 1961, he founded Allstates Capital Corporation to provide a comprehensive range of commercial finance services to small and medium sized companies. In 1979, he sold his 100 per cent shareholding in the company to a regional One Bank holding company. In 1981, he founded Nemaha Exploration Inc. as an independent exploration and production company, and operator. Under his leadership as President and CEO, Nemaha drilled a number of prospects and leased and farmed out acreage to other operators to drill. In 1983, the company was, by agreement, liquidated.

In 1984, together with a partner, he founded MRI Production Inc. to acquire the oil and gas assets of Mahan-Rowsey Inc. of Oklahoma City. In 1986, all the company's oil and gas assets were sold to the American subsidiary of a UK oil and gas company. In 1985, he founded Bellwood Petroleum Corporation ("BPC") which participated as a non-operator working interest owner in wells drilled and properties purchased by numerous independent oil and gas operators. In 2007, BPC sold all its interests and changed its name to Bellwood International Corporation, carrying on the consulting services business previously undertaken through a different company owned by Mr. Harwood. In 2008, he formed Bellwood Petroleum LLC to carry on the oil and gas royalty business previously undertaken through a Mr. Harwood-owned trust.

In 1991, he founded Colony Petroleum Corporation (subsequently Colony Petroleum LLC), acting as President and CEO. The company was an investment fund that secured US and international equity investors, as well as bank credit lines, to participate in oil and gas exploration and production ventures originated and operated by American and Canadian independent oil and gas companies. In 1999, he sold his shareholding back to Colony Petroleum LLC.

**Substantial interests**

As of 16 May 2012, the following interests of three percent or more of the issued ordinary share capital had been notified to the Company:

| | **%** | **Number of ordinary shares** |
|---|---|---|
| Steven Otis Snead | 29.75 | 198,974,820 |
| TD Direct Investing Nominees (Europe) Limited | 5.42 | 36,282,570 |
| Barclayshare Nominees Limited | 5.31 | 35,507,956 |
| Ronald Sanford Harwood | 4.12 | 27,541,250 |
| HSDL Nominees Limited | 3.77 | 25,183,437 |
| Sunvest Corporation Limited | 3.74 | 25,000,000 |
| BBHISL Nominees Limited | 3.27 | 21,850,470 |

**Key performance indicators**

The Board monitors the overall performance of the Group by reference to Key Performance Indicators ("KPIs"). KPIs for the year, together with comparative data, are presented below:

| | **2011** | **2010** |
|---|---|---|
| Revenue | $241,038 | $238,097 |
| Gross profit margin | 39.7% | 62.1% |

Participations in well drilling programmes are monitored on an individual project basis in terms of revenue and cost per barrel of oil or mcf (one thousand cubic feet) of gas, together with the anticipated payback period on each project.

**Supplier payment policy**

Whilst there is no formal code or standard, it is Company policy to settle terms of payment with creditors when agreeing the terms of each transaction and to abide by the creditors' terms of payment. There are no creditors subject to special arrangements outside of suppliers' terms and conditions except those creditors which are party to the Deferral Amendment Agreement dated 15 November 2011. Under this agreement, payment of certain fees and expenses are deferred until 23 April 2013.

At 31 December 2011 the number of creditor days in respect of trade creditors was 101 (2010: 89).

**Directors' and Officers' Indemnity Insurance**

The Company has made qualifying third-party indemnity provisions for the benefit of its Directors and Officers. These were made during the previous period and remain in force at the date of this report.

**Post Balance Sheet Events**

The post balance sheet events are set out in note 21 to the Financial Statements.

**Provision of information to auditors**

So far as each of the Directors is aware at the time this report is approved:

- there is no relevant audit information of which the Company's auditors are unaware; and
- the Directors have taken all 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.

**Auditors**

Littlejohn LLP has signified its willingness to continue in office as auditors.

**ANNUAL GENERAL MEETING – EXPLANATION OF BUSINESS**

The 2012 annual general meeting will be held at 10.00am on Friday 29 June at 18452 E 111th, Broken Arrow, Oklahoma, OK74011, USA. The notice of meeting is set out on pages 49 - 51 of this document and a form of proxy is enclosed.

Details of the business to be considered at the meeting are given below.

Resolution 1 is to receive the annual report and accounts. Resolutions 2 and 3 concern Gavin Burnell and Steven Snead, who retire by rotation and offer themselves for re-election as directors. Resolution 4 is to reappoint Littlejohn LLP as auditors and to authorise the directors to set their fees.

Authority of directors to allot shares (Resolutions 5 and 6)

Under UK law, directors are not permitted to allot new shares (or to grant rights over shares) unless they are authorised to do so by shareholders. In addition, directors require specific authority from shareholders before allotting new shares (or granting rights over shares) for cash without first offering them to existing shareholders in proportion to their holdings. Resolution 5 gives the directors the necessary authority to allot up to a maximum of 334,400,000 relevant securities. This represents approximately 50% of the current issued ordinary share capital.

Resolution 6 empowers the directors to allot such securities for cash otherwise than on a pro-rata basis to existing shareholders, up to a maximum of 334,400,000 ordinary shares of 0.1p each, equivalent to 50% of the current issued ordinary share capital. These authorities will continue in force until the AGM to be held in 2013 or 30 June 2013, whichever is the earlier.

Authority for the Company to purchase its own shares (Resolution 7)

Resolution 7 authorises the Company, until next year's AGM or 30 June 2013 (whichever is earlier) to purchase in the market up to a maximum of 100,332,148 ordinary shares (equivalent to approximately 15% of the current issued share capital of the Company). The Companies Act 2006 allows the Company to hold any repurchased shares in treasury, instead of cancelling them immediately. If the Company buys back its own shares and holds them in treasury it may then deal with some or all of them in several ways. It may sell them for cash; transfer them under the provisions of an employee share scheme; cancel them; or continue to hold them in treasury. Holding shares in treasury in this way would allow the Company to reissue them quickly and cost effectively, giving increased flexibility to the management of its capital base. Dividends are not paid on shares held in treasury, nor do they carry voting rights while they remain there. The directors intend to decide at the time of any share buyback, whether to cancel the shares immediately or to hold them in treasury, depending on the interests of the Company and its shareholders as a whole, at the time. The Company does not currently hold any shares in treasury.

The proposal should not be taken as an indication that the Company will purchase shares at any particular price or indeed at all, and the directors will only consider making purchases if they believe that such purchases would result in an increase in earnings per share and are in the best interests of shareholders.

It is intended to renew each of the above authorities at each annual general meeting.

This report was approved by the board on 21 May 2012 and signed on its behalf:

**Gavin Burnell**
Director

The Directors are responsible for preparing the Annual Report and the Financial Statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare Financial Statements for each financial year. Under that law the Directors have elected to prepare the Group and Parent Company Financial Statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. Under company law the Directors must not approve the Financial Statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and Company as at the end of the financial year, and of the profit or loss of the Group for that period. In preparing these Financial Statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently; and
- make judgements and accounting estimates that are reasonable and prudent.

The Directors confirm that they have complied with the above requirements in preparing the Financial Statements.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Group and Company and enable them to ensure that the Financial Statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Group and Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

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

**The Board of Directors**
As at 31 December 2011, the Board of Directors comprised five members: two Executive Directors and three Non-Executive Directors including the Chairman, Dr John Cubitt. The Executive Directors have a wealth of experience in the oil and gas industry. Similarly the Non-Executive Directors together have extensive mineral, oil and gas exploration experience and financial experience.

**Board meetings**
The Board ordinarily meets on a monthly basis and as and when further required, providing effective leadership and overall management of the Company's affairs by reference to those matters reserved for its decision. This includes the approval of the budget and business plan, major capital expenditure, acquisitions and disposals, risk management policies and the approval of the financial statements. Formal agendas, papers and reports are sent to the Directors in a timely manner, prior to the Board meetings.

**Corporate governance practices**
The Board recognises the importance of sound corporate governance commensurate with the size of the Company and the interests of Shareholders. As the Company grows, the Directors will develop policies and procedures which reflect the requirements of the Code of Best Practice (commonly known as the "UK Corporate Governance Code"), as published by the Financial Reporting Council so far as is practicable, taking into account the size and nature of the Company.

**Remuneration and audit committees**
The remuneration committee comprise of Ronald Harwood (Chairman), John Cubitt and Gavin Burnell, and is responsible for reviewing the performance of the Executive Directors and for setting the framework and broad policy for the scale and structure of their remuneration taking into account all factors which it shall deem necessary. The remuneration committee also determines the allocation of share options and is responsible for setting up any performance criteria in relation to the exercise of options granted under any share options schemes adopted by the Company.

The audit committee comprise John Cubitt (Chairman), Gavin Burnell and Ronald Harwood, and has primary responsibility for monitoring the quality of internal controls, ensuring that the financial performance of the Company is properly measured and reported on and for reviewing reports from the Company's auditors relating to the Group's accounting and internal controls.

**Internal controls**
The Board recognises the importance of both financial and non-financial controls and has reviewed the Company's control environment and any related shortfalls during the year. Since the Company was established, the Directors are satisfied that, given the current size and activities of the Company, adequate internal controls have been implemented. Whilst they are aware that no system can provide absolute assurance against material misstatement or loss, in light of the current activity and proposed future developments of the Company, continuing reviews of internal controls will be undertaken to ensure that they are adequate and effective.

**Relations with Shareholders**
The Board is committed to providing effective communication with the shareholders of the Company. Significant developments are disseminated through stock exchange announcements and regular updates on the Company website. The Board views the Annual General Meeting as a forum for communication between the Company and its shareholders and encourages their participation in its agenda.

