Tethys Petroleum Limited

Annual Financial Information
December 31, 2012

The Tethys Petroleum Limited Annual Report and Accounts for 2012 consists of two documents as detailed below:

1) Management's Discussion & Analysis: this includes the documents required to be disclosed pursuant to National Instrument 51-102 of Canadian Securities Administrators "Continuous Disclosure Obligations" ("Canadian NI 51-102") in respect of an annual Management's Discussion & Analysis and the documents required to be disclosed pursuant to UK's Disclosure & Transparency Rules with respect to DTR 4.1 "Annual Financial Report" (DTR 4.1); and

2) Annual financial information: this includes the Consolidated Financial Statements, the documents required to be disclosed pursuant to Canadian NI 51-102 with respect to an annual financial report and the documents required to be disclosed pursuant to DTR 4.1, Directors' Responsibility Statement and the Independent Auditor's Report to Tethys Petroleum Limited.

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Responsibility Statement of the Directors in Respect of the Annual Report and Accounts

The accompanying consolidated financial statements and all the information in the Annual Report and Accounts are the responsibility of The Board of Directors. The consolidated financial statements have been prepared by management, acting on behalf of the Board of Directors, in accordance with the accounting policies described in the notes to the consolidated financial statements. In the opinion of management, the consolidated financial statements have been prepared within acceptable limits of materiality and are in accordance with International Financial Reporting Standards, appropriate in the circumstances, as issued by the International Accounting Standards Board. The consolidated financial information contained elsewhere in the Annual Report and Accounts has been reviewed to ensure consistency with that in the consolidated financial statements.

Management has developed and maintains systems of internal accounting controls, policies and procedures in order to provide reasonable assurance as to the reliability of the financial records and the safeguarding of assets.

External auditors, appointed by the shareholders of the Company, have examined the consolidated financial statements and have expressed an opinion on the consolidated statements. Their report is included with the consolidated financial statements.

The Board of Directors is responsible for ensuring that management fulfils its responsibilities for financial reporting and internal control. The Board of Directors of the Company has established an Audit Committee, consisting of independent non-management directors, to review the consolidated financial statements with management and the auditors. The Board of Directors has approved the consolidated financial statements on the recommendation of the Audit Committee.

We confirm that to the best of our knowledge:

- the financial statements, prepared in accordance with International Financial Reporting Standard ("IFRSs"), give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole; and

- the Management Discussion & Analysis includes a fair review of the development and performance of the business and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

For and on behalf of the Board

Dr. D. Robson	***B. Murphy***
Executive Chairman	Chief Financial Officer
March 28, 2013	March 28, 2013

Independent Auditor's Report to Tethys Petroleum Limited

We have audited the accompanying consolidated financial statements of Tethys Petroleum Limited ("the Company"), which comprise the consolidated statement of financial position as at 31 December 2012 and 31 December 2011 the consolidated statements of comprehensive income, changes in equity and cash flows for the years then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

This report is made solely to the Company in accordance with the terms of our engagement. Our audit work has been undertaken so that we might state to the Company those matters we have been engaged to state to it in this report and for no other purpose. We have conferred on the Company's shareholders, as a body, in the engagement terms agreed with the Company, the right to rely on this report and to assert claims in relation thereto, on the basis that such right is enforceable subject to and in accordance with those engagement terms and the Contracts (Rights of Third Parties) Act 1999. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and, on the basis stated above, the Company's shareholders as a body, for our audit work, for this report, or for the opinions we have formed.

Directors' Responsibility for the Consolidated Financial Statements

The directors are responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as the directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Company as at 31 December 2012 and 31 December 2011, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards.

Juliette Lowes

Juliette Lowes
for and on behalf of KPMG Audit Plc, Statutory auditor
Chartered Accountants
March 28, 2013
15 Canada Square, London, E14 5GL, United Kingdom

Tethys Petroleum Limited

Consolidated Statement of Financial Position
(in US dollars)

	Note	2012 $'000	2011 $'000
		As at December 31	
Non-current assets			
Intangible assets	12	107,374	99,959
Property, plant and equipment	13	121,097	128,918
Restricted cash	14	1,543	1,407
Prepayments and other receivables	15	6,444	10,217
Investment in jointly controlled entities	17	1,116	1,113
		237,574	241,614
Current assets			
Inventories	18	2,046	2,025
Trade and other receivables	15	7,703	5,478
Loan receivable from jointly controlled entity	16	2,403	2,013
Cash and cash equivalents	19	1,750	10,746
Restricted cash	14	477	885
Derivative financial instruments – interest rate swap	20	-	630
		14,379	21,777
Total assets		251,953	263,391
Equity attributable to shareholders			
Share capital	23	28,671	28,669
Share premium	23	306,725	306,725
Other reserves	23	41,705	38,530
Accumulated deficit		(165,385)	(144,962)
Non-controlling interest	24	8,437	8,918
Total equity		220,153	237,880
Non-current liabilities			
Financial liabilities - borrowings	20	3,688	1,632
Deferred taxation	10	2,912	2,111
Trade and other payables	21	351	547
Asset retirement obligations	22	524	386
		7,475	4,676
Current liabilities			
Financial liabilities - borrowings	20	13,625	8,396
Derivative financial instruments – warrants	20	523	264
Derivative financial instruments – foreign currency hedge	20	-	157
Current taxation	10	233	-
Deferred revenue		1,713	1,839
Trade and other payables	21	8,231	10,179
		24,325	20,835
Total liabilities		31,800	25,511
Total shareholders' equity and liabilities		251,953	263,391
Commitments and contingencies	28		

The notes on pages 8 to 68 form part of these consolidated financial statements. The consolidated financial statements were approved by the Board on March 28, 2013 and were signed on its behalf.

Dr. D. Robson — Executive Chairman

B. Murphy — Chief Financial Officer

Tethys Petroleum Limited

Consolidated Statement of Comprehensive Income
(in US dollars)

	Note	Year ended December 31, 2012 $'000	2011 $'000 (re-presented)
	2		
Sales and other operating revenues	6	38,107	22,922
Other operating income	7	-	7,375
Total revenue and other income		38,107	30,297
Production expenditures		(12,970)	(10,785)
Depreciation, depletion and amortization		(18,424)	(13,111)
Impairment charge	12,13	-	(8,983)
Unsuccessful exploration and evaluation expenditures		(1,093)	(1,807)
Listing expenses		-	(606)
Business development expenses		(1,591)	(3,149)
Administrative expenses	8	(19,673)	(19,763)
Share based payments	9	(2,932)	(3,814)
Foreign exchange (loss) / gain - net		(455)	74
Fair value gain / (loss) - net on derivative financial instrument		53	(625)
Gain on previously held interest in jointly controlled entity	25	-	27,381
Loss on settlement of pre-existing loan relationship	25	-	(24,423)
Profit / (loss) from jointly controlled entity	16	191	(722)
Finance (costs) / income - net	20	(1,083)	1,100
Loss before taxation		**(19,870)**	**(28,936)**
Taxation	10	(1,034)	1,947
Loss for the year		**(20,904)**	**(26,989)**
Loss attributable to:			
Shareholders		(20,423)	(26,939)
Non-controlling interest		(481)	(50)
Loss for the year		**(20,904)**	**(26,989)**
Loss per share attributable to shareholders			
Basic and diluted	11	(0.07)	(0.10)

No dividends were paid or are declared for the year (2011 – $Nil).

The notes on pages 8 to 68 form part of these consolidated financial statements.

Tethys Petroleum Limited

Consolidated Statement of Changes in Equity
(in US dollars)

	Note	Share capital $'000	Share premium $'000	Accumulated deficit $'000	Option reserves $'000	Warrant reserves $'000	Non-controlling interest $'000	Total equity $'000
		Attributable to shareholders						
Balance at January 1, 2011	23	26,063	297,222	(118,023)	17,706	16,555	-	239,523
Comprehensive loss for the year		-	-	(26,939)	-	-	(50)	(26,989)
Acquisition of subsidiary with non-controlling interests		-	-	-	-	-	8,968	8,968
Transactions with shareholders								
Issue of share capital	23	2,606	10,396	-	-	-	-	13,002
Cost of share issue		-	(893)	-	-	-	-	(893)
Share-based payments		-	-	-	4,269	-	-	4,269
Total transactions with shareholders		2,606	9,503	-	4,269	-	-	16,378
Balance at January 1, 2012		**28,669**	**306,725**	**(144,962)**	**21,975**	**16,555**	**8,918**	**237,880**
Comprehensive loss for the year		-	-	(20,423)	-	-	(481)	(20,904)
Transactions with shareholders								
Share-based payments		-		-	3,142	-	-	3,142
Issue of warrants		-	-	-	-	37	-	37
Exercise of options		2	11	-	(4)	-	-	9
Cost of share issue		-	(11)	-	-	-	-	(11)
Total transactions with shareholders		2	-	-	3,138	37	-	3,177
At December 31, 2012		**28,671**	**306,725**	**(165,385)**	**25,113**	**16,592**	**8,437**	**220,153**

The option reserve and warrant reserve are denoted together as "other reserves" on the consolidated statement of financial position. These reserves are non distributable.

The notes on pages 8 to 68 form part of these consolidated financial statements.

Tethys Petroleum Limited

Consolidated Statement of Cash Flows
(in US dollars)

	Note	Year ended December 31, 2012 $'000	2011 $'000
Cash flow from operating activities			
Loss before taxation		(19,870)	(28,936)
Adjustments for			
Share based payments	9	2,932	3,814
Net finance cost / (income)		1,083	(1,100)
Unsuccessful exploration and evaluation expenditures	12	955	1,807
Depreciation, depletion and amortization		18,424	13,111
Impairment charge	12,13	-	8,983
Loss on disposal of assets		-	96
Fair value (gain) / loss on derivative financial instrument		(53)	625
Gain on previously held interest in SSEC	25	-	(27,381)
Loss on settlement of pre-existing loan relationship	25	-	24,423
Net unrealised foreign exchange loss / (gain)		46	(72)
(Profit) / loss from jointly controlled entity		(191)	722
Deferred revenue		(126)	(611)
Other operating income		-	(7,375)
Net change in non-cash working capital	27	(1,842)	(664)
Net cash used in operating activities		1,358	(12,558)
Cash flow from investing activities			
Interest received		6	138
Expenditure on exploration and evaluation assets		(7,764)	(11,633)
Expenditures on property, plant and equipment		(9,737)	(30,269)
Movement in restricted cash		272	(1,277)
Acquisition of subsidiary, net of cash received		-	(6,785)
Payments made on behalf of jointly controlled entity		-	(18,292)
Movement in advances to construction contractors		778	2,490
Movement in value added tax receivable		2,995	(2,982)
Net change in non-cash working capital	27	(2,279)	682
Net cash used in investing activities		(15,729)	(67,928)
Cash flow from financing activities			
Investment in jointly controlled entity		(3)	(1,113)
Proceeds from issuance of borrowings – net of issue costs	20	15,670	2,393
Repayment of borrowings	20	(8,563)	(642)
Interest paid on borrowings		(1,433)	(356)
Non-current other payables	21	(283)	(284)
Proceeds from issuance of equity, net of issue costs	23	-	12,109
Net cash generated from financing activities		5,388	12,107
Effects of exchange rate changes on cash and cash equivalents		(13)	(10)
Net decrease in cash and cash equivalents		(8,996)	(68,389)
Cash and cash equivalents at beginning of the year		10,746	79,135
Cash and cash equivalents at end of the year		1,750	10,746

The notes on pages 8 to 68 form part of these consolidated financial statements.