**Independent Auditors' Report to the members of Magnolia Petroleum Plc**

We have audited the Financial Statements of Magnolia Petroleum plc for the year ended 31 December 2011 which comprise the Consolidated Statement of Comprehensive Income, the Consolidated and Parent Company Balance Sheets, the Consolidated and Parent Company Statements of Cash Flow, the Consolidated and Parent Company Statements of Changes in Equity, and the related notes. 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 regards the Parent Company Financial Statements, 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 Directors' Responsibilities Statement, the Directors are responsible for the preparation of the Financial Statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the Financial Statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical 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. In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited Financial Statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

**Opinion on Financial Statements**

In our opinion:

- the Financial Statements give a true and fair view of the state of the Group's and of the Parent Company's affairs as at 31 December 2011 and of the Group's loss 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 matter prescribed by the Companies Act 2006**

In our opinion 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.

**Mark Ling (Senior statutory auditor)**
For and on behalf of Littlejohn LLP
Statutory Auditor

1 Westferry Circus
Canary Wharf
London E14 4HD

21 May 2012

| | Note | Year ended 31 December 2011 $ | Year ended 31 December 2010 $ |
|---|---|---|---|
| **Continuing Operations** | | | |
| Revenue | | 241,038 | 238,097 |
| Operating expenses | | (145,365) | (90,224) |
| **Gross Profit** | | 95,673 | 147,873 |
| Impairment of mineral leases | 10 | (224,892) | - |
| Administrative expenses | 16 | (213,228) | (206,987) |
| **Operating Loss** | 6 | (342,447) | (59,114) |
| Finance income | | - | - |
| Finance costs | | - | - |
| **Loss before Tax** | | (342,447) | (59,114) |
| Taxation | 8 | - | - |
| **Loss for the year** | | (342,447) | (59,114) |
| **Other Comprehensive Income:** | | | |
| Exchange differences on translating foreign operations | | (10,931) | (1,536) |
| **Other Comprehensive Income for the Year, Net of Tax** | | (10,931) | (1,536) |
| **Total Comprehensive Income for the Year** | | (353,378) | (60,650) |
| **Loss per share for loss attributable to the equity holders of the Company during the year** | | | |
| Basic and diluted (cents per share) | 17 | (0.09) | (0.02) |

The Company has elected to take the exemption under Section 408 of the Companies Act 2006 from presenting the Parent Company Statement of Comprehensive Income.

The loss for the Parent Company for the year was $80,574 (2010 - $8,708).

The Notes on pages 25 to 48 form part of these Financial Statements.

## CONSOLIDATED BALANCE SHEET
**As at 31 December 2011**

| | Note | As at 31 December 2011 $ | As at 31 December 2010 $ |
|---|---|---|---|
| **ASSETS** | | | |
| **Non–Current Assets** | | | |
| Property, plant and equipment | 9 | 861,975 | 615,908 |
| Intangible assets | 10 | 1,111,634 | 1,109,988 |
| **Total Non-Current Assets** | | 1,973,609 | 1,725,896 |
| **Current Assets** | | | |
| Trade and other receivables | 12 | 70,308 | 66,200 |
| Cash and cash equivalents | 13 | 874,037 | 97,523 |
| **Total Current Assets** | | 944,345 | 163,723 |
| **TOTAL ASSETS** | | 2,917,954 | 1,889,619 |
| **EQUITY AND LIABILITIES** | | | |
| **Equity attributable to Owners of Parent** | | | |
| Ordinary shares | 14 | 926,128 | 587,336 |
| Share premium | 14 | 2,218,877 | 1,347,983 |
| Warrants and options reserve | | 66,603 | 66,603 |
| Merger reserve | | 1,975,950 | 1,867,790 |
| Reverse acquisition reserve | | (2,250,672) | (2,250,672) |
| Translation reserve | | (126,624) | (115,693) |
| Retained losses | | (502,718) | (160,271) |
| **Total Equity - Capital and Reserves** | | 2,307,544 | 1,343,076 |
| **Non-Current Liabilities** | | | |
| Trade and other payables | 15 | 278,431 | - |
| | | 278,431 | - |
| **Current Liabilities** | | | |
| Trade and other payables | 15 | 331,979 | 546,543 |
| **Total Current Liabilities** | | 331,979 | 546,543 |
| **TOTAL EQUITY AND LIABILITIES** | | 2,917,954 | 1,889,619 |

These Financial Statements were approved by the Board of Directors on 21 May 2012 and were signed on its behalf by:

**Steven Snead**
Chief Executive Officer

**Rita Whittington**
Chief Operations Officer

The Notes on pages 25 to 48 form part of these Financial Statements.

| | Note | As at 31 December 2011 $ | As at 31 December 2010 $ |
|---|---|---|---|
| **ASSETS** | | | |
| **Non–Current Assets** | | | |
| Investments in subsidiaries | 11 | 3,615,907 | 3,662,897 |
| **Total Non–Current Assets** | | 3,615,907 | 3,662,897 |
| **Current Assets** | | | |
| Trade and other receivables | 12 | 1,057,957 | 79,443 |
| Cash and cash equivalents | 13 | 193,788 | 94,226 |
| **Total Current Assets** | | 1,251,745 | 173,669 |
| **TOTAL ASSETS** | | 4,867,652 | 3,836,566 |
| **EQUITY AND LIABILITIES** | | | |
| **Shareholders' Equity** | | | |
| Ordinary shares | 14 | 926,128 | 587,336 |
| Share premium | 14 | 2,218,877 | 1,347,983 |
| Warrants and options reserve | | 66,603 | 66,603 |
| Merger reserve | | 1,975,950 | 1,867,790 |
| Translation reserve | | (425,334) | (372,117) |
| Retained losses | | (234,852) | (154,278) |
| **Total Equity - Capital and Reserves** | | 4,527,372 | 3,343,317 |
| **Non–Current Liabilities** | | | |
| Trade and other payables | 15 | 243,431 | - |
| **Total Non–Current Liabilities** | | 243,431 | - |
| **Current Liabilities** | | | |
| Trade and other payables | 15 | 96,849 | 493,249 |
| **Total Current Liabilities** | | 96,849 | 493,249 |
| **TOTAL EQUITY AND LIABILITIES** | | 4,867,652 | 3,836,566 |

These Financial Statements were approved by the Board of Directors on 21 May 2012 and were signed on its behalf by:

**Steven Snead**
Chief Executive Officer

**Rita Whittington**
Chief Operations Officer

The Notes on pages 25 to 48 form part of these Financial Statements.

| Group ($) | Share capital | Share Premium | Merger reserve | Share option reserve | Reverse acquisition reserve | Translation reserve | Retained earnings | Total equity |
|---|---|---|---|---|---|---|---|---|
| **Balance at 31 December 2009** | **587,336** | **1,347,983** | **1,867,790** | **66,603** | **(2,250,672)** | **(114,157)** | **(101,157)** | **1,403,726** |
| **Comprehensive Income** | | | | | | | | |
| Loss for the period | - | - | - | - | - | - | (59,114) | (59,114) |
| **Other Comprehensive Income** | | | | | | | | |
| Currency translation differences | - | - | - | - | - | (1,536) | - | (1,536) |
| **Total Comprehensive Income for the Year** | - | - | - | - | - | (1,536) | (59,114) | (60,650) |
| **Balance at 31 December 2010** | **587,336** | **1,347,983** | **1,867,790** | **66,603** | **(2,250,672)** | **(115,693)** | **(160,271)** | **1,343,076** |
| **Comprehensive Income** | | | | | | | | |
| Loss for the period | - | - | - | - | - | - | (342,447) | (342,447) |
| **Other Comprehensive Income** | | | | | | | | |
| Currency translation differences | - | - | - | - | - | (10,931) | - | (10,931) |
| **Total Comprehensive Income for the Year** | - | - | - | - | - | (10,931) | (342,447) | (353,378) |
| **Transaction with Owners** | | | | | | | | |
| Proceeds from share issue | 338,792 | 1,524,567 | - | - | - | - | - | 1,863,359 |
| Share issue costs | - | (653,673) | - | - | - | - | - | (653,673) |
| Movements in the year | - | - | 108,160 | - | - | - | - | 108,160 |
| **Total Transactions with Owners** | 338,792 | 870,894 | 108,160 | - | - | - | - | 1,317,846 |
| **Balance at 31 December 2011** | **926,128** | **2,218,877** | **1,975,950** | **66,603** | **(2,250,672)** | **(126,624)** | **(502,718)** | **2,307,544** |

The movement in the merger reserve during the year consisted of the partial write back of a liability and the recovery of input VAT in respect of certain share issue costs incurred in the year ended 31 December 2009.

The Notes on pages 25 to 48 form part of these Financial Statements.

| Company ($) | Share capital | Share Premium | Merger reserve | Share option reserve | Translation reserve | Retained earnings | Total equity |
|---|---|---|---|---|---|---|---|
| **Balance at 31 December 2009** | **587,336** | **1,347,983** | **1,867,790** | **66,603** | **(313,712)** | **(145,570)** | **3,410,430** |
| **Comprehensive Income** | | | | | | | |
| Loss for the period | - | - | - | - | - | (8,708) | (8,708) |
| **Other Comprehensive Income** | | | | | | | |
| Currency translation differences | - | - | - | - | (58,405) | - | (58,405) |
| **Total Comprehensive Income for the Year** | - | - | - | - | (58,405) | (8,708) | (67,113) |
| **Balance at 31 December 2010** | **587,336** | **1,347,983** | **1,867,790** | **66,603** | **(372,117)** | **(154,278)** | **3,343,317** |
| **Comprehensive Income** | | | | | | | |
| Loss for the period | - | - | - | - | - | (80,574) | (80,574) |
| **Other Comprehensive Income** | | | | | | | |
| Currency translation differences | - | - | - | - | (53,217) | - | (53,217) |
| **Total Comprehensive Income for the Year** | - | - | - | - | (53,217) | (80,574) | (133,791) |
| **Transactions with Owners** | | | | | | | |
| Proceeds from share issue | 338,792 | 1,524,567 | - | - | - | - | 1,863,359 |
| Share issue costs | - | (653,673) | - | - | - | - | (653,673) |
| Movements in the year | - | - | 108,160 | - | - | - | 108,160 |
| **Total Transactions with Owners** | 338,792 | 870,894 | 108,160 | - | - | - | 1,317,846 |
| **Balance at 31 December 2011** | **926,128** | **2,218,877** | **1,975,950** | **66,603** | **(425,334)** | **(234,852)** | **4,527,372** |

The Notes on pages 25 to 48 form part of these Financial Statements.

| | Note | Year ended 31 December 2011 $ | Year ended 31 December 2010 $ |
|---|---|---|---|
| **Cash Flows from Operating Activities** | | | |
| Loss before tax | | (342,447) | (59,114) |
| Impairment of mineral leases | | 224,892 | - |
| Depreciation | | 101,284 | 83,916 |
| Foreign exchange | | (781) | - |
| Decrease in trade and other receivables | | 19,619 | 6,257 |
| Increase/(Decrease) in trade and other payables | | 147,892 | (136,205) |
| **Net Cash generated from/(used in) Operating Activities** | | 150,459 | (105,146) |
| | | | |
| **Cash Flows from Investing Activities** | | | |
| Purchases of intangible assets | | (364,998) | (24,447) |
| Purchases of property, plant and equipment | | (213,593) | (12,927) |
| **Net Cash generated used in Investing Activities** | | (578,591) | (37,374) |
| | | | |
| **Cash Flows from Financing Activities** | | | |
| Proceeds from issue of ordinary shares | | 1,863,359 | - |
| Issue costs | | (653,673) | - |
| **Net Cash generated from Financing Activities** | | 1,209,686 | - |
| | | | |
| **Net Increase/(Decrease) in Cash and Cash Equivalents** | | 781,554 | (142,520) |
| | | | |
| **Movement in Cash and Cash Equivalents** | | | |
| Cash and cash equivalents at the beginning of the period | 13 | 97,523 | 245,581 |
| Exchange loss on cash and cash equivalents | | (5,040) | (5,538) |
| Net increase/(decrease) in cash and cash equivalents | | 781,554 | (142,520) |
| **Cash and Cash Equivalents at the End of the Period** | 13 | 874,037 | 97,523 |

The Notes on pages 25 to 48 form part of these Financial Statements.

**COMPANY STATEMENT OF CASH FLOWS**
**Year ended 31 December 2011**

| | Note | Year ended 31 December 2011 $ | Year ended 31 December 2010 $ |
|---|---|---|---|
| **Cash Flows from Operating Activities** | | | |
| Loss before tax | | (80,574) | (8,708) |
| Increase/(decrease) in trade and other receivables | | 5,384 | (294) |
| Decrease in trade and other payables | | (43,942) | (71,763) |
| **Net Cash used in Operating Activities** | | (119,132) | (80,765) |
| **Cash Flows from Financing Activities** | | | |
| Proceeds from issue of ordinary shares | | 1,863,359 | - |
| Issue costs | | (597,139) | - |
| Increase in funding subsidiary undertaking | | (1,042,486) | (44,741) |
| **Net Cash from Financing Activities** | | 223,734 | (44,741) |
| **Net Increase/(Decrease) in Cash and Cash Equivalents** | | 104,602 | (125,506) |
| **Movement in Cash and Cash Equivalents** | | | |
| Cash and cash equivalents at the beginning of the period | 13 | 94,226 | 225,270 |
| Exchange loss on cash and cash equivalents | | (5,040) | (5,538) |
| Net increase/(decrease) in cash and cash equivalents | | 104,602 | (125,506) |
| **Cash and Cash Equivalents at the End of the Period** | 13 | 193,788 | 94,226 |

Share issue costs of $56,534 were paid by the subsidiary undertaking.

The Notes on pages 25 to 48 form part of these Financial Statements.

## 1 GENERAL INFORMATION

The Consolidated Financial Statements of Magnolia Petroleum plc ("the Company") consist of the following companies; Magnolia Petroleum plc and Magnolia Petroleum Inc. (together "the Group").

The Company is a public limited company which is listed on the AIM market and incorporated and domiciled in England and Wales. Its registered office address is The Fitzpatrick Building, 188-194 York Way, London, N7 9AS.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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

### 2.1 Basis of preparation of Financial Statements

The consolidated Financial Statements have been prepared in accordance with EU-endorsed International Financial Reporting Standards (IFRSs) and IFRIC interpretations and the parts of the Companies Act 2006 applicable to companies reporting under IFRS.

The Financial Statements have been prepared under the historical cost convention.

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

### 2.2 Basis of consolidation

The consolidated Financial Statements consolidate the Financial Statements of Magnolia Petroleum plc and the audited Financial Statements of its subsidiary undertaking made up to 31 December 2011.

Subsidiaries are entities over which the Group has control. Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The Group obtains and exercises control through voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

The Company acquired Magnolia Petroleum Inc. on 23 October 2009 through a share exchange. As the shareholders of Magnolia Petroleum Inc. have control of the legal parent, Magnolia Petroleum plc, the transaction was accounted for as a reverse acquisition in accordance with IFRS 3 "Business Combinations". The following accounting treatment has been applied in respect of the reverse acquisition:

- the assets and liabilities of the legal subsidiary Magnolia Petroleum Inc. are recognised and measured in the Consolidated Financial Statements at their pre-combination carrying amounts, without restatement to fair value; and

- the equity structure appearing in the Consolidated Financial Statements reflects the equity structure of the legal parent, Magnolia Petroleum plc, including the equity instruments issued to effect the business combination.

The cost of acquisition was measured as the fair value of the assets acquired, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus certain costs directly attributable to the acquisition.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

### 2.2 Basis of consolidation (continued)

In accounting for the acquisition of Magnolia Petroleum Inc., the Company has taken advantage of Section 612 of the Companies Act 2006 and accounted for the transaction using merger relief.

Investments in subsidiaries are accounted for at cost less impairment. Where necessary, adjustments are made to the financial statements of subsidiaries to bring the accounting policies used into line with those used by other members of the Group. All significant inter-company transactions and balances between Group entities are eliminated on consolidation.

### 2.3 Goodwill

Goodwill arising on consolidation represents the excess of the cost of acquisition over the Group's interest in the fair value of the identifiable assets and liabilities of a subsidiary, associate or jointly controlled entity at the date of acquisition. Goodwill is initially recognised as an asset at cost and is subsequently measured at cost less any impairment. Goodwill which is recognised as an asset is reviewed for impairment at least annually. Any impairment is recognised immediately and is not subsequently reversed.

Under the reverse acquisition, goodwill represents the excess of the cost of the combination over the acquirer's interest in the net fair values of the legal parent. The fair value of the equity instruments of the legal subsidiary issued to effect the combination was not available and therefore the fair value of all the issued equity instruments of the legal parent prior to the business combination was used as the basis for determining the cost of the combination.

### 2.4 Going concern

The Group's business activities, together with the factors likely to affect its future development and performance are set out in the Chief Executive Officer's Statement. In addition, notes 3 and 22 to the Financial Statements disclose the Group's and Company's objectives, policies and processes for managing financial risks and capital.

The Company raised $1,266,220 after expenses via a placing in the year and, as detailed in note 21, a further £1.3 million before expenses was raised on 2 March 2012. The Group's cash flow forecasts and projections prepared up to June 2013 show that the Group has sufficient funds to fund its ongoing operating costs. The Directors have a reasonable expectation that the Company and Group has adequate resources to continue in operational existence for the foreseeable future. For this reason, the Directors continue to adopt the going concern basis of accounting in preparing the Financial Statements.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

### 2.5 Changes in accounting policy and disclosure

*(a) New and amended standards adopted by the Group*

There are no IFRSs or IFRIC interpretations that are effective for the first time for the financial year beginning 1 January 2011 that would be expected to have a material impact on the Group.

*(b) New and amended standards, and interpretations mandatory for the first time for the financial year beginning 1 January 2011 but not currently relevant to the Group*

The following standards and amendments to existing standards have been published and are mandatory for the Group's accounting periods beginning on or after 1 January 2011, but are not currently relevant to the Group.

A revised version of IAS 24 ''Related Party Disclosures" simplified the disclosure requirements for government-related entities and clarified the definition of a related party. This revision was effective for periods beginning on or after 1 January 2011.

An amendment to IFRS 1 ''First-time Adoption of International Financial Reporting Standards" relieved first-time adopters of IFRSs from providing the additional disclosures introduced in March 2009 by ''Improving Disclosures about Financial Instruments" (Amendments to IFRS 7). This amendment was effective for periods beginning on or after 1 July 2010.

Amendments to IAS 32 ''Financial Instruments: Presentation" addressed the accounting for rights issues that are denominated in a currency other than the functional currency of the issuer. These amendments were effective for periods beginning on or after 1 February 2010.