(tabular amounts in thousands of US dollars)

1 General information

The principal executive office of Tethys Petroleum Limited and its subsidiaries (collectively "Tethys" or "the Company") are in Guernsey, British Isles. The domicile of Tethys Petroleum Limited is the Cayman Islands, where it is incorporated. The address of the Company's registered office is 89 Nexus Way, Camana Bay, Grand Cayman, Cayman Islands. Tethys is an oil and gas company operating within the Republic of Kazakhstan, Republic of Uzbekistan and the Republic of Tajikistan. Tethys' principal activity is the acquisition of and exploration and development of crude oil and natural gas fields.

The Company has its primary listing on the Toronto Stock Exchange (TSX) and a secondary listing on the Kazakhstan Stock Exchange (KASE) in Almaty. On July 25, 2011 the Company was admitted to the London Stock Exchange with respect to a Standard Listing.

Statement of compliance

These consolidated financial statements have been prepared on a going concern basis under the historical cost convention except as modified by the revaluation of available for sale financial assets, and financial assets and financial liabilities at fair value through profit and loss and are in accordance with International Financial Reporting Standards ("IFRSs") and IFRIC interpretations issued by the IFRS Interpretations Committee and effective or issued and early adopted as at the time of preparing these consolidated financial statements.

These consolidated financial statements have also been prepared in accordance with the requirements of the Disclosure and Transparency Rules ('DTR') of the Financial Services Authority ('FSA') in the United Kingdom.

The preparation of financial statements in conformity with IFRS requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on management's best knowledge of the amount, event or actions, actual results ultimately may differ from those estimates. Areas where estimates are significant to the consolidated financial statements are disclosed in note 4.

2 Summary of significant accounting policies

Basis of preparation

The consolidated financial statements are presented in United States Dollars ('USD' or '$'). Foreign operations are included in accordance with the policies set out in this note.

Going concern

The directors have considered the Company's current activities, funding position and projected funding requirements for the period of at least twelve months from the date of approval of the consolidated financial statements, in concluding whether it is appropriate to adopt the going concern basis in preparing the consolidated financial statements for the year ended 31 December 2012. The Company's activities, together with the factors likely to affect its future development, performance and position are set out in the Management Discussion & Analysis document. The financial position of the Company, its cash flows and liquidity position are as set out in these consolidated financial statements and discussed further in the Management Discussion & Analysis document. The Company reports a loss for the twelve months ended December 31, 2012 of USD24.1 million (2011: USD27.0 million) and has net current liabilities of USD9.9 million as at 31 December 2012. As at February 28, 2013, the Company held cash of USD2.3 million.

Phases 1 and 2 of the AOT rail terminal at Shalkar have been completed (though Phase 2 is still subject to State Commission approval) which, following the installation of two 1,000 cubic metre tanks (approximately 12,500 barrels), associated dehydration and pumping equipment, allows an increase in throughput capacity from 4,200 barrels of oil per day up to 6,300 bopd. The terminal will cope comfortably with the production levels of 4,000 bopd, which the Company believes will be sufficient to generate adequate levels of cash to fund its ongoing activities and its current capital expenditure plans.

In the third quarter of 2012 the oil produced and trucked steadily increased every month and this trend continued into the final quarter of the year. The further production increases in the fourth quarter would suggest that we are on route to achieving the maximum production output, which Tethys believes is 4,500 bopd with the current wells drilled but our cash flow forecasts have been based on 4,000 bopd.

To assist with its commitments, the Company put in place a loan secured against drilling equipment. The total amount of the loan was USD10 million and the first tranche of USD4 million was completed in December 2011, the second tranche of USD3.2 million was completed in February and of the final tranche of USD2.8 million, was completed in March 2012. With regard to those lenders who elected for Option A, the loans were due for settlement after 12 months which would have seen USD2.17 million repaid in December 2012, USD2.40 million in February and USD1.30 million in March. All of these loans have been successfully rolled over for a further twelve months and repayments in full assumed in the cash flows for the period under consideration

Also the Company through its Kazakh subsidiary had reached agreement on an USD16.0 million (KZT 2,460 million) funding facility. This facility is provided to Tethys Aral Gas ("TAG") by a Kazakh bank via its partners in Kazakhstan, and is available to fund capital expenditures in Kazakhstan. While the funds were initially provided in the form of a loan this was subsequently changed in January 2013 to be on an advanced payment of sales basis. An initial USD3.5 million of this facility was drawn down in June 2012 with further monthly drawdowns in the period September to December 2012 resulting in a total of USD8.9 million at the end of the year. A request for a further USD4 million has been submitted and we are anticipating these funds to be received shortly.

While the Directors are confident based on discussions with their Kazakh partners that the USD4 million will be received shortly, should it not do so or be delayed then the Company is confident that appropriate steps can be taken to ease this situation through the postponement of certain capital expenditure items combined with the short term deferral of certain supplier payments. In the longer term the increased production levels in Kazakhstan should fund the Company's ongoing operations while the Company makes further arrangements for other areas of expansion.

The Company is currently adopting a prudent approach to cash management and will proceed with such projects when certain milestones have been met and adequate funding is available. Discussions have also been initiated with regard to reserve based lending and on other corporate and project related financing options. Discussions are ongoing with a number of banks which could see the Company adding to or replacing the existing Kazakh loan.

With regard to longer term requirements, the Company regularly considers farm-out/farm-in and joint venture opportunities as a means of developing its business and sharing financial and/or commercial risks

On October 26, 2012, the Company announced that Kulob Petroleum Limited, its subsidiary, which is the Contractor party to the Bokhtar Production Sharing Contract in Tajikistan, had signed a MOU to execute a farm-out agreement ("FOA") on the PSC. The potential acquiring party was an international oil and gas company. This was followed on December 21 2012 when it was announced that the Company had signed a FOA with subsidiaries of Total S.A. and the China National Oil and Gas Exploration and Development Corporation. Should this FOA go ahead then the Company cash flow would be boosted by a sum of approximately USD60 million.

The Directors have examined these matters to form a view on the Company's ability to realise its assets and discharge its liabilities in the normal course of business. After making enquiries and considering the circumstances referred to above, the Directors have a reasonable expectation that the company has adequate resources and potential to continue operations for at least the next twelve months. For these reasons they continue to adopt the going concern basis of accounting in preparing the consolidated financial statements.

Foreign Operations

Tethys' future operations and earnings will depend upon the results of Tethys' operations in the Republic of Kazakhstan, Uzbekistan and Tajikistan. There can be no assurance that Tethys will be able to successfully conduct such operations, and a failure to do so would have a material adverse effect on Tethys' financial position, results of operations and cash flows. Also, the success of Tethys' operations will be subject to numerous contingencies, some of which are beyond management control. These contingencies include general and regional economic conditions, prices for crude oil and natural gas, competitions and changes in regulation. Since Tethys is dependent on international operations, Tethys will be subject to various additional political, economic and other uncertainties. Among other risks, Tethys' operations may be subject to the risks and restrictions on transfer of funds, import and export duties, quotas and embargoes, domestic and international customs and tariffs, and changing taxation policies, foreign exchange restrictions, political conditions and regulations.

Changes in presentation

From January 1, 2012, the Company re-classified the administrative costs associated with two of its subsidiaries to business development expenses in the consolidated statement of comprehensive income. The comparative information has been reclassified to conform to the current presentation. The amount re-classified from administrative costs to business development in 2011 was $786,447.

(tabular amounts in thousands of US dollars)

Business development expenses are costs associated with identifying new business opportunities for the Company either within countries in which the Company is currently operating, or in new countries.

New and amended accounting standards adopted by the Company

There were no significant new or amended standards introduced for the current accounting year relevant for the Company for these financial statements.

Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the Company

The following standards and amendments to existing standards have been published and are mandatory for the Company's accounting periods beginning on or after January 1, 2013 or later periods, but the Company has not adopted them early:

- IFRS 10 'Consolidated Financial Statements' – issued in May 2011. This standard is part of a new suite of standards on consolidation and related standards, replacing the existing accounting for subsidiaries and joint ventures (now joint arrangements), and making limited amendments in relation to associates. It supersedes IAS 27 'Consolidated and Separate Financial Statements' and SIC-12 'Consolidation – Special Purpose Entities' (SPEs). It provides a single model to be applied in the control analysis for all investees, including entities that currently are SPEs in the scope of SIC-12. This standard is not applicable until January 1, 2013. The amendments will not result in a material impact on the Company's consolidated financial statements.

- IFRS 11 'Joint Arrangements' – issued in May 2011. This standard is part of a new suite of standards on consolidation and related standards, replacing the existing accounting for subsidiaries and joint ventures (now joint arrangements), and making limited amendments in relation to associates. All parties to a joint arrangement are within the scope of IFRS 11. IFRS 11 carves out from IAS 31 'Interests in Joint Ventures', those cases in which there is a separate vehicle but that separation is overcome by form, contract or other facts and circumstances. It also removes the choice of equity or proportionate accounting for jointly controlled entities. Although this standard is not applicable until January 1, 2013, the Company has considered the potential impact this standard will have on the accounting for existing jointly controlled entities. There will be no impact as the Company will still be able to account for its existing joint arrangements under equity accounting.

- IFRS 12 'Disclosure of Interests in Other Entities' – issued in May 2011. This standard is part of a new suite of standards on consolidation and related standards, replacing the existing accounting for subsidiaries and joint ventures (now joint arrangements), and making limited amendments in relation to associates. It contains the disclosure requirements for entities that have interests in subsidiaries, joint arrangements, associates and/or unconsolidated structured entities. This standard is not applicable until January 1, 2013 and will not result in a material impact to the Company's consolidated financial statements.

- IFRS 13 'Fair Value Measurement' – issued in May 2011. The is a new standard to replace existing guidance on fair value measurement in different IFRSs with a single definition of fair value, a framework for measuring fair values and disclosures about fair value measurements. The standard applies to assets, liabilities and an entity's own equity instruments that, under other IFRSs are required or permitted to be measured at fair value or when disclosure of fair value is provided. This standard is not applicable until January 1, 2013 and will not result in a material impact to the Company's consolidated financial statements.