IFRIC 19 ''Extinguishing Financial Liabilities with Equity Instruments" clarified the treatment required when an entity renegotiates the terms of a financial liability with its creditor, and the creditor agrees to accept the entity's shares or other equity instruments to settle the financial liability fully or partially. This interpretation was effective for periods beginning on or after 1 July 2010.

An amendment to IFRIC 14 ''IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction", on prepayments of a minimum funding requirement, applies in the limited circumstances when an entity is subject to minimum funding requirements and makes an early payment of contributions to cover those requirements. The amendment permitted such an entity to treat the benefit of such an early payment as an asset. This amendment was effective for periods beginning on or after 1 January 2011.

*(c) New standards, amendments and interpretations issued but not effective for the financial year beginning 1 January 2011 and not early adopted*

The Group and Company's assessment of the impact of these new standards and interpretations is set out below.

IFRS 10 ''Consolidated Financial Statements" builds on existing principles by identifying the concept of control as the determining factor in whether an entity should be included within the consolidated financial statements of the parent company. The standard provides additional guidance to assist in the determination of control where this is difficult to assess. This standard is effective for periods beginning on or after 1 January 2013, subject to EU endorsement. The Directors are assessing the possible impact of this standard on the Group's and Parent Company's Financial Statements.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

### 2.5 Changes in accounting policy and disclosure (continued)

*(c) New standards, amendments and interpretations issued but not effective for the financial year beginning 1 January 2011 and not early adopted (continued)*

IFRS 11 ''Joint Arrangements" provides for a more realistic reflection of joint arrangements by focusing on the rights and obligations of the arrangement, rather than its legal form (as is currently the case). The standard addresses inconsistencies in the reporting of joint arrangements by requiring a single method to account for interests in jointly controlled entities. This standard is effective for periods beginning on or after 1 January 2013, subject to EU endorsement. The Directors are assessing the possible impact of this standard on the Group's and Parent Company's Financial Statements.

IFRS 12 ''Disclosure of Interests in Other Entities" is a new and comprehensive standard on disclosure requirements for all forms of interests in other entities, including joint arrangements, associates, special purpose vehicles and other off balance sheet vehicles. This standard is effective for periods beginning on or after 1 January 2013, subject to EU endorsement. The Directors are assessing the possible impact of this standard on the Group's and Parent Company's Financial Statements.

IFRS 13 ''Fair Value Measurement" improves consistency and reduces complexity by providing, for the first time, a precise definition of fair value and a single source of fair value measurement and disclosure requirements for use across IFRSs. It does not extend the use of fair value accounting, but provides guidance on how it should be applied where its use is already required or permitted by other standards. This standard is effective for periods beginning on or after 1 January 2013, subject to EU endorsement. The Directors are assessing the possible impact of this standard on the Group's and Parent Company's Financial Statements.

IAS 27 ''Separate Financial Statements" replaces the current version of IAS 27 ''Consolidated and Separate Financial Statements" as a result of the issue of IFRS 10 (see above). This revised standard is effective for periods beginning on or after 1 January 2013, subject to EU endorsement. The Directors are assessing the possible impact of this standard on the Group's and Parent Company's Financial Statements.

IAS 28 ''Investments in Associates and Joint Ventures" replaces the current version of IAS 28 ''Investments in Associates" as a result of the issue of IFRS 11 (see above). This revised standard is effective for periods beginning on or after 1 January 2013, subject to EU endorsement. The Directors are assessing the possible impact of this standard on the Group's and Parent Company's Financial Statements.

Amendments to IAS 1 ''Presentation of Financial Statements" require items that may be reclassified to the profit or loss section of the income statement to be grouped together within other comprehensive income (OCI). The amendments also reaffirm existing requirements that items in OCI and profit or loss should be presented as either a single statement or two consecutive statements. These amendments are effective for periods beginning on or after 1 July 2012, subject to EU endorsement. The Directors are assessing the possible impact of these amendments on the Group's and Parent Company's Financial Statements.

Amendments to IAS 19 ''Employment Benefits" eliminate the option to defer the recognition of gains and losses, known as the ''corridor method"; streamline the presentation of changes in assets and liabilities arising from defined benefit plans, including requiring remeasurements to be presented in other comprehensive income; and enhance the disclosure requirements for defined benefit plans, providing better information about the characteristics of defined benefit plans and the risks that entities are exposed to through participation in those plans. These amendments are effective for periods beginning on or after 1 January 2013, subject to EU endorsement, and are not expected to have an impact on the Group's or Parent Company's Financial Statements.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

### 2.5 Changes in accounting policy and disclosure (continued)

*(c) New standards, amendments and interpretations issued but not effective for the financial year beginning 1 January 2011 and not early adopted (continued)*

IFRIC 20 ''Stripping Costs in the Production Phase of a Surface Mine" clarifies when stripping costs incurred in the production phase of a mine's life should lead to the recognition of an asset and how that asset should be measured, both initially and in subsequent periods. This interpretation is effective for periods beginning on or after 1 January 2013, subject to EU endorsement. The Directors do not expect any impact on the Group's or Parent Company's Financial Statements.

Amendments to IFRS 7 "Financial Instruments: Disclosures" require disclosure of information that will enable users of financial statements to evaluate the effect or potential effect of netting arrangements, including rights of set-off associated with the entity's recognised financial assets and recognised financial liabilities, on the entity's financial position. These amendments are effective for periods beginning on or after 1 January 2013, subject to EU endorsement. The Directors are assessing the possible impact of these amendments on the Group's and Parent Company's Financial Statements.

Amendments to IFRS 9 "Financial Instruments" and IFRS 7 "Financial Instruments: Disclosures" require entities to apply IFRS 9 for annual periods beginning on or after 1 January 2015 instead of on or after 1 January 2013. Early application continues to be permitted. The amendments also require additional disclosures on transition from IAS 39 "Financial Instruments: Recognition and Measurement" to IFRS 9. The Directors are assessing the possible impact of these amendments on the Group's and Parent Company's Financial Statements.

Amendments to IAS 32 "Financial Instruments: Presentation" add application guidance to address inconsistencies identified in applying some of the criteria when offsetting financial assets and financial liabilities. This includes clarifying the meaning of "currently has a legally enforceable right of set-off" and that some gross settlement systems may be considered equivalent to net settlement. These amendments are effective for periods beginning on or after 1 January 2014, subject to EU endorsement, and are not expected to have an impact on the Group's and Parent Company's Financial Statements.

### 2.6 Revenue recognition

Revenue represents the amounts receivable from operators for the Group's share of oil and / or gas revenues less any royalties payable to the lessor or assignor of the mineral rights. Revenue is recognised in the period to which the declarations from the operators relate.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

### 2.7 Foreign currencies

*(a) Functional and presentation currency*

Items included in the Financial Statements of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the 'functional currency'). The functional currency of the UK parent entity is sterling and the functional currency of the subsidiary is US Dollars. The Financial Statements are presented in US Dollars, rounded to the nearest Dollar, which is the Group's functional and Company's presentation currency.

*(b) Transactions and balances*

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions or valuation where such items are re-measured. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in profit or loss.

*(c) Group companies*

The results and financial position of all the Group entities (none of which has the currency of a hyperinflationary economy) that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;

- income and expenses for each statement of comprehensive income are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions); and

- all resulting exchange differences are recognised in other comprehensive income.

On consolidation, exchange differences arising from the translation of the net investment in foreign entities, and of monetary items receivable from foreign subsidiaries for which settlement is neither planned nor likely to occur in the foreseeable future are taken to other comprehensive income. When a foreign operation is sold, such exchange differences are recognised in the income statement as part of the gain or loss on sale.

### 2.8 Commercial reserves

Proven and probable oil and gas reserves are estimated quantities of commercially producible hydrocarbons which the existing geological, geophysical and engineering data show to be recoverable in future years from known reservoirs. The proven and probable reserves included therein conform to the definition approved by the Society of Petroleum Engineers (SPE) and the World Petroleum Council (WPC).

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

### 2.9 Exploration costs

The Group applies the successful efforts method of accounting for oil and gas assets, having regard to the requirements of IFRS 6 'Exploration for and Evaluation of Mineral Resources'. Costs incurred prior to obtaining the legal rights to explore an area are expensed immediately to profit or loss.

Expenditure incurred on the acquisition of a licence interest is initially capitalised within intangible assets on a licence by licence basis. Costs are held, unamortised, within exploration costs until such time as the exploration phase of the licence area is complete or commercial reserves have been discovered. The cost of the licence is subsequently transferred into "Producing Properties" within property, plant and equipment and depreciated over its estimated useful economic life.

Exploration expenditure incurred in the process of determining exploration targets is capitalised initially within intangible assets as exploration costs. Exploration costs are initially capitalised on a well by well basis until the success or otherwise has been established. The success or failure of each exploration effort is judged on a well by well basis. Drilling costs are written off on completion of a well unless the results indicate that hydrocarbon reserves exist and there is a reasonable prospect that these reserves are commercially viable. All such costs are subject to regular technical, commercial and management review on at least an annual basis to confirm the continued intent to develop or otherwise extract value from the discovery. Where this is no longer the case, the costs are immediately expensed to profit or loss.

Following evaluation of successful exploration wells, if commercial reserves are established and the technical feasibility of extraction demonstrated, and once a project is sanctioned for commercial development, then the related capitalised exploration costs are transferred into a single field cost centre within development / producing assets within property, plant and equipment after testing for impairment. Where results of exploration drilling indicate the presence of hydrocarbons which are ultimately not considered commercially viable, all related costs are written off to profit or loss.