- IFRS 9 'Financial instruments' – issued in November 2009. This standard is the first step in the process to replace IAS 39, 'Financial instruments: recognition and measurement'. IFRS 9 introduces new requirements for classifying and measuring financial assets and liabilities, which may affect the Company's accounting for its financial assets. The standard is not applicable until January 1, 2015 but is available for early adoption. This standard will have no impact on the Company's consolidated financial statements as currently reported.

Basis of consolidation

Subsidiaries

Subsidiaries are all entities over which the Company has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. Subsidiaries are fully consolidated from the date on which control is transferred to the Company.

The acquisition method of accounting is used to account for business combinations. The cost of acquisition is measured at the fair value of assets given, equity instruments issued and debt incurred or assumed at the date of acquisition, being the date on which the Company gains control. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Acquisition related costs are expensed as incurred. The excess of the cost over the fair value of the Company's share of identifiable net assets acquired is recorded as goodwill. If the cost is less than the fair value of net assets acquired, the difference is recognised directly in the statement of comprehensive loss. All subsidiaries, as listed in note 26, have been consolidated into the Company's consolidated financial statements.

Inter-Company transactions, balances and unrealised gains or losses between subsidiaries are eliminated. The financial statements of the subsidiaries are prepared using consistent accounting policies and reporting date as of the Company.

Joint ventures

The Company's interests in jointly controlled entities are accounted for using the equity method of accounting. Under the equity method, the investment in a jointly controlled entity is carried in the consolidated statement of financial position at cost plus post-acquisition changes in the Company's share of net assets of the jointly controlled entity, less distributions received and less any impairment in value of the investment. The Company's consolidated statement of comprehensive income reflects the Company's share of the results after tax of the jointly controlled entity.

When the Company's share of losses in the jointly controlled entity equals or exceeds its interest in the entity, including any other unsecured receivables, the Company does not recognise further losses, unless it has incurred obligations or made payments on behalf of the jointly controlled entity. Financial statements of jointly controlled entities are prepared for the same reporting year as the Company.

The Company recognises the portion of gains or losses on the sale of assets by the Group to the joint venture that is attributable to the other parties in the joint venture. The Company does not recognise its share of profits or losses that results from the purchase of assets by the Group from the joint venture until when the asset is resold or, where relevant, as the asset is depreciated by the jointly controlled entity.

In circumstances where the significant risks and rewards of ownership of non-monetary assets transferred have not been transferred to the jointly controlled entity, the associated gain or loss is unrealised and, thus, not recognised in profit or loss but recognised as a deferred gain on the consolidated statement of financial position. The deferred gain is recognised in the consolidated statement of comprehensive income when the asset is resold or, where relevant, as the asset is depreciated by the jointly controlled entity.

Accounting policies of the joint venture are consistent with accounting policies adopted by the Company.

Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-makers have been identified as the Executive Directors that make strategic decisions.

Foreign currency translation

Items included in the financial statements of each of the Company's entities are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'), translated into USD where relevant. These consolidated financial statements are presented in USD, which is the Company's presentation currency.

All monetary assets and liabilities denominated in foreign currencies are translated into USD at the rate of exchange in effect at the reporting date. Non-monetary assets are translated at historical exchange rates.

Revenue and expense items (excluding depreciation and amortization which are translated at the same rates as the related assets) are translated at the average rate of exchange.

Exchange gains and losses arising on translation are taken to the consolidated statement of comprehensive income.

(tabular amounts in thousands of US dollars)

Oil and gas exploration and evaluation expenditure

Oil and natural gas exploration and evaluation expenditures are accounted for using the 'successful efforts' method of accounting. Costs are accumulated on a field-by-field basis. Exploration and evaluation expenditures, including license acquisition costs, are capitalised as exploration and evaluation assets when incurred. Expenditure directly associated with an exploration well is capitalised until the determination of reserves is evaluated. All other associated exploration and evaluation expenditures are carried forward as an intangible asset in the consolidated statement of financial position where the rights of tenure of the property are current and it is considered probable that the costs will be recouped through successful development of the property, or alternatively by its sale. Capitalised exploration and evaluation expenditure is written down to its recoverable amount where the above conditions are no longer satisfied.

If it is determined that a commercial discovery has not been achieved in relation to the property, all other associated costs are written down to their recoverable amount. If commercial reserves are found, exploration and evaluation intangible assets are tested for impairment and transferred to appraisal and development tangible assets i.e. Property, Plant and Equipment ('PPE'). No depreciation and/or amortisation is charged during the exploration and evaluation phase.

Test production and the appraisal and development phase

Test production is production that is generated in the appraisal and development phase before commercial discovery of oil is officially recognised. Revenue generated from test production is credited against the cost of the well until commercial and technical feasibility is established and the project is deemed to have crossed over into the production phase. Revenue and costs generated from a field classified as operating in the production phase is recorded through the income statement.

Oil and gas properties in the production phase

Oil and gas properties within PPE are stated at cost, less accumulated depreciation and accumulated impairment losses.

Expenditure on the construction, installation or completion of infrastructure facilities such as platforms, pipelines and the drilling of development wells, including unsuccessful development or delineation wells, is capitalised within oil and gas properties, as long as the facts and circumstances indicate that the field has commercially viable reserves.

The initial cost of an asset comprises its purchase price or construction cost, any costs directly attributable to bringing the asset into operation, the initial estimate of the asset retirement obligation, and for qualifying assets, borrowing costs. The purchase price or construction cost is the aggregate amount paid and the fair value of any other consideration given to acquire the asset. The capitalised value of a finance lease is also included within property, plant and equipment.

Once commercial production in an area of interest has commenced, oil and gas properties are depleted on a unit-of-production basis over the proved and probable reserves of the field concerned, except in the case of assets whose useful life is shorter than the lifetime of the field, in which case

(tabular amounts in thousands of US dollars)

the straight-line method is applied. Rights and concessions are depleted on the unit-of-production basis over the total proved and probable reserves of the relevant area. The unit-of-production rate for the depletion of field development costs takes into account expenditures incurred to date, together with future development expenditure to develop the proved and probable reserves. Changes in factors such as estimates of proved and probable reserves that affect unit-of-production calculations do not give rise to prior year financial period adjustments and are dealt with on a prospective basis.

Other property, plant and equipment

Property, plant and equipment are carried at cost less accumulated depreciation. Depreciation is charged so as to write off the cost of these assets less residual value over their estimated useful economic lives, for the following classes of assets:

Drilling rigs and related oil and gas equipment	Unit of production	3,650 operating days
Smaller rig related equipment	Straight line	6 – 8 years
Vehicles	Straight line	4 years
Computer equipment	Straight line	3 years
Office equipment	Straight line	5 years

Gains and losses on disposal are determined by comparing the proceeds with the carrying amount and are recognised within the consolidated statement of comprehensive income.

Other intangible assets

Production enhancement contracts are stated at cost less accumulated amortisation and have a finite useful life. Amortization is calculated using a unit-of-production basis over the estimated incremental production entitlement expected to be received over the life of the contract.

Impairment of non-financial assets

Exploration and evaluation costs are tested for impairment when reclassified to oil and gas properties or whenever facts and circumstances indicate potential impairment. An impairment loss is recognised for the amount by which the exploration and evaluation expenditure's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of the exploration and evaluation expenditure's fair value less costs to sell and their value in use.

Values of oil and gas properties and other property, plant and equipment are reviewed for impairment when indicators of such impairment exist. If any indication of impairment exists an estimate of the asset's recoverable amount is calculated. Individual assets are grouped for impairment assessment purposes at the lowest level at which there are identifiable cash flows that are largely independent of the cash flows of other groups of assets. An asset group’s recoverable amount is the higher of its fair value less costs to sell and its value in use. Where the carrying amount of an asset group exceeds its recoverable amount, the asset group is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are adjusted for the risks specific to the asset group and are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money.

(tabular amounts in thousands of US dollars)

If the carrying amount of the asset exceeds its recoverable amount, the asset is impaired and an impairment loss is charged to the consolidated statement of comprehensive income so as to reduce the carrying amount to its recoverable amount (i.e. the higher of fair value less costs to sell and value in use).

For assets excluding goodwill, an assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the Company makes an estimate of the recoverable amount. A previously recognised impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. If that is the case, the carrying amount of the asset is increased to its recoverable amount. That increased amount cannot exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years.

Asset retirement obligation (ARO)

Provision is made for the present value of the future cost of abandonment of oil and gas wells and related facilities. This provision is recognised when a legal or constructive obligation arises.

The estimated costs, based on engineering cost levels prevailing at the reporting date, are computed on the basis of the latest assumptions as to the scope and method of abandonment. Provisions are measured at the fair value of the expenditures expected to be required to settle the obligation using a pre-tax risk free rate, updated at each reporting date that reflects current market assessments of the time value of money and the risks specific to the obligation. The corresponding amount is capitalised as part of exploration and evaluation expenditure or oil and gas properties and is amortised on a unit-of-production basis as part of the depreciation, depletion and amortisation charge. Any adjustment arising from the reassessment of estimated cost of ARO is capitalised, whilst the charge arising from the accretion of the discount applied to the ARO is treated as a component of finance costs.

Financial instruments

Financial assets and financial liabilities are recognised on the Company’s consolidated statement of financial position when the Company becomes party to the contractual provisions of the instrument. Financial assets are de-recognised when the contractual rights to the cashflows from the financial asset expire or when the contractual rights to those assets are transferred. Financial liabilities are de-recognised when the obligation specified in the contract is discharged, cancelled or expired. There were no own-use derivative contracts in place during the year.

(tabular amounts in thousands of US dollars)

Restricted cash

Non-current restricted cash comprises restricted current balances that are held on deposit with banks in the Republic of Kazakhstan in respect of the Company's asset retirement obligations (ARO) in that country and are classified as non-current. They are carried at fair value with gains or losses taken to the consolidated statement of comprehensive income.

Current restricted cash comprises monies placed on temporary deposit as a security against corporate credit cards and a deposit with the Ministry of Finance in Dubai as fixed term deposits with banks.

Trade receivables, loans and other receivables

Trade receivables, loans and other receivables, which are non-derivative financial assets that have fixed or determinable payments that are not quoted in an active market, are classified as loans and receivables. They are included in current assets, except for maturities greater than 12 months after the reporting date, which are classified as non-current assets. The Company's loans and receivables comprise trade and other receivables in the consolidated statement of financial position.

Loans and receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest rate method, net of any impairment.

A provision for impairment of trade receivables is established when there is objective evidence that the Company will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments are considered indicators that the trade receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the loss is recognised in the statement of comprehensive loss. When a trade receivable is not collectable, it is written off against the allowance account for trade receivables.

Cash and cash equivalents

Cash and cash equivalents comprise cash in hand, deposits held at call with banks and other short-term highly liquid investments with original maturities of three months or less. These are carried at fair value with gains or losses recognized through the consolidated statement of comprehensive income.

Financial liabilities - borrowings

Borrowings are initially recognised at the fair value of the consideration received less directly attributable transaction costs. After initial recognition, interest bearing loans and borrowings are subsequently measured at amortised cost using the effective interest method. Gains and losses are recognised in the consolidated statement of comprehensive income when the liabilities are derecognised as well as through the amortisation process.

(tabular amounts in thousands of US dollars)

Trade payables

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

Equity instruments

Equity instruments issued by the Company are recorded at the proceeds received net of direct issue costs.

Derivative financial instruments

Derivative financial instruments are initially recognized at fair value on the date a derivative contract was entered into and are subsequently remeasured at their fair value with changes in the fair value immediately recognised in the consolidated statement of comprehensive income.

Derivatives embedded in other financial instruments or other host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of the host contract. Contracts are assessed for embedded derivatives when the Company becomes a party to them, including at the date of a business combination.

Derivative contracts qualifying for the 'own-use' treatment

An 'own-use' contract is one that was entered into and continues to be held for the purpose of the receipt or delivery of the non financial item in accordance with the entity's expected purchase, sale or usage requirements. Contracts that are for the Company's own-use are exempt from the requirements of IAS 39.

Inventories

Inventories consist of refined oil products, spare parts and consumable materials and are shown at the lower of cost and net realisable value. Cost is determined on a weighted average cost method for refined oil products and the first-in-first-out method for spare parts and consumable materials inventories.

Taxation including deferred taxation

The tax expense represents current tax and deferred tax.

Current tax is based on the taxable profits for the year. The Company's current tax is calculated using tax rates that have been enacted or substantively enacted by the reporting date in the countries where the Company and its subsidiaries operate and generate taxable income.

Deferred income tax is recognised, using the liability method, on temporary differences arising between the bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction, other than a business combination, that at the time of the transaction affects neither the accounting nor the taxable profit or loss. Deferred income tax assets are recognised to the extent that it is probable that the future taxable profit will be available against which the temporary differences can be utilised and the carry forward of unused tax credits and unused tax losses can be utilised.

Deferred income tax is determined using tax rates (and laws) that have been enacted or substantively enacted by the reporting date and are expected to apply when the related deferred tax asset is realised or the deferred income tax liability settled.

Share–based payments

The Company operates share-based compensation plans, under which the entity receives services from employees as consideration for equity instruments (options and warrants) of the Company. The fair value of the employee options and warrants granted in exchange for the employee services is recognised as an expense. The total amount to be expensed is determined by reference to the fair value of the options granted, excluding the impact of any non-market service and performance vesting conditions. Non-market vesting conditions are included in assumptions about the number of options that are expected to vest. When options vest in instalments over the vesting period, each instalment is accounted for as a separate arrangement. At each reporting date, the entity revises its estimates of the number of options that are expected to vest. It recognises the impact of the revision of original estimates, if any, in the consolidated statement of comprehensive income, with a corresponding adjustment to equity.

The proceeds received net of any directly attributable transaction costs are credited to share capital and share premium when the options are exercised.

Warrants

Warrants issued to loan holders are regarded as derivative instruments, with a fair value at inception representing the value attributable to the option to convert the warrants into equity of the Company.

IAS 32.11 'Financial Instruments Presentation' states that a derivative contract that will be settled by the equity receiving or delivering a fixed number of its own equity instruments in exchange for a fixed amount of cash or another financial asset is an equity instrument. It also states that a contract that will be settled by the entity delivering or receiving a fixed number of its own equity instruments in exchange for a variable amount of cash or another financial asset is a financial asset or financial liability.

For warrants issued to loan holders by the Company, where there is a difference between the currency in which shares of the parent company are denominated and the functional currency of the Company, the option to convert the warrants is recorded as a derivative liability because it is not a contract to exchange a fixed number of shares for a fixed amount of US dollars. The derivative liability component is separately identified and measured at fair value through the consolidated statement of comprehensive income.

Provisions

Provisions are recognised when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the Company expects some or all of a provision to be reimbursed, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain. The expense relating to any provision is presented in the consolidated statement of comprehensive income, net of any reimbursement. The increase in the provision due to passage of time is recognised as interest expense.

Revenue recognition

Revenue comprises the fair value of the consideration received or receivable for the sale of natural gas and oil products in the ordinary course of the Company's activities and is recognized when the amount can be reliably measured, it is probable that future economic benefits will flow to the entity, and when specific criteria have been met for each of the Company's activities as described below. Revenue is shown after eliminating sales within the Company.

Revenue from natural gas and oil sales is recognised when it has been lifted and the risk of loss transferred to a third-party purchaser and is shown net of Mineral Extraction Tax (MET) and value-added tax. In Kazakhstan, gas was sold under a two year take or pay contract that expired at the end of 2012 and was re-negotiated in 2013. Under IFRIC 4 the economic substance of the transaction is considered, despite the absence of a specific lease contract. Implicitly the sales contract gives the customer specific use of gas assets as they take all gas produced by the Akkulka and Kyzyloi fields, therefore the revenue from Kazakh gas sales is recognised under IAS 17 'Leases', on a production basis over the lease term. Revenue from refined product sales is recognized upon delivery and is shown net of value-added tax. All payments received before delivery are recorded as deferred revenue until delivery has occurred.

The Company recognises finance income earned on the Company's cash and cash equivalents and short term investments on an accrual basis.

Barter transactions

Where goods or services are exchanged for goods or services of a dissimilar nature, the revenue is measured at the fair value of the goods or services received, adjusted by the amount of cash or cash equivalents received or paid. If the fair value of the goods or services received cannot be reliably measured, the revenue is measured at the fair value of the goods or services given up, again adjusted by the amount of cash or cash equivalents received.

(tabular amounts in thousands of US dollars)

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of a qualifying capital asset or project under construction are capitalised and added to the asset or project cost during construction until such time as the asset or project is substantially ready for its intended use. Where funds are specifically borrowed to finance an asset or project, the amount capitalised represents the actual amount of borrowing cost incurred. Where funds used to finance an asset or project form part of general borrowings, the amount capitalised is calculated by using a weighted average of rates applicable to relevant general borrowings of the Company during the period. All other borrowing costs are recognised in the consolidated statement of comprehensive income in the period in which they are incurred.

Leases

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 are charged to the consolidated statement of comprehensive income on a straight-line basis over the period of the lease.

Business combinations

Business combinations are accounted for using the acquisition method of accounting. The cost of an acquisition is measured as the cash paid and the fair value of other assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange. The acquired identifiable assets, liabilities and contingent liabilities are measured at their fair values at the date of acquisition. Any excess of the cost of acquisition over the net fair value of the identifiable assets, liabilities and contingent liabilities acquired is recognized as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognized directly in the consolidated statement of comprehensive income. Acquisition related costs are expensed as incurred.

Goodwill represents the excess of the cost of an acquisition over the fair value of the Company's share of the net identifiable assets of the acquired subsidiary at the date of acquisition. Goodwill on acquisitions of subsidiaries is included in 'intangible assets'. Goodwill is tested annually for impairment and carried at cost less accumulated impairment losses. Impairment losses on goodwill are not reversed. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

Fair value

The fair value of investments, trade and other receivables, trade and other payables approximate their carrying amounts due to the short term maturity of the instruments. Derivative financial instruments are recorded at fair value with movements in fair value recognised through the consolidated statement of comprehensive income.

(tabular amounts in thousands of US dollars)

Amortised Cost

Loan receivables, long term debt and other non-current liabilities have been recorded at amortized cost using the effective interest rate method.

3 Financial Risk Management

The Company's activities expose it to a variety of financial risks: market risk, credit risk and liquidity risk. The Company's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Company's financial performance.

The Executive Board of Directors has overall responsibility for the Company's management of risk, including the identification and analysis of risks faced by the Company and the consideration of controls that monitor changes in risk and minimise risk wherever possible.

a) Financial risk factors

Credit risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to financial instruments fails to meet its contractual obligations. Credit risk arises from the Company's loans receivable from jointly controlled entities, cash and cash equivalents and accounts receivable balances.

With respect to the Company's financial assets, the maximum exposure to credit risk due to default of the counter party is equal to the carrying value of these instruments. The maximum exposure to credit risk as at the reporting date is:

	December 31 2012 $'000	December 31 2011 $'000
Trade receivables	2,096	837
Cash and cash equivalents	1,750	10,746
Restricted cash	2,020	2,292
Loans receivable from jointly controlled entities	2,403	2,013
	8,269	15,888

Concentration of credit risk associated with the above trade receivable balances in Kazakhstan is as a result of contracted sales to three customers during the year. The Company does not believe it is dependent upon these customers for sales due to the nature of gas products and the associated market. The Company's sales in Kazakhstan commenced in December 2007 and the Company has not experienced any credit loss to date. At December 31, 2012, the trade receivable amounted to $2,096,171 (2011 - $836,837), none of which was greater than 30 days overdue. The Company has

(tabular amounts in thousands of US dollars)

therefore not recorded a provision against this amount as it does not consider the balance to be impaired.

In Uzbekistan, the Company has four customers. Full payment is required before delivery of the oil and therefore there is limited exposure to credit risk in this country.

In Tajikistan, the Company has four customers. Full payment is required before delivery of the oil and therefore there is limited exposure to credit risk in this country.

Although a significant amount of the deposits at financial institutions are not covered by bank guarantees, the Company does not believe there to be a significant risk of credit loss as the majority of counterparty banks used are those with high credit ratings (A- or equivalent) assigned by international ratings agencies (Fitch and Standard and Poors). Banks used in Central Asia generally do not have credit ratings assigned by international ratings agencies, however deposits held with these banks are kept to a minimum as far as possible.

The Company is exposed to credit risk in relation to its loans receivable from jointly controlled entities to the extent that the jointly controlled entities fail to meet their contractual obligations. The Company does not believe that the balance is impaired at the reporting date. The carrying amount of the loans receivable represents the maximum exposure to credit risk at each balance sheet date.

Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. This risk relates to the Company's ability to generate or obtain sufficient cash or cash equivalents to satisfy these financial obligations as they become due. Since inception, the Company has incurred significant consolidated losses from operations and negative cash flows from operating activities, and has an accumulated deficit at December 31, 2012.