The net book values of development / producing assets are depreciated on a unit of production basis at a rate calculated by reference to proven and probable reserves and incorporating the estimated future cost of developing and extracting those reserves.

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

Net proceeds from any disposal of an exploration asset are initially credited against the previously capitalised costs. Any surplus proceeds are credited to profit or loss.

### 2.10 Decommissioning

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

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

### 2.11 Property, plant and equipment

All property, plant and equipment other than oil and gas assets are stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company and the cost of the item can be measured reliably. All other repairs and maintenance are charged to profit or loss during the financial period in which they are incurred.

Depreciation is charged so as to write off the cost of assets, over their estimated useful lives, on a straight line basis as follows:

Drilling Costs and Equipment – 10 years

Oil and gas producing assets held in property, plant and equipment are mainly depreciated on a unit of production basis at a rate calculated by reference to proven and probable reserves and incorporating the estimated future cost of developing and extracting those reserves.

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each financial year-end.

Gains and losses on disposal are determined by comparing proceeds with carrying amount. These are included in profit or loss.

### 2.12 Trade receivables

Trade receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables.

### 2.13 Cash and cash equivalents

Cash and cash equivalents comprise cash at bank and in hand and demand deposits with banks.

### 2.14 Share capital

Shares are classified as equity when there is no obligation to transfer cash or other assets. Incremental costs directly attributable to the issue of equity instruments are shown in equity as a deduction from the proceeds, net of tax. Incremental costs directly attributable to the issue of equity instruments as consideration for the acquisition of a business are included in the cost of acquisition.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

### 2.15 Taxation

The charge for current tax is based on the results of the Group for the year as adjusted for items which are non-assessable or disallowed. It is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

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

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries and associates, and interests in joint ventures, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax is calculated at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled. Deferred tax is charged or credited in the Statement of Comprehensive Income, except when it relates to items credited or charged directly to equity, in which case the deferred tax is also dealt with in equity. Deferred tax assets and liabilities are offset when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

### 2.16 Leasing

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to profit or loss on a straight-line basis over the period of the lease.

### 2.17 Financial assets and liabilities

Financial assets comprise trade and other receivables and cash and cash equivalents in the balance sheet. They are classified as loans and receivables. Financial liabilities comprise trade and other payables in the balance sheet, and are held at amortised cost.

*Derecognition*
The Group derecognises a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of the ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by the Group is recognised as a separate asset or liability.

Derecognition also takes place for certain assets when the Group writes-off balances pertaining to the assets deemed to be uncollectible.

The Group derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

### 2.17 Financial assets and liabilities (continued)

*Identification and measurement of impairment*
At each balance sheet date, the Group assesses whether there is objective evidence that financial assets are impaired. Financial assets are impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset, and the loss event has an impact on the future cash flows of the asset that can be estimated reliably.

The Group considers the evidence of impairment at both a specific asset and collective level. All individually significant financial assets are assessed for specific impairment. All significant assets found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Assets that are not individually significant are then collectively assessed for impairment by grouping together financial assets (carried at amortized cost) with similar risk characteristics.

When a subsequent event causes the amount of impairment loss to decrease, the impairment loss is reversed through profit or loss.

### 2.18 Share based incentive

The fair value of the services received in exchange for the grant of warrants is recognised as an expense and as a component of equity, if material. The total amount to be expensed over the vesting period is determined by reference to the fair value of the warrants granted using the Black-Scholes option pricing model.

### 2.19 Segment Information

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-makers, who are responsible for allocating resources and assessing performance of the operating segments and making strategic decisions.

## 3 FINANCIAL RISK MANAGEMENT

The Group's activities expose it to a variety of financial risks to include market risk (including currency risk), credit risk and liquidity risk.

*Market risk*
The Group operates in an international market for hydrocarbons and is exposed to risk arising from variations in the demand for and price of the hydrocarbons. Oil and gas prices historically have fluctuated widely and are affected by numerous factors over which the Group has no control, including world production levels, international economic trends, exchange rate fluctuations, speculative activity and global or regional political events.

*Credit risk*
Credit risk represents the risk of loss the Group would incur if operators and counterparties fail to fulfil their credit obligations. The maximum exposure to credit risk is represented by the carrying amount of each financial asset.

The Group's trade receivables and accrued income result from contractual amounts due from third party operators. The risk is concentrated between a relatively small group of operators given the small number of parties involved in oil and gas exploration and production activities. The Group seeks to mitigate this risk where possible by assessing the credit quality of the operators and by establishing ongoing and long term relationships.

*Liquidity risk*
Prudent liquidity risk management implies maintaining sufficient cash and marketable securities to finance the Group's operations. The Group monitors its cash flow position and overall liquidity risk. The Group maintains a level of cash deemed sufficient to finance operations to mitigate the effects of fluctuations in cash flows. The Group negotiates its payment terms in its sales agreements so as to minimize any periods of negative cash flows in any agreement.

*Foreign exchange risk*
The majority of the Group's sales and purchase transactions are denominated in US dollars. The Company's expenditure is predominantly denominated in sterling The currencies are stable and any exchange risk is managed by maintaining bank accounts denominated in those currencies.

## 4 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

*Use of estimates and judgements*
The preparation of Financial Statements in conformity with IFRSs requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods. In particular, information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amount recognised in the financial statements are described below:

*Recoverability of mineral leases*
Mineral leases and drilling costs on non producing properties have a carrying value at 31 December 2011 of $755,418 (2010: $749,070). Management tests annually whether non producing mineral leases have future economic value in accordance with the accounting policy stated in note 2.9. This assessment takes into consideration the likely commerciality of the asset, the future revenues and costs pertaining and the discount rates to be applied for the purposes of deriving a recoverable value. In the event that a lease does not represent an economic drilling target and results indicate that there is no additional upside, the mineral lease and drilling costs will be impaired. The Directors have reviewed the estimated value of the licences and have concluded that no additional impairment charge is necessary above that recognised in the year.

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

*Estimated impairment of goodwill*
Goodwill has a carrying value at 31 December 2011 of $356,216 (2010: $360,918). The Group tests annually whether goodwill has suffered any impairment in accordance with the accounting policy stated in Note 2.3. Management have concluded that there is no impairment charge necessary to the carrying value of goodwill.

*Estimated useful lives of property, plant and equipment*
Useful lives are based on industry standards and historical experience which are subjected to yearly evaluation. For leasehold improvements, the Group's considerations include the lease period of the agreement. Management review property, plant and equipment at each balance sheet date to determine whether there are any indications of impairment. If any such indication exists, an estimate of the recoverable amount is performed, and an impairment loss is recognised to the extent that the carrying amount exceeds the recoverable amount.

*Share based payments*
The Group has made awards of options and warrants over its unissued capital. The valuation of these options and warrants involves making a number of estimates relating to price volatility, future dividend yields, expected life and forfeiture rates.

## 5 SEGMENTAL INFORMATION

The Group operates in two geographical areas, the United Kingdom and the United States of America. Activities in the UK are mainly administrative in nature whilst the activities in the USA relate to exploration and production from oil and gas wells. The reports reviewed by the Board of Directors that are used to make strategic decisions are based on these geographical segments.

**Year ended 31 December 2011**

| | USA<br>$ | UK<br>$ | Intra-segment balances<br>$ | Total<br>$ |
|---|---|---|---|---|
| Revenue from external customers | 241,038 | - | - | 241,038 |
| Gross profit | 95,673 | - | - | 95,673 |
| Operating loss | (261,873) | (80,574) | - | (342,447) |
| Impairment - expired leases | 224,892 | - | - | 224,892 |
| Depreciation | 101,284 | - | - | 101,284 |
| Capital expenditure | 578,593 | - | - | 578,593 |
| Total assets | 2,314,906 | 4,867,652 | (4,620,820) | 2,561,738 |
| Total liabilities | 1,275,042 | 340,280 | (1,004,912) | 610,410 |

**Year ended 31 December 2010**

| | USA<br>$ | UK<br>$ | Intra-segment balances<br>$ | Total<br>$ |
|---|---|---|---|---|
| Revenue from external customers | 238,097 | - | - | 238,097 |
| Gross profit | 147,873 | - | - | 147,873 |
| Operating loss | (50,406) | (8,708) | - | (59,114) |
| Depreciation | 83,916 | - | - | 83,916 |
| Capital expenditure | 37,375 | - | - | 37,375 |
| Total assets | 1,399,773 | 3,836,566 | (3,707,638) | 1,528,701 |
| Total liabilities | 98,036 | 493,248 | (44,741) | 546,543 |

A reconciliation of the operating loss to loss before taxation is provided as follows:

| | Year ended 31December 2011<br>$ | Year ended 31December 2010<br>$ |
|---|---|---|
| Operating loss for reportable segments | (342,447) | (59,114) |
| Finance income | - | - |
| Finance costs | - | - |
| Loss before tax | (342,447) | (59,114) |

The amounts provided to the Board of Directors with respect to total assets are measured in a manner consistent with that of the Financial Statements. These assets are allocated based on the operations of the segment and physical location of the asset. Goodwill recognised by the Group is managed centrally and is not considered to be a segmental asset.