The Company's processes for managing liquidity risk includes preparing and monitoring capital and operating budgets, co-ordinating and authorizing project expenditures and ensuring appropriate authorization of contractual agreements. The budget and expenditure levels are reviewed on a regular basis and updated when circumstances indicate change is appropriate. The Company seeks additional financing based on the results of these processes.

(tabular amounts in thousands of US dollars)

The following are the contractual maturities of financial liabilities, including estimated interest payments:

December 31, 2012 Non-derivative financial liabilities	**Carrying amount**	**Contractual cash flows**	**Less than 1 year**	**1-3 years**	**4-5 years**	**Thereafter**
	$’000	**$’000**	**$’000**	**$’000**	**$’000**	**$’000**
Trade and other payables	8,852	9,124	8,589	374	161	-
Financial liabilities -	17,313	19,800	15,569	4,231	-	-
	26,165	28,924	24,158	4,605	161	-

At December 31, 2012 there were no derivative financial liabilities.

December 31, 2011 Non-derivative financial liabilities	**Carrying amount**	**Contractual cash flows**	**Less than 1 year**	**1-3 years**	**4-5 years**	**Thereafter**
	$’000	**$’000**	**$’000**	**$’000**	**$’000**	**$’000**
Trade and other payables	10,726	11,108	10,289	437	382	-
Financial liabilities - borrowings (note 20)	10,028	11,029	9,537	1,492	-	-
	20,754	22,137	19,826	1,929	382	-

December 31, 2011 Derivative financial liabilities	**Carrying amount**	**Contractual cash flows**	**Less than 1 year**	**1-3 years**	**4-5 years**	**Thereafter**
	$’000	**$’000**	**$’000**	**$’000**	**$’000**	**$’000**
Foreign currency hedge contracts	157	157	157	-	-	-

The gross cash outflows disclosed in the above table represent the contractual undiscounted cash flows relating to derivative financial liabilities held for risk management purposes and which are not usually closed out prior to contractual maturity. The disclosure shows expected outflow amounts for derivatives that have simultaneous gross cash settlement. These derivatives are foreign currency put options with a clause requiring conversion to a forward should a barrier of $1.5675 be breached. The cash flows may be different from the recorded amount depending on movements in the USD/GBP foreign exchange rate. Should the foreign exchange rate on the date of expiry be above $1.5675 then no payment would be required. Should the rate be above $1.6495 then the options could be exercised at a gain.

It is not expected that the cash flows included in the maturity schedule could occur significantly earlier, or at significantly different amounts.

There can be no assurance that debt or equity financing will be available or sufficient to meet the Company's requirements or if debt or equity financing is available, that it will be on terms acceptable to the Company. The inability of the Company to access sufficient capital for its operations could have a material adverse impact on the Company's financial condition, results of operations and prospects.

Market risk

Market risk is the risk of loss that may arise from changes in market factors such as commodity prices, interest rate and foreign exchange rates.

Commodity price risk

Commodity price risk arises from the effect that fluctuations of future commodity prices may have on the price received for sales of gas and refined oil products. The marketability and price of natural gas and oil that is produced and may be discovered by the Company will be affected by numerous factors that are beyond the control of the Company.

Natural gas prices are subject to wide fluctuations: the Company has therefore entered into a fixed price contract for sales of gas from the Kyzyloi field in Kazakhstan. However, any material decline in natural gas prices could result in a reduction of Tethys' future net production revenues and impact on the commercial viability of the Company's existing and future oil and gas discoveries. It may become uneconomic to produce from some wells as a result of lower prices, which could result in a reduction in volumes and the value of Tethys' gas reserves, if the Company elected not to produce from certain wells at lower prices.

Any material decline in oil product prices could result in a reduction of the Company's oil revenues in both Uzbekistan and Kazakhstan.

All of these factors could result in a material decrease in the Company's net production revenue causing a reduction in its acquisition and development activities.

Interest rate risk

Interest rate risk is the risk that the value of a financial instrument will be affected by changes in market interest rates. Existing long term debt is agreed at fixed interest rates and consequently has limited exposure to changes in market interest rates.

(tabular amounts in thousands of US dollars)

The Company is exposed to interest rate risk on short term deposits to the extent that the significant reductions in market interest rates would result in a decrease in the interest earned by the Company. A change of 100 basis points in the interest rate would have had a change of $4,344 in the interest earned in the current year (2011 - $305,365).

As at the reporting date the Company's interest rate profile was:

At December 31, 2012	**Fixed rate financial instruments $'000**	**Variable rate financial instruments $'000**	**Total $'000**
Restricted cash	1,543	477	2,020
Cash and cash equivalents	-	1,750	1,750
Financial liabilities - borrowings	(17,313)	-	(17,313)
	(15,770)	2,227	(13,543)

At December 31, 2011	**Fixed rate financial instruments $'000**	**Variable rate financial instruments $'000**	**Total $'000**
Restricted cash	1,407	885	2,292
Cash and cash equivalents	3,465	7,281	10,746
Financial liabilities - borrowings	(10,028)	-	(10,028)
Interest rate swap	630	-	630
	(4,526)	8,166	3,640

Foreign exchange risk

The Company is exposed to risks resulting from fluctuations in foreign currency exchange rates. A material change in the value of any such foreign currency could result in a material adverse effect on the Company's cash flow and future profits. The Company is exposed to exchange rate risk to the extent that balances and transactions are denominated in a currency other than the USD. In addition, a portion of expenditures in Kazakhstan and Tajikistan are denominated in local currency, the Tenge and Somoni, respectively. The Company also attempts to negotiate exchange rate stabilization conditions in new local Tenge denominated service and supply contracts in Kazakhstan.

During 2011, the Company used an exchange rate derivative to manage its risk as a result of the significant exchange rate fluctuation of the USD against GBP (note 20.4).

The Company holds the majority of its cash and cash equivalents in USD. However, the Company does maintain deposits in other currencies, as disclosed in the following table, in order to fund ongoing general and administrative activity and other expenditure incurred in these currencies.

(tabular amounts in thousands of US dollars)

The carrying amounts of the Company's significant foreign currency denominated monetary assets and liabilities at the reporting dates are as follows:

In USD equivalent at December 31, 2012	**CAD '000**	**GBP '000**	**EUR '000**	**KZT '000**
Cash and cash equivalents	1	220	21	1,032
Trade and other receivables	-	39	18	11,840
Trade and other payables	(53)	(449)	(6)	(448)
Financial liabilities – borrowings	-	(2,005)	-	(8,559)
Net exposure	**(52)**	**(2,195)**	**33**	**3,865**

In USD equivalent at December 31, 2011	**CAD '000**	**GBP '000**	**EUR '000**	**KZT '000**
Cash and cash equivalents	137	810	62	1,647
Trade and other receivables	-	31	42	12,651
Trade and other payables	-	(229)	-	(4,187)
Financial liabilities – borrowings	-	(433)	-	-
Net exposure	**137**	**179**	**104**	**10,111**

The following table details the Company's sensitivity to a 10% movement in USD against the respective foreign currencies, which represents management's assessment of a reasonably likely change in foreign exchange rates.

2012 Effect in USD'000	**CAD**	**GBP**	**EUR**	**KZT**
Profit or (loss) before tax	(5)	(219)	3	386
2011 Effect in USD'000				
Profit or (loss) before tax	14	18	10	1,011

A 10% strengthening of the USD against the currencies above at December 31, 2012 would have had an equal but opposite effect on the amounts shown above, assuming all other variables remained constant.

b) Capital risk management

The Company's capital structure is comprised of shareholders' equity and net debt.

The Company's objectives when managing capital is to maintain adequate financial flexibility to preserve its ability to meet financial obligations, both current and long term. The capital structure of the Company is managed and adjusted to reflect changes in economic conditions.

(tabular amounts in thousands of US dollars)

The Company funds its expenditures on commitments from existing cash and cash equivalent balances, primarily received from issuances of shareholders equity and some debt financing. None of the outstanding debt is subject to externally imposed capital requirements.

Financing decisions are made by management and the Board of Directors based on forecasts of the expected timing and level of capital and operating expenditure required to meet the Company's commitments and development plans. Factors considered when determining whether to issue new debt or to seek equity financing include the amount of financing required, the availability of financial resources, the terms on which financing is available and consideration of the balance between shareholder value creation and prudent financial risk management.

Net debt is calculated as total borrowings (including 'current and non-current borrowings' as shown in the consolidated statement of financial position) less cash and cash equivalents. Total capital is calculated as 'equity' as shown in the consolidated statement of financial position plus net debt.

At December 31	**2012**	**2011**
	$'000	**$'000**
Total financial liabilities - borrowings (Note 20)	17,313	10,028
Less: cash and cash equivalents	(1,750)	(10,746)
Net debt / (funds)	15,563	(718)
Total equity	220,153	237,880
Total capital	235,716	237,162

If the Company is in a net debt position, the Company will assess whether the projected cash flow is sufficient to service this debt and support ongoing operations. Consideration will be given to reducing the total debt or raising funds through an alternative route such as the issuing of equity.

c) Fair value hierarchy

The tables below analyse financial instruments carried at fair value by valuation method. The different levels have been defined as follows:

Level 1: Quoted prices (unadjusted) in active markets for identical assets and liabilities. The Company does not have any assets or liabilities that require Level 1 inputs.

Level 2: Inputs other than quoted prices included within Level 1 that are observable, either directly or indirectly. For the Company, Level 2 inputs include prices that can be corroborated with other observable inputs for substantially the complete term of the contract.

Level 3: Unobservable inputs. For the Company, Level 3 inputs include production and price assumptions that are not based on observable market data (unobservable inputs) or are reliant on adjustments or interpolations are made by management to an otherwise standard valuation model.

(tabular amounts in thousands of US dollars)

December 31, 2012	**Level 1 $'000**	**Level 2 $'000**	**Level 3 $'000**	**Total $'000**
Warrants (note 20.2)	-	523	-	523
Total liabilities	**-**	**523**	**-**	**523**

December 31, 2011	**Level 1 $'000**	**Level 2 $'000**	**Level 3 $'000**	**Total $'000**
Interest rate swap (note 20.3)	-	-	630	630
Total assets	**-**	**-**	**630**	**630**
Warrants (note 20.2)	-	264	-	264
Foreign currency hedge (note 20.4)	-	157	-	157
Total liabilities	**-**	**421**	**-**	**421**

4 Critical judgements and accounting estimates

The preparation of financial statements requires management to make certain judgements, accounting estimates and assumptions that affect the amounts reported for assets and liabilities as at the reporting date and the amounts reported for revenues and expenses during the year. The nature of estimation means that actual outcomes could differ from those estimates. Accordingly, the impact of these estimates, assumptions and judgments on the consolidated financial statements in future periods could be material. The key sources of estimation uncertainty that have a significant risk of causing material adjustment to the carrying amounts of assets and liabilities are discussed below.

Recoverability of asset carrying values

The Company assesses its property, plant and equipment, including intangible exploration and evaluation assets, for possible impairment if there are events or changes in circumstances that indicate that carrying values of the assets may not be recoverable, or at least at every reporting date. Such indicators include changes in the Company's business plans, changes in commodity prices, evidence of physical damage and, for oil and gas properties, significant downward revisions of estimated recoverable volumes or increases in estimated future development expenditure.

If there are low oil prices or natural gas prices during an extended period the Company may need to recognise significant impairment charges. The assessment for impairment entails comparing the carrying value of the cash-generating unit with its recoverable amount, that is, value in use. Value in use is usually determined on the basis of discounted estimated future net cash flows. Determination as to whether and how much an asset is impaired involves management estimates on highly uncertain matters such as future commodity prices, the effects of inflation on operating expenses, discount rates, production profiles and the outlook for regional market supply-and-demand conditions for crude oil, natural gas and refined products.

At December 31, 2012 and 2011, the Company considered circumstances relating to its property plant and equipment and intangible and exploration and evaluation assets and concluded that the further decline in production from the North Urtabulak field to be an indicator of impairment. An impairment test was performed as detailed in notes 12 and 13.

Oil and gas reserves

Proved and probable oil and gas reserves are used in the units of production calculation for depletion as well as the determination of the timing of well closure costs and impairment analysis. There are numerous uncertainties inherent in estimating oil and gas reserves. Assumptions that are valid at the time of estimation may change significantly when new information becomes available. Changes in the forecast prices of commodities, exchange rates, production costs or recovery rates may change the economic status of reserves and may ultimately result in the reserves being restated.

The Company makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. Such estimates and assumptions are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Asset retirement obligation

Provisions for environmental clean-up and remediation costs associated with the Company's drilling operations are based on current legal or constructive requirements, technology, price levels and expected plans for remediation. Actual costs and cash outflows can differ from estimates because of changes in laws and regulations, public expectations, prices, discovery and analysis of site conditions and changes in clean-up technology.

Income taxes

The Company is subject to income taxes in numerous jurisdictions. Significant judgement is required in determining the worldwide provision for income taxes. There are many transactions and calculations for which the ultimate tax determination is uncertain. The Company recognises liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the current and deferred income tax assets and liabilities in the period in which such determination is made.

Fair value of derivative and other financial instruments

The fair value of financial instruments that are not traded in an active market is determined by using valuation techniques. The Company uses its judgement to select a variety of methods and make assumptions that are mainly based on market conditions existing at the end of each reporting period.

(tabular amounts in thousands of US dollars)

Other significant areas of judgement

The estimates, assumptions and judgments made in relation to the fair value of stock based compensation and warrants and the associated expense recognition are subject to measurement uncertainty. The estimated fair values of financial assets and liabilities, by their very nature, are subject to measurement uncertainty.

5 Segmental Reporting

Geographical segments

Management has determined the operating segments based on the reports reviewed by the executive directors that are used to make strategic decisions. Reports provided to the executive directors with respect to segment information are measured in a manner consistent with that of the consolidated financial statements. The assets and liabilities are allocated based on the operations of the segment and for assets, the physical location of the asset.

The Executive Directors consider the business from predominantly a geographic perspective and the Company currently operates in three geographical markets: Kazakhstan, Tajikistan and Uzbekistan.

In Kazakhstan, the Company is producing oil and gas from the Kyzyloi and Akkulka fields and is undertaking exploration and evaluation activity in the Kul-bas field. In Tajikistan, the Company is currently undertaking exploration and evaluation activity together with a small amount of production and, in Uzbekistan, the Company operates under the North Urtabulak Production Enhancement Contract, which gives incremental production rights to increase the production volume of oil from wells on the North Urtabulak Oil Field. The Company also operates a corporate segment which acquired a number of drilling rigs and related oil and gas equipment which are utilised in Kazakhstan, Tajikistan, and Uzbekistan according to operational requirements.

(tabular amounts in thousands of US dollars)

The segment results for the year ended December 31, 2012 are as follows:

	Kazakhstan $'000	Tajikistan $'000	Uzbekistan $'000	Other and Corporate $'000	Consolidated $'000
Gas sales	5,875	-	-	-	5,875
Oil sales	25,632	1,875	-	-	27,507
Refined product sales	-	-	4,478	-	4,478
Other income	247	-	-	-	247
Other operating income	-	-	-	3,928	3,928
Segment revenue and other income	**31,754**	**1,875**	**4,478**	**3,928**	**42,035**
Inter-segment revenue	-	-	-	(3,928)	(3,928)
Segment revenue and other income from external customers	**31,754**	**1,875**	**4,478**	**-**	**38,107**
Profit from jointly controlled entity	191	-	-	-	191
Profit / (loss) before taxation	**2,826**	**(2,816)**	**292**	**(20,172)**	**(19,870)**
Taxation	(1,215)	-	(236)	417	(1,034)
Net profit / (loss) for the year	**1,611**	**(2,816)**	**56**	**(19,755)**	**(20,904)**

Sales in the Kazakhstan segment were made to three customers. Sales to those customers representing greater than 10% of total segment revenue were $25,631,680 and $5,874,776.

Sales in the Uzbekistan segment were to one customer.

Sales in the Tajikistan segment were to four customers. Sales to those customers representing greater than 10% of total segment revenue were $536,905, $818,572 and $228,049.

Borrowing costs of $697,896 and $678,398 incurred in the Corporate segment were capitalised in the Tajik and Kazakh segments respectively during the year.

Amortisation of $193,454 of assets held in the Corporate segment was capitalised in the Kazakh segment during the year.

(tabular amounts in thousands of US dollars)

Segment results for the year ended December 31, 2011 were as follows:

	Kazakhstan $'000 re-presented	**Tajikistan $'000 re-presented**	**Uzbekistan $'000 re-presented**	**Other and Corporate $'000 re-presented**	**Consolidated $'000 re-presented**
Gas sales	7,027	-	-	-	7,027
Oil sales	8,130	55	-	-	8,185
Refined product sales	-	-	7,255	-	7,255
Other income	260	-	195	-	455
Other operating income	-	-	-	9,246	9,246
Segment revenue and other income from external customers	**15,417**	**55**	**7,450**	**9,246**	**32,168**
Inter-segment revenue	(-)	-	-	(1,871)	(1,871)
Segment revenue and other income from external customers	**15,417**	**55**	**7,450**	**7,375**	**30,297**
Loss from jointly controlled entity	-	(722)	-	-	(722)
(Loss) / Profit before taxation	**(7,563)**	**2,650**	**(7,843)**	**(16,180)**	**(28,936)**
Taxation	1,105	-	843	(1)	1,947
Net (loss) / profit for the year	**(6,458)**	**2,650**	**(7,000)**	**(16,181)**	**(26,989)**

Sales in the Kazakhstan segment were made to two customers. Sales to those customers representing greater than 10% of total segment revenue were $7,027,105 and $8,130,464. Sales in the Uzbekistan segment were to three customers. Sales to two of those customers representing greater than 10% of total segment revenue were $2,387,530 and $4,160,777 respectively.

The profit of the Tajik segment was as a result of the net fair value gain arising on the acquisition of Seven Stars Energy Corporation ('SSEC') as detailed in note 25.

Borrowing costs of $973,506 were incurred in the Corporate segment during the year. These borrowing costs were capitalised in the Kazakhstan segment.

Amortisation of $506,120 of assets held in the Corporate segment were capitalised in Kazakhstan.

(tabular amounts in thousands of US dollars)

The segment assets and liabilities as at December 31, 2012 and capital expenditures for the year then ended are as follows:

	Kazakhstan $'000	Tajikistan $'000	Uzbekistan $'000	Other and Corporate $'000	Consolidated $'000
Total assets	138,510	87,075	6,815	19,553	251,953
Total liabilities	13,945	2,989	4,367	10,499	31,800
Cash expenditure on exploration & evaluation assets, property, plant and equipment	8,929	8,043	471	58	17,501
Depreciation, depletion & amortization	14,250	1,373	1,111	1,690	18,424

Included in Kazakh and Tajik liabilities are payables in relation to exploration and evaluation assets of $3,320 and $2,377,198 respectively.

Total assets and liabilities for Tajikistan include the underlying assets of Seven Stars Energy Corporation ('SSEC') and its subsidiaries.

The segment assets and liabilities at December 31, 2011 and capital expenditures for the year then ended are as follows:

	Kazakhstan $'000	Tajikistan $'000	Uzbekistan $'000	Other and Corporate $'000	Consolidated $'000
Total assets	148,844	78,158	7,702	28,687	263,391
Total liabilities	8,074	1,811	4,000	11,626	25,511
Cash expenditure on exploration & evaluation assets, property, plant and equipment	37,020	880	3,772	230	41,902
Depreciation, depletion & amortization	9,418	77	1,058	2,558	13,111

Included in Kazakhstan liabilities are payables in relation to exploration and evaluation assets of $409,985.

Total assets and liabilities for Tajikistan include the underlying assets of Seven Stars Energy Corporation ('SSEC') and its subsidiaries.

(tabular amounts in thousands of US dollars)

6 Sales and other operating revenues

	Year ended	
	December 31, 2012 $'000	**December 31, 2011 $'000**
Gas sales	5,875	7,027
Oil sales	27,507	8,185
Refined product sales	4,478	7,255
Other revenue	247	455
	38,107	22,922

Revenue has been grossed up for non-monetary transactions, namely utility services of $474,430 provided with respect to Uzbekistan (2011: $707,018). The corresponding expenses are shown within production expenses.

7 Other operating income

	Year ended	
	December 31, 2012 $'000	**December 31, 2011 $'000**
Other operating income	-	7,375

During 2010 and the first half of 2011, a drilling rig together with associated equipment, all owned by the Company, was rented to a subsidiary of Seven Stars Energy Corporation ('SSEC') on commercial terms. In accordance with the shareholders agreement, the amounts receivable on respect of the rental are to be added to the loan due from that entity. When preparing the 2010 annual financial statements and the interim financial statements for Q1 2011, these amounts were eliminated in full rather than proportionate to the Company's equity accounted interest, and no income was recognised. Following progress made on the EOL09 well, as set out in more detail on page 9 of the Management's Discussion and Analysis document, the directors reconsidered this matter and considered it appropriate that the income be included for the period to December 13, 2011 – the date that SSEC became a subsidiary (note 16).

Accordingly, other operating income for the period to December 13, 2011 includes $7,374,090 in respect of these transactions, of which $3,835,320 relates to the year ended December 31, 2010. The invoices have not been settled and there was consequently no impact on the Company's cash flows. There was also no impact on tax expense as a result of this income being recognised.

Since December 13, 2011, the date on which SSEC became a subsidiary of the Company, this operating income has been eliminated on consolidation.