## 5 SEGMENTAL INFORMATION (CONTINUED)

Reportable segments' assets are reconciled to total assets as follows:

| | Year ended 31December 2011 $ | Year ended 31December 2010 $ |
|---|---|---|
| Segmental assets for reportable segments | 2,561,738 | 1,528,701 |
| Unallocated: goodwill | 356,216 | 360,918 |
| Total assets per balance sheet | 2,917,954 | 1,889,619 |

**Information about major customers**

Revenues of $94,649 and $30,768 are derived from two external operators. These revenues were all generated in the USA.

## 6 OPERATING LOSS

| | 2011 $ | 2010 $ |
|---|---|---|
| Loss from operating activities is stated after charging/(crediting): | | |
| Auditors' remuneration | | |
| - audit of parent company and consolidated financial statements | 16,044 | 20,077 |
| - other services in relation to accountancy and tax | 8,423 | 16,988 |
| Depreciation | 101,284 | 83,916 |
| Impairment of mineral leases | 224,892 | - |
| Differences due to foreign exchange | (10,988) | - |

Fees payable to the auditors of $72,196 for work undertaken on the placing at the date of admission to AIM have been charged to share premium.

## 7 STAFF COSTS

The Group and Company incurred no staff costs during 2011 and 2010.

**Directors' Emoluments**

The Directors' emoluments in respect of qualifying services were:

| | Group | | Company | |
|---|---|---|---|---|
| | 2011 $ | 2010 $ | 2011 $ | 2010 $ |
| Directors' salary and fees | 8,186 | - | (5,314) | - |

Directors' fees for 2010 and for the period up to AIM admission have been waived. The accrual originally recognised in 2009 has been released in 2011.

## 7 STAFF COSTS (CONTINUED)

| | 2011 $ | 2010 $ |
|---|---|---|
| J M Cubitt | 1,604 | - |
| S O Snead | 1,604 | - |
| R S Harwood | 1,604 | - |
| G J Burnell | 1,604 | - |
| R F Whittington | 13,500 | - |
| Total | 19,916 | - |

The average monthly number of staff, including the Directors, during the financial year was as follows:

| | Group 2011 No. | Group 2010 No. |
|---|---|---|
| Administrative and managerial | 5 | 5 |

## 8 TAXATION

**Tax charge for the period**

The tax charge for the period is $Nil (2010: $Nil).

**Factors affecting the tax charge for the period**

The tax charge for each period is explained below:

| | 2011 $ | 2010 $ |
|---|---|---|
| Loss for the period before taxation | (342,447) | (59,114) |
| Loss for the period before tax multiplied by the standard rate of UK corporation tax of 26.5% (2010: 28%) | (90,748) | (16,552) |
| Tax losses carried forward - US | 132,198 | 5,246 |
| Tax losses carried forward - UK | 21,352 | 2,438 |
| IFRS adjustments | 13,778 | 8,868 |
| US tax permanent and timing differences | (76,580) | - |
| | - | - |

The Group has UK tax losses of approximately $225,000 (2010: losses of approximately $148,000) and US tax losses of approximately $817,000 (2010: losses of approximately $266,000) available to carry forward against future taxable profits. A potential deferred tax asset of approximately $56,250 on the UK losses and $135,000 on the US losses has not been recognised because of uncertainty over the timing of future taxable profits against which the losses may be offset.

## 9 PROPERTY, PLANT AND EQUIPMENT

**Group**

| | Producing properties $ | Drilling costs and equipment $ | Total $ |
|---|---|---|---|
| **Cost** | | | |
| At 1 January 2010 | 133,055 | 86,923 | 219,978 |
| Additions | - | 12,928 | 12,928 |
| Transferred from intangible assets | 190,835 | 298,755 | 489,590 |
| At 31 December 2010 | 323,890 | 398,606 | 722,496 |
| Additions | - | 213,593 | 213,593 |
| Transferred from intangible assets | 133,758 | - | 133,758 |
| At 31 December 2011 | 457,648 | 612,199 | 1,069,847 |
| **Depreciation** | | | |
| At 1 January 2010 | 17,741 | 4,931 | 22,672 |
| Charge for the period | 30,046 | 53,870 | 83,916 |
| At 31 December 2010 | 47,787 | 58,801 | 106,588 |
| Charge for the period | 50,171 | 51,113 | 101,284 |
| At 31 December 2011 | 97,958 | 109,914 | 207,872 |
| **Net Book Amount at 1 January 2010** | 115,314 | 81,992 | 197,306 |
| **Net Book Amount at 31 December 2010** | 276,103 | 339,805 | 615,908 |
| **Net Book Amount at 31 December 2011** | 359,690 | 502,285 | 861,975 |

Transfers from intangible assets represent licence areas where production has commenced together with drilling costs associated with these licences.

Depreciation expense of $50,171 (2010: $30,046) has been charged in cost of sales and $51,113 (2010: $53,870) in administrative expenses.

## 10 INTANGIBLE ASSETS

### Group

| **Cost** | **Goodwill $** | **Drilling costs $** | **Mineral leases $** | **Total $** |
|---|---|---|---|---|
| At 1 January 2010 | 367,051 | 287,196 | 927,017 | 1,581,264 |
| Additions | - | 11,559 | 12,888 | 24,447 |
| Transferred to property, plant and equipment | - | (298,755) | (190,835) | (489,590) |
| Exchange movements | (6,133) | - | - | (6,133) |
| At 31 December 2010 | 360,918 | - | 749,070 | 1,109,988 |
| Additions | - | 364,998 | - | 364,998 |
| Transferred to property, plant and equipment | - | - | (133,758) | (133,758) |
| Exchange movements | (4,702) | - | - | (4,702) |
| Impairment | - | - | (224,892) | (224,892) |
| As at 31 December 2011 | 356,216 | 364,998 | 390,420 | 1,111,634 |
| **Amortisation** | | | | |
| At 1 January 2010 | - | - | - | - |
| Charge for the period | - | - | - | - |
| At 31 December 2010 | - | - | - | - |
| Charge for the period | - | - | - | - |
| At 31 December 2011 | - | - | - | - |
| **Net Book Amount at 1 January 2010** | 367,051 | 287,196 | 927,017 | 1,581,264 |
| **Net Book Amount at 31 December 2010** | 360,918 | - | 749,070 | 1,109,988 |
| **Net Book Amount at 31 December 2011** | 356,216 | 364,998 | 390,420 | 1,111,634 |

### Impairment review

Drilling costs and mineral leases represent acquired intangible assets with an indefinite useful life and are tested annually for impairment. As disclosed within Accounting Policies, expenditure incurred on the acquisition of mineral leases is capitalised within intangible assets until such time as the exploration phase is complete or commercial reserves have been discovered. Exploration expenditure including drilling costs are capitalised on a well by well basis if the results indicate the existence of a commercially viable level of reserves.

The directors have undertaken a review to assess whether circumstances exist which could indicate the existence of impairment as follows:

- The Group no longer has title to the mineral lease.
- A decision has been taken by the Board to discontinue exploration due to the absence of a commercial level of reserves.
- Sufficient data exists to indicate that the costs incurred will not be fully recovered from future development and participation.

Following their assessment the directors recognised an impairment charge to the cost of mineral leases of $224,892 (2010 - $Nil) in respect of expired mineral leases.

The directors believe that no impairment is necessary on the carrying value of goodwill. Goodwill arose on the reverse acquisition of Magnolia Petroleum Plc. The goodwill represents the value of the parent company being an AIM quoted entity to Magnolia Petroleum Inc.

## 11 INVESTMENTS

### Investments in subsidiaries

| | 2011 $ | 2010 $ |
|---|---|---|
| **Company** | | |
| Shares in group undertakings | | |
| At 1 January | 3,662,897 | 3,725,899 |
| Exchange movements | (46,990) | (63,002) |
| **At 31 December** | 3,615,907 | 3,662,897 |

Investments in group undertakings are recorded at cost, which is the fair value of the consideration paid.

### Principal subsidiaries

| Name | Country of incorporation and residence | Nature of business | Registered capital | Proportion of equity shares held by Company |
|---|---|---|---|---|
| Magnolia Petroleum Inc. | United States of America | Oil and gas exploration | Ordinary shares US$1 | 100% |

This subsidiary undertaking is included in the consolidation. The proportion of the voting rights in the subsidiary undertaking held directly by the Parent Company does not differ from the proportion of ordinary shares held.

## 12 TRADE AND OTHER RECEIVABLES

| | Group | | Company | |
|---|---|---|---|---|
| | 2011 | 2010 | 2011 | 2010 |
| | $ | $ | $ | $ |
| Trade receivables | 16,820 | 31,498 | - | - |
| Other receivables | 47,670 | 29,438 | 47,227 | 29,438 |
| Amounts due from Group undertakings | - | - | 1,004,912 | 44,741 |
| Prepayments | 5,818 | 5,264 | 5,818 | 5,264 |
| | 70,308 | 66,200 | 1,057,957 | 79,443 |

Trade receivables comprise customer receivables in credit. The Group retains all risks associated with these receivables until fully recovered.

## 12 TRADE AND OTHER RECEIVABLES (continued)

As at 31 December 2011, trade receivables of $16,820 (2010: $31,498) were fully performing.

**Group**

The carrying amounts of the Group's trade and other receivables are denominated in the following currencies:

| | 2011 | 2010 |
|---|---|---|
| | $ | $ |
| UK Pounds | 53,044 | 34,702 |
| US Dollar | 17,264 | 31,498 |
| | 70,308 | 66,200 |

The maximum exposure to credit risk at the reporting date is the carrying value of each class of receivable mentioned above. The Group does not hold any collateral as security.

**Company**

The carrying amounts of the Company's trade and other receivables are denominated in UK pound sterling.