(tabular amounts in thousands of US dollars)

8 Administrative expenses

Administrative expenses by nature	Year ended December 31, 2012 $'000	Year ended December 31, 2011 $'000 (re-presented)
Staff expenses	9,418	8,346
Travel expenses	3,091	3,548
Professional fees	2,516	2,577
Office costs	2,491	2,537
Other administrative expenses	2,157	2,755
	19,673	19,763

Key management personnel have been identified as four Board of Directors and ten vice presidents. Details of key management remuneration are shown in note 26.

As disclosed in note 2, from January 1, 2012, the Company re-classified the administrative costs associated with two of its subsidiaries to business development expenses in the consolidated statement of comprehensive income. The comparative information has been reclassified to conform to the current presentation. The amount re-classified from administrative costs to business development in 2011 was $786,447.

9 Share-based payments

The Company has adopted a stock incentive plan referred to as the "2007 Long Term Stock Incentive Plan" pursuant to which the Company may grant stock options to any director, employee or consultant of the Company, or any subsidiary or Vazon Energy Limited (collectively, "Service Providers").

The maximum number of Ordinary Shares reserved for issuance under the plan equals 12% (2011: 12%) of the outstanding Ordinary Shares. The plan is administered by the Compensation and Nomination Committee of the Board of Directors. Options may be granted pursuant to recommendations of the Compensation and Nomination Committee. The Compensation and Nomination Committee may determine the vesting schedule and term, provided that options may not have a term exceeding ten years. Subject to any resolution passed by the Compensation and Nomination Committee, options will terminate three months after an option holder ceases to be a Service Provider.

The exercise price of options granted under the plan may not be less than the closing price of Ordinary Shares on the principal stock exchange where the Ordinary Shares are listed as of the date of the option grant. The plan contains amendment provisions which allow amendments to the plan by the Board of Directors, without shareholder approval, for amendments of a "housekeeping" nature, changes to vesting or termination provisions, and discontinuance of the plan. The plan also provides that outstanding options will vest immediately on the occurrence of a "change of control"

(tabular amounts in thousands of US dollars)

(as defined in the plan). Options granted under the plan are only assignable to certain related entities of an option holder or otherwise with the consent of the Company.

Under the plan, the options vest in three tranches with one third vesting immediately, one third after one year and one third after two years. These options are equity settled share based payment transactions.

Stock options

The following table summarizes the stock option activity under the 2007 Long Term Stock Incentive Plan.

	Number of options	Weighted average exercise price $
Outstanding at January 1, 2011	22,263,000	1.65
Granted	6,720,000	0.78
Forfeited	(40,000)	1.56
Exercised	-	n/a
Expired	(20,000)	1.56
Outstanding at December 31, 2011	28,923,000	1.45
Exercisable at December 31, 2011	20,791,000	1.58
Outstanding at January 1, 2012	28,923,000	1.45
Granted	5,505,000	0.87
Forfeited	(122,000)	1.00
Exercised	(15,000)	0.60
Expired	(427,000)	1.63
Outstanding at December 31, 2012	33,864,000	1.35
Exercisable at December 31, 2012	28,056,000	1.46

In 2012, the weighted average share price at the date of exercise was $0.96. No options were exercised during 2011.

(tabular amounts in thousands of US dollars)

The following table lists the options outstanding at December 31, 2012 by exercise price:

Exercise price $	Options outstanding	Weighted average remaining term (in years)	Options exercisable	Weighted average remaining term (in years)
0.60	4,570,000	1.59	4,570,000	1.59
CAD0.66	6,240,000	1.64	4,120,000	1.64
CAD0.71	60,000	2.09	20,000	2.09
0.80	3,314,000	2.00	3,314,000	2.00
0.88	120,000	1.83	120,000	1.83
CAD0.88	5,172,000	4.32	1,724,000	4.32
CAD1.60	3,954,000	2.80	3,954,000	2.80
CAD1.72	240,000	3.21	160,000	3.21
2.00	360,000	3.12	240,000	3.12
2.10	3,384,000	2.27	3,384,000	2.27
2.50	2,280,000	2.57	2,280,000	2.57
2.75	4,170,000	1.52	4,170,000	1.52
Total	33,864,000	2.35	28,056,000	2.16

The fair value of the share-based payment grants is estimated using the Black-Scholes pricing model using the following average assumptions:

	December 31, 2012	December 31, 2011
Weighted average fair value	$0.4164	$0.2825
Risk free rate	1.08%	1.6%
Expected term	2.96 years	2 years
Volatility	79%	71.6%
Dividend	Nil	Nil
Weighted average share price of options exercised in year	$0.96	-

In estimating expected volatility, the Company considers the historical volatility of its own share price over the most recent period that is commensurate with the expected option term.

(tabular amounts in thousands of US dollars)

Warrants

The following table summarizes the warrant activity for the years ended December 31, 2012 and December 31, 2011.

	Number of warrants	Weighted average exercise price $
Outstanding at January 1, 2011	7,504,003	5.25
Expired	(2,255,835)	5.50
Outstanding at December 31, 2011	5,248,168	5.14
Exercisable at December 31, 2011	5,248,168	5.14
Outstanding at January 1, 2012	5,248,168	5.14
Granted	164,538	1.01
Expired	(3,158,168)	6.88
Outstanding at December 31, 2012	2,254,538	2.39
Exercisable at December 31, 2012	2,254,538	2.39

Of the warrants outstanding and exercisable at the end of the year, 590,000 relate to warrants granted to the Company's officers.

There are no performance conditions attached to the warrants and all the granted warrants were immediately vested. Warrants are equity settled share based payment transactions.

In estimating expected volatility, the Company considers the historical volatility of its own share price over the most recent period that is commensurate with the expected warrant term.

The following table lists the warrants outstanding at December 31, 2012 by exercise price.

Exercise price $	Warrants outstanding	Weighted average remaining term (in years)	Warrants exercisable	Weighted average remaining term (in years)
2.50	2,090,000	4.44	2,090,000	4.44
1.12	100,038	0.92	100,038	0.92
0.84	64,500	0.65	64,500	0.65
	2,254,538	4.17	2,254,538	4.17

As at December 31, 2012, there was no unrecognized expense related to unvested warrants.

(tabular amounts in thousands of US dollars)

10 Taxation

Tethys is domiciled in the Cayman Islands which has no Company income tax. The Group also operates in other tax jurisdictions, the most significant of which is Kazakhstan where the tax rate is 20%.

The Company had the following balances of non-capital losses in respect of which no deferred tax asset has been recognized:

	Kazakhstan $'000	Netherlands $'000	December 31, 2012 $'000
Within one year	-	-	-
One to five years	218	-	218
After five years	-	3,403	3,403
No expiry date	-	-	-
	218	3,403	3,621

The temporary differences comprising the net deferred income tax liability are as follows:

	December 31, 2012 $'000	December 31, 2011 $'000
Capital assets	1,861	2,937
Tax losses	(582)	(969)
Other	1,633	143
Net deferred tax liability	2,912	2,111

(tabular amounts in thousands of US dollars)

The provision for income taxes is different from the expected provision for income taxes for the following reasons:

	Year ended December 31, 2012 $'000	December 31, 2011 $'000
Loss before income taxes	(19,870)	(28,936)
Income tax rate	20%	20%
Expected income tax (recovery)	(3,974)	(5,787)
Increase/ (decrease) resulting from:		
Non-deductible expenses	(31)	68
Impact of effective tax rates in other foreign jurisdictions	3,899	2,177
Losses and tax assets not utilised/recognised	881	1,629
Prior year adjustments	278	-
Other	(19)	(34)
	1,034	(1,947)
Current tax expense	233	-
Deferred tax (benefit) / expense	801	(1,947)
	1,034	(1,947)

11 Loss per share

Basic and diluted loss per share

	Loss for the year $'000	Weighted average number of shares (thousands)	Per share amount $
Year ended December 31, 2012			
Loss attributable to ordinary shareholders – Basic and diluted	(20,423)	286,709	(0.07)
Year ended December 31, 2011			
Loss attributable to ordinary shareholders – Basic and diluted	(26,939)	262,272	(0.10)

Basic loss per share is calculated by dividing the loss attributable to shareholders of the Company by the weighted average number of ordinary shares in issue during the year. Diluted per share information is calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares. Potential ordinary shares, including share options and warrants, are considered to be anti-dilutive and have therefore been excluded from the diluted per share calculation.

(tabular amounts in thousands of US dollars)

12 Intangible assets

	Other intangible asset	Exploration and evaluation assets	Total
	$'000	$'000	$'000
Year ended December 31, 2011			
Opening net book amount	4,560	12,332	16,892
Additions	-	12,737	12,737
Additions through acquisition of subsidiary (note 25)	-	75,096	75,096
Impairment charge	(2,695)	-	(2,695)
Unsuccessful exploration and evaluation expenditure	-	(1,807)	(1,807)
Amortisation charge	(264)	-	(264)
Closing net book amount	1,601	98,358	99,959
At December 31, 2011			
Cost	5,553	98,358	103,911
Accumulated amortisation	(3,952)	-	(3,952)
Net book amount	1,601	98,358	99,959
Year ended December 31, 2012			
Opening net book amount	1,601	98,358	99,959
Additions	-	8,712	8,712
Transfers to property. plant and equipment	-	(142)	(142)
Unsuccessful exploration and evaluation expenditure	-	(955)	(955)
Amortisation	(200)	-	(200)
Closing net book amount	1,401	105,973	107,374
At December 31, 2012			
Cost	5,553	105,973	111,526
Accumulated amortisation and impairment	(4,152)	-	(4,152)
Net book amount	1,401	105,973	107,374

Other intangible assets consist of the fair value of the licence relating to the Production Enhancement Contract ('PEC') for the North Urtabulak field. Amortisation is calculated using a unit-of-production basis over the estimated incremental production entitlement expected to be received over the life of the contract.

Additions through the acquisition of a subsidiary relate to the intangible assets acquired from SSEC (note 25), including a fair value uplift arising on acquisition of $8,784,664.

Borrowing costs of $723,649 (2011 – $333,033) have been capitalised within exploration and evaluation assets during the year. The effective weighted average interest rate of the relevant borrowings was 18% (2011 – 12%).

(tabular amounts in thousands of US dollars)

The effective interest rate is higher than the nominal rate due to the cost of associated warrants (Note 20.2) and royalties (Note 20.3).

For the year ended December 31, 2012 $664,203 (2011 - $520,595) was capitalised from staff costs and share-based payment expense.

Impairment loss

During 2012, due to the further decline in production from the North Urtabulak field, management assessed the recoverable amount of this cash-generating unit (CGU) which is a reportable segment “Uzbekistan”. The recoverable amount of the CGU was estimated based on its value in use. Based on the results of the assessment, the carrying amount of assets (Intangible: $1,400,275 and Property, plant and equipment: $3,827,560) was determined to be recoverable.