## 13 CASH AND CASH EQUIVALENTS

| | Group | | Company | |
|---|---|---|---|---|
| | 2011 | 2010 | 2011 | 2010 |
| | $ | $ | $ | $ |
| Cash at bank | 874,037 | 97,523 | 193,788 | 94,226 |
| Cash and cash equivalents | 874,037 | 97,523 | 193,788 | 94,226 |

At 31 December 2011, the Group held cash of $193,788 in a bank with a Fitch credit rating of A(Stable) and $680,249 in a bank with a credit rating of AA-minus.

## 14 SHARE CAPITAL AND PREMIUM

**Allotted, called-up and fully paid**

| | Ordinary shares | | | Share Premium | |
|---|---|---|---|---|---|
| | **Number** | **Nominal value £** | **Nominal value $** | **Nominal value £** | **Nominal value $** |
| At 1 January 2010 and at 31 December 2010 – shares of 0.1p each | 341,038,441 | 341,039 | 587,336 | 731,391 | 1,347,983 |
| Issued in the year | 218,181,820 | 218,181 | 338,792 | 560,682 | 870,894 |
| At 31 December 2011 – shares of 0.1p each | 559,220,261 | 559,220 | 926,128 | 1,292,073 | 2,218,877 |

On 25 November 2011, the Company issued 218,181,280 new ordinary shares of 0.1p each fully paid at 0.55p per share.

**Group**

| | **Number of shares** | **Ordinary shares $** | **Share premium $** |
|---|---|---|---|
| At 1 January 2010 and At 31 December 2010 | 341,038,441 | 587,336 | 1,347,983 |
| Placing shares | 218,181,820 | 338,792 | 1,524,567 |
| Issue costs | - | - | (653,673) |
| **At 31 December 2011** | 559,220,261 | 926,128 | 2,218,877 |

Under reverse acquisition accounting, the equity structure appearing in the consolidated Financial Statements reflects the equity structure of the legal parent, including the equity instruments issued by the legal parent to effect the combination.

## 14 SHARE CAPITAL AND PREMIUM (continued)

**Share options and warrants**

Share options and warrants outstanding and exercisable at the end of the year have the following expiry dates and exercise prices:

| Expiry date | Exercise price in pence per share | No. Options/warrants 2011 | No. Options/warrants 2010 |
|---|---|---|---|
| 23 April 2011 | 2.00 | - | 10,980,759 |
| 25 November 2016 | 0.55 | 9,545,454 | - |
| 25 November 2018 | 1.30 | 52,820,768 | 52,820,768 |
| | | 62,366,222 | 63,801,527 |

The options and warrants are exercisable starting immediately from the date of grant. The Company and Group have no legal or constructive obligation to settle or repurchase the warrants or options in cash.

| | Year ended 31 December 2011 | | Year ended 31 December 2010 | |
|---|---|---|---|---|
| | **No. of options and warrants** | **Weighted average exercise price (in pence)** | **No. of options and warrants** | **Weighted average exercise price (in pence)** |
| Outstanding at beginning of period | 63,801,527 | 1.42 | 63,801,527 | 1.42 |
| Granted during the period | 9,545,454 | 0.55 | - | - |
| Expired during the period | (10,980,759) | 2.00 | - | - |
| Outstanding at end of period | 62,366,222 | 1.19 | 63,801,527 | 1.42 |
| Exercisable at end of period | 62,366,222 | 1.19 | 63,801,527 | 1.42 |

The warrants and options outstanding at 31 December 2011 had a weighted average remaining contractual life of 6.57 years.

No options or warrants were exercised during the period. On 25 November 2011, 9,545,454 warrants were granted as part of the placing and AIM admission. The warrants have an exercise price of 0.55 pence and an expiry date of 25 November 2016.

As part of the arrangements for the AIM admission, 52,820,768 options and warrants with an original expiry date of 23 October 2014 had their expiry date extended to 25 November 2018. The exercise price remained unchanged at 1.3 pence. The financial effect of the modification is not material.

## 15 TRADE AND OTHER PAYABLES

| | Group 2011 $ | Group 2010 $ | Company 2011 $ | Company 2010 $ |
|---|---|---|---|---|
| **Non-current** | | | | |
| Trade and other payables | 278,431 | - | 243,431 | - |
| | 278,431 | - | 243,431 | - |
| **Current** | | | | |
| Trade and other payables | 227,907 | 332,431 | 41,604 | 305,279 |
| Social security and other taxes | 122 | 124 | 122 | 124 |
| Accrued expenses | 103,950 | 213,988 | 55,123 | 187,846 |
| | 331,979 | 546,543 | 96,849 | 493,249 |

Under the terms of the Deferral Amendment Agreement dated 15 November 2011, non-current trade and other payables of $243,431 are repayable on 23 April 2013. Under the terms of the Enerlex Loan Agreement dated 15 November 2011, non-current other payables of $3,500, $6,500 and $25,000 are repayable on demand to Enerlex Inc. on a date on or after 11 April 2013, 14 September 2013 and 17 October 2013 respectively.

## 16 EXPENSES BY NATURE

| **Group** | 2011 $ | 2010 $ |
|---|---|---|
| Directors' fees | 8,186 | - |
| Management fees | - | 51,000 |
| Consulting fees | 24,350 | 151 |
| Legal, professional and compliance costs | 90,762 | 76,669 |
| Difference due to foreign exchange | (10,988) | - |
| Depreciation | 51,113 | 53,870 |
| Other costs | 49,805 | 25,297 |
| **Total administrative expenses** | 213,228 | 206,987 |

## 17 LOSS PER SHARE

The calculation of the basic loss per share of 0.09 cents per share (31 December 2010 loss per share: 0.02 cents) is based on the loss attributable to ordinary shareholders of $342,447 (31 December 2010 loss: $59,114) and on the weighted average number of ordinary shares of 363,155,502 (31 December 2010: 341,038,441) in issue during the period.

In accordance with IAS 33, no diluted earnings per share are presented as the effect on the exercise of share options would be to decrease the loss per share.

Details of share options and warrants that could potentially dilute earnings per share in future periods are set out in Note14.

## 18 TREASURY POLICY AND FINANCIAL INSTRUMENTS

The Company and Group operate informal treasury policies which include ongoing assessments of interest rate management and borrowing policy. The Board approves all decisions on treasury policy.

The Company has financed its activities by the raising of funds through the placing of shares. There are no material differences between the book value and fair value of the financial assets.

## 19 RELATED PARTY TRANSACTIONS

### Transactions with Group undertakings

During the year ended 31 December 2011 the Company charged management fees of $17,632 (2010: $44,741) to Magnolia Petroleum Inc, the Company's wholly owned subsidiary for the provision of administrative and management services. $17,632 (2010: $44,741) in relation to these fees was outstanding at the balance sheet date and is included within Trade and other receivables. As at 31 December 2011, the amount due to the Company from Magnolia Petroleum Inc was $1,004,912 (2010: $44,741).

All Group transactions were eliminated on consolidation.

### Transactions with Enerlex Inc

Steven Snead and his wife are interested in 100 per cent of the issued share capital of Enerlex Inc. ("Enerlex"). Under the Enerlex Services Agreement dated 23 October 2009, Enerlex agreed to provide executives, staff, premises and business services to Magnolia Petroleum Inc. to enable it to acquire, manage and develop its drilling and working interests business. In addition, Enerlex provided 50 per cent of the working time of Steven Snead as Chief Executive Officer, of Rita Whittington as Operations Manager and of Ronald Harwood as Chairman and Chief Financial Officer, as well as the use of other unnamed personnel required for the performance of the above services. The Enerlex Services Agreement ran for a fixed period of one year and was renewable in the twelfth month of each year for a further year by agreement.

A Services Termination Agreement dated 15 November 2011 between Enerlex, Magnolia Petroleum Inc and the Company terminated the Enerlex Services Agreement with effect from 31 October 2011. A rental agreement between Enerlex and Magnolia Petroleum Inc was signed on 15 November 2011 whereby Enerlex agreed to provide Magnolia Petroleum Inc on a month to month basis with office premises and services for $2,500 per month. A charge of $2,500 was recognised during the year under this agreement.

At 31 December 2011 accrued interest of $26,143 (2010: $26,143) was due to Enerlex in relation to a loan granted to the Company which was repaid in full in October 2010. No interest was charged by Enerlex during the year (2010: $Nil).

Enerlex gave an undertaking to Magnolia Petroleum Inc dated 15 November 2011 whereby Enerlex undertakes that if any of the leases granted to Magnolia Petroleum Inc on any of the mineral interests in the Woodford/Hunton play in Oklahoma expires at the end of the primary period because of non-drilling, Enerlex will at Magnolia Petroleum Inc's request grant a further three year lease on the same terms as the expired lease.

### Other Transactions

At 31 December 2011 the total accrued remuneration to Directors was $18,137 (2010: $11,212).

Under the Deferral Amendment Agreement dated 15 November 2011, all Directors agreed to waive their services fees up to the date of AIM admission.

## 20 ULTIMATE CONTROLLING PARTY

As at the Balance Sheet date, the Directors do not consider there is an ultimate controlling party.

## 21 POST BALANCE SHEET EVENTS

On 20 January 2012, 4,545,455 share warrants over ordinary shares of 0.1p each were exercised for a total consideration of £25,000.

On 27 January 2012, 4,999,999 share warrants over ordinary shares of 0.1p each were exercised for a total consideration of £27,500.

On 2 March 2012, the Group raised approximately £1.3 million before expenses via a placing of 100,115,270 new ordinary shares at a price of 1.3p per share.

## 22 CAPITAL MANAGEMENT POLICES

The Group and Company's capital management objectives are:

- to ensure the Group's and Company's ability to continue as a going concern; and
- to provide an adequate return to shareholders.

The Group and Company monitor capital on the basis of the carrying amount of equity less cash and cash equivalents as presented on the face of the balance sheet.

Although the Group and Company are not constrained by any externally imposed capital requirements, its goal is to maximise their capital-to-overall financing structure ratio.

The Group and Company set the amount of capital in proportion to its overall financing structure and manage their capital structure and make adjustments to it in the light of changes in economic conditions and the risk characteristics of the underlying assets.

## 23 CAPITAL COMMITMENTS

The Group has capital commitments for drilling and equipment costs contracted but not provided for of approximately $433,000 at the balance sheet date.

# MAGNOLIA PETROLEUM PLC
# NOTICE OF ANNUAL GENERAL MEETING

**Notice is given that the Annual General Meeting of Magnolia Petroleum plc ("the Company") will be held at 10.00am on Friday 29 June 2012 at 18452 E 111th, Broken Arrow, Oklahoma, OK74011, USA to consider and, if thought fit, pass the following resolutions, of which resolutions 1 to 5 will be proposed as ordinary resolutions and resolutions 6 and 7 as special resolutions:**

1. To receive the directors' report and audited financial statements of the Company for the year ended 31 December 2011.

2. To re-elect Gavin Burnell as a director of the Company.

3. To re-elect Steven Snead as a director of the Company

4. To re-appoint Littlejohn LLP as auditors of the Company and to authorise the directors to set their fees.

5. THAT, in substitution for any existing authority the directors be and they are hereby generally and unconditionally authorised under section 551 of the Companies Act 2006 to exercise all the powers of the Company to allot shares in the Company or grant rights to subscribe for or to convert any security into shares in the Company ("Rights") within the meaning of that section on and subject to such terms as the directors may determine up to an aggregate nominal amount of £334,440 such authority unless previously renewed, revoked or varied to expire at the end of next year's AGM on 30 June 2013 save that the Company may before such expiry make an offer or agreement which would or might require relevant securities to be allotted after such expiry and the directors may allot relevant securities under such an offer or agreement as if the authority conferred hereby had not expired.

6. THAT, subject to the passing of Resolution 5 above, the directors be and are hereby empowered under section 570 of the Companies Act 2006 ("the Act") to allot equity securities (within the meaning of section 560 of the Act) for cash under the general authority already given as if sub-section 561(1) of the Act did not apply to any such allotment, provided that this power shall be limited to:

   (a) the allotment of equity securities in connection with an offer of such securities to holders of ordinary shares where the equity securities for which ordinary shares are respectively entitled to subscribe are proportionate (as nearly as may be) to the respective numbers of ordinary shares held by them, but subject to such exclusions or other arrangements as the directors may deem necessary or expedient in relation to fractional entitlements or any legal or practical problems under the laws of any overseas territory or the requirements of any regulatory body or stock exchange; and

   (b) the allotment (otherwise than under sub-paragraph (a) above) of equity securities up to an aggregate nominal value of £334,440;

   and so that such power (unless previously revoked or varied) shall expire at the end of next year's annual general meeting, (or if earlier at the close of business on 30 June 2013) provided that the directors may, before the power expires, make an offer or enter into an agreement which would or might require equity securities to be allotted after such power expires.

7. THAT, the Company be generally and unconditionally authorised to make market purchases (as defined in the Companies Act 2006) of ordinary shares of 0.1p each in the capital of the Company ("ordinary shares") on such terms and in such manner as the directors may from time to time determine, provided that:

   (a) the maximum number of ordinary shares authorised to be purchased shall be 100,332,148;
   (b) the minimum price which may be paid for an ordinary share is 0.1p;

(c) the maximum price which may be paid for an ordinary share is an amount equal to 105 per cent of the average of the middle market quotations for an ordinary share (as derived from the Daily Official List) for the five business days immediately preceding the date on which the ordinary share is contracted to be purchased;

(d) the minimum and maximum prices per ordinary share referred to in sub-paragraphs (b) and (c) of this resolution are in each case exclusive of any expenses payable by the Company;

(e) the authority conferred by this resolution shall expire at the end of next year's annual general meeting (or if earlier at the close of business on 30 June 2013) unless such authority is varied, revoked or renewed prior to such time by the Company in general meeting; and

(f) the Company may make a contract to purchase ordinary shares under the authority hereby conferred prior to the expiry of such authority which will or may be completed wholly or partly after the expiration of such authority.

By Order of the Board
S Salter
Secretary

Registered Office:
The Fitzpatrick Building
188-194 York Way
London N7 9AS
United Kingdom

Dated: 30 May 2012

**Notes:**

**1. Right to attend, speak and vote**

If you want to attend, speak and vote at the AGM you must be on the Company's register of members at 6pm on 27 June 2012. This will allow us to confirm how many votes you have on a poll. Changes to the entries in the register of members after that time, or, if the AGM is adjourned, 48 hours before the time of any adjourned meeting, shall be disregarded in determining the rights of any person to attend, speak or vote at the AGM.

**2. Appointment of proxies**

If you are a member of the Company you may appoint one or more proxies to exercise all or any of your rights to attend, speak and vote at the meeting. You may only appoint a proxy using the procedures set out in these notes and in the notes on the proxy form, which you should have received with this notice of meeting.

A proxy does not need to be a member of the Company but must attend the meeting to represent you. Details of how to appoint the Chairman of the meeting or another person as your proxy using the proxy form are set out in the notes on the form. If you wish your proxy to speak on your behalf at the meeting you will need to appoint your own choice of proxy (not the Chairman) and give your instructions directly to them.

You may appoint more than one proxy in relation to the AGM provided that each proxy is appointed to exercise the rights attached to a different share or shares which you hold. If you wish to appoint more than one proxy you may photocopy the proxy form or alternatively you may contact the Company's registrars, Share Registrars Limited on 01252 821 390.

**3. Appointment of proxy using hard copy proxy form**

The notes to the proxy form explain how to direct your proxy how to vote on each resolution or withhold their vote. A vote withheld is not a vote in law, which means that the vote will not be counted in the calculation of votes for or against the resolution. If you do not indicate on the proxy form how your proxy should vote, they will vote or abstain from voting at their discretion. They will also vote (or abstain from voting) at they think fit in relation to any other matter which is put before the meeting.

To appoint a proxy using the proxy form, the form must be completed and signed and received by Share Registrars Limited no later than 48 hours before the meeting. Any proxy forms (including any amended proxy appointments) received after the deadline will be disregarded.

The completed form may be returned by any of the following methods:

- Sending or delivering it to Share Registrars Limited at Suite E, First Floor, 9 Lion and Lamb Yard, Farnham, Surrey GU9 7LL
- Sending it by fax to 01252 719 232
- Scanning it and sending it by email to proxies@shareregistrars.uk.com;

If the shareholder is a company, the proxy form must be executed under its common seal or signed on its behalf by an officer or attorney. Any power of attorney or any other authority under which the proxy form is signed (or a duly certified copy of such power or authority) must be included with the proxy form.

**4. Appointment of proxy by joint members**

In the case of joint holders, where more than one joint holder purports to appoint a proxy, only the appointment submitted by the most senior holder will be accepted. Seniority is determined by the order in which the names of the joint holders appear in the Company's register of members in respect of the joint holding (the first-named being the most senior).

**5. Changing your instructions**

To change your proxy instructions simply submit a new proxy appointment using the methods set out above. The amended instructions must be received by the registrars by the same cut-off time noted above. Where you have appointed a proxy using a hard copy proxy form and would like to change the instructions using another hard copy proxy form, please contact Share Registrars Limited on 01252 821 390. If you submit more than one valid proxy form, the one received last before the latest time for the receipt of proxies will take precedence.

**6. Termination of proxy appointments**

In order to revoke a proxy instruction you will need to inform the Company by sending a signed hard copy notice clearly stating your intention to revoke your proxy appointment to Share Registrars Limited at Suite E, First Floor, 9 Lion and Lamb Yard, Farnham, Surrey GU9 7LL. Alternatively you may send the notice by fax to 01252 719 232. In the case of a member which is a company, the revocation notice must be executed under its common seal or signed on its behalf by an officer or attorney. Any power of attorney or any other authority under which the revocation notice is signed (or a duly certified copy of such power or authority) must be included with the revocation notice.

In either case, your revocation notice must be received by Share Registrars Limited no later than 48 hours before the meeting. If your revocation is received after the deadline, your proxy appointment will remain valid. However, the appointment of a proxy does not prevent you from attending the meeting and voting in person. If you have appointed a proxy and attend the meeting in person, your proxy appointment will automatically be terminated.

**7. Communications with the Company**

Except as provided above, members who have general queries about the meeting should telephone Share Registrars on 01252 821 390 (no other methods of communication will be accepted). You may not use any electronic address provided either in this notice of general meeting; or any related documents (including the Chairman's letter and proxy form), to communicate with the Company for any purposes other than those expressly stated.

**8. Issued shares and total voting rights**

As at 5.00 pm on the day immediately prior to the date of posting of this notice of AGM, the Company’s issued share capital comprised 668,880,985 ordinary shares of 0.1p each. Each ordinary share carries the right to one vote at a general meeting of the Company and, therefore, the total number of voting rights in the Company at that time was 668,880,985.