Key assumptions used in discounted cash flows projection calculations

The value in use calculation is based on assumptions in respect of projections of cash flows approved by management. The cash flow forecast covers the period until 2017.

- Management determined future production based on current production levels, planned workovers and decline rates;
- Sales price is assumed to be in line with inflation;
- 50% of operating costs have been re-allocated to the potential Chegara PEC in Uzbekistan and are assumed to increase in line with inflation of 2% per annum over the next five years;
- General and administrative costs have been reduced by 66% through re-allocation to the potential Chegara PEC in Uzbekistan and are projected to remain constant; and
- The estimate of value in use was determined using a post-tax discount rate of 10%. The discount rate is an estimate which is based on a range of current borrowing costs of Uzbekistan operations and the interest rate at which the Company raised original funds to purchase assets in Uzbekistan.

Sensitivity to changes in assumptions

Management identified two key assumptions for which there could reasonably be a possible change that could cause an additional impairment to be recognised. If production volume on projected new workover wells was to reduce by 10%, or if only 25% of the operating costs are re-allocated to the potential Chegara PEC, there would be no impairment.

During 2011, a similar exercise was undertaken with respect to the North Urtabulak field, the recoverable amount of the CGU was estimated based on its value in use. Based on the assessment, the carrying amount of assets was determined to be $8,982,793 higher than its recoverable amount, and an impairment loss was recognised (see below).

(tabular amounts in thousands of US dollars)

The impairment loss was allocated pro-rata to the individual assets constituting the CGU as follows:

In $'000	Original carrying amount	Loss in 2011	Carrying amount after impairment recognised
Intangible assets	4,296	(2,695)	1,601
Property, plant and equipment (see note 13)	10,765	(6,288)	4,477
	15,061	**(8,983)**	**6,078**

Key assumptions used in discounted cash flows projection calculations

The value in use calculation is based on assumptions in respect of projections of cash flows approved by management. The cash flow forecast covers the period until 2017.

- Management determined future production based on current production and decline rates and new production to be generated from workovers of 4 wells, using a water flooding technique.

- Sales price growth is assumed to be in line with inflation of 2.5% for the next six years in line with information obtained from external data of forecast growth rates in the Central Asia region.

- Operating costs per barrel in 2012 are based on management's budget and are assumed to increase in line with inflation for the next five years.

- General and administrative costs are projected to reduce in 2013 when it is expected that current project resources will be diverted to new licences in the country.

- The estimate of value in use was determined using a post-tax discount rate of 10%. The discount rate is an estimate which is based on a range of current borrowing costs of Uzbekistan operations and the interest rate at which the Company raised original funds to purchase assets in Uzbekistan.

Sensitivity to changes in assumptions

Management identified one key assumption for which there could reasonably be a possible change that could cause an additional impairment to be recognised. A 10% reduction in projected production volume per year would increase the total impairment calculation from $8,982,793 to $10,547,358. This would have increased the impairment of the intangible assets and property, plant and equipment by $469,370 and $1,095,195 respectively.

(tabular amounts in thousands of US dollars)

13 Property, plant and equipment

	Oil and gas properties $'000	Oil and gas equipment $'000	Vehicles $'000	Office and computer equipment $'000	Total $'000
Year ended December 31, 2011					
Opening net book amount	90,926	22,123	1,248	1,356	115,653
Additions	30,280	166	813	319	31,578
Additions through acquisition of subsidiary	1,693	-	99	76	1,868
Disposals	-	-	(432)	(218)	(650)
Impairment charge	(6,288)	-	-	-	(6,288)
Depreciation charge	(9,732)	(2,765)	(883)	(424)	(13,804)
Accumulated depreciation on disposal	-	-	408	153	561
Closing net book amount	106,879	19,524	1,253	1,262	128,918
At December 31, 2011					
Cost	133,322	25,337	2,260	1,978	162,897
Accumulated depreciation and impairment	(26,443)	(5,813)	(1,007)	(716)	(33,979)
Net book amount	106,879	19,524	1,253	1,262	128,918
Year ended December 31, 2012					
Opening net book amount	106,879	19,524	1,253	1,262	128,918
Additions	10,778	-	421	94	11,293
Transfers from intangible assets	143	-	-	-	143
Disposals	-	-	-	(1)	(1)
Depreciation	(16,633)	(1,139)	(1,070)	(415)	(19,257)
Accumulated depreciation on disposal	-	-	-	1	1
Closing net book amount	101,167	18,385	604	941	121,097
At December 31, 2012					
Cost	144,243	25,337	2,681	2,071	174,332
Accumulated depreciation and impairment	(43,076)	(6,952)	(2,077)	(1,130)	(53,235)
Net book amount	101,167	18,385	604	941	121,097
Asset under construction at net book amount included in above					
At December 31, 2012	27,202	-	-	-	27,202
At December 31, 2011	19,613	-	-	-	19,613

(tabular amounts in thousands of US dollars)

Assets under construction as at December 31, 2012 and December 31, 2011 includes the cost of developing the Akkulka oil concession and are not being depreciated until commencement of production.

During 2011, management assessed the recoverable amount of the North Urtabulak cash-generating unit (CGU) following a decline in production and recorded an impairment adjustment. Full details of the impairment test and sensitivities are disclosed in note 12.

Borrowing costs of $650,645 have been capitalised to oil and gas properties in the current year (2011 - $640,473). The effective weighted average interest rate of the relevant borrowing was 18%, (2011 - 12%). The effective interest rate is higher than the nominal rate due to the cost of associated warrants (note 20.2).

For the year ended December 31, 2012, $577,414 (2011 - $1,225,911) was capitalised from staff costs and share-based payment expense.

A net book value of assets included under “Oil and gas properties” amounting to $19,334,689 has been pledged by Tethys Aral Gas LLP (“TAG”) as security for the above-mentioned bank loan facility (note 20.1). The value of this guarantee has been assessed as nil.

14 Restricted Cash

Non Current

	December 31, 2012 $’000	**December 31, 2011 $’000**
Restricted cash	1,543	1,407

The above amounts consist of interest bearing bank deposits held in Kazakhstan. These deposits have been placed to satisfy local Kazakhstan requirements in respect of asset retirement obligations.

Current

	December 31, 2012 $’000	**December 31, 2011 $’000**
Restricted cash	477	885

The above amounts consist of monies placed on temporary deposit as a security against corporate credit cards and a deposit with the Ministry of Finance in Dubai as fixed term deposits with banks.

(tabular amounts in thousands of US dollars)

15 Trade and other receivables

	December 31, 2012 $'000	December 31, 2011 $'000
Other receivables - non-current		
Advances to construction contractors	362	1,140
Value added tax receivable	6,082	9,077
	6,444	10,217
Current		
Trade receivables	2,096	837
Prepayments	1,074	999
Other receivables	764	974
Value added tax receivable	3,769	2,668
	7,703	5,478

Current trade and other receivables are unsecured and non-interest bearing. Normal payment terms for the Company are 30 days. Prepayments primarily relate to prepaid insurance and other corporate operating expense items.

There are no trade receivables overdue past thirty days (December 31, 2011 – $nil). The other classes within trade and other receivables do not contain impaired assets.

Non-current advances to construction contractors relate to suppliers who were paid in advance for materials and services relating to both the Akkulka and the Kul-Bas contracts.

16 Loan receivable from jointly controlled entities

Joint Venture – Seven Stars Energy Corporation

As disclosed in note 24, on December 13, 2011, a wholly owned subsidiary of the Company increased its investment in the ordinary shares of SSEC, whereupon SSEC became a subsidiary and its assets and liabilities were consolidated into the Company's financial statements.

The Company has a loan receivable from SSEC, which up until the date of acquisition was net of the 51% share of loss of the joint venture as calculated using the equity method of accounting.

The following amounts represent the movements in the loan receivable from January 1 to December 13 2011, the date at which SSEC became a subsidiary. Following the increase in investment and the subsequent consolidation of SSEC into the Company's consolidated financial statements, the loan is eliminated on consolidation.

(tabular amounts in thousands of US dollars)

	December 13, 2011 $'000
Balance, beginning of year	35,460
Share of loss	(722)
Finance income on loan receivable	1,113
Movement in deferred gain	-
Increase in loan to jointly controlled entity	29,566
Removal of unrealised profit from SSEC	(5,706)
Loan balance pre-acquisition	59,711
Add back	
Investment as part of gain on disposal	5,706
Cumulative losses from jointly controlled entity	1,355
	66,772
Loss on settlement of pre-existing relationship	(24,423)
Settlement of pre-existing loan relationship	(42,349)
Balance, end of year	-

As with operating income (note 7), the Directors gave similar consideration to the position of interest on the loan to the jointly controlled entity, SSEC, with the result that cumulative interest income of $1,112,995 on the loan of $65,658,931 as at December 13, 2011 was recognised for the period from inception to December 13, 2011. Of this amount, $420,489 related to the year ended December 31, 2010. This change also has no effect on tax expense or cash flows.

Joint Venture – Aral Oil Terminal (Kazakhstan)

On February 16 2011, the Company signed a Joint Venture agreement with Olisol Investments Limited (note 17) to construct and operate a rail oil loading terminal in Kazakhstan through a separate jointly controlled legal entity, Aral Oil Terminal LLP "AOT". The terminal is used to deliver and sell oil for the Akkulka block. In conjunction with the Company's installation of oil production facilities at the Akkulka field to enable the processing of oil to refinery specification, the project at the Terminal will enhance operations by significantly reducing current trucking operations and enable production to be increased through the development of increased storage capacity and unloading/loading facilities.

The following amounts represent the movements in the loan receivable:

	Year ended December 31, 2012 $'000	December 31, 2011 $'000
Balance, beginning of year	2,013	-
Share of profit	191	-
Finance income on loan receivable (at market rate)	199	13
Increase in loan to jointly controlled entity	-	2,000
Balance, end of year	2,403	2,013

(tabular amounts in thousands of US dollars)

17 Investment in jointly controlled entity

As discussed in note 16, in 2011, the Company entered into a Joint Venture Agreement with Olisol Investments Limited under which it has a 50% interest in the jointly controlled entity, AOT. At December 31, 2011, investment in the joint venture was $1,112,899. The Company's interest is equity accounted, with its 50% share of profit or loss in the jointly controlled entity added to / offset against its investment.

Summary financial information for Aral Oil Terminal is as follows:

	December 31, 2012 $'000	December 31, 2011 $'000
Assets		
Non-current assets	10,033	3,898
Current assets	1,105	473
Total assets	11,138	4,371
Liabilities		
Trade and other payables	(10,747)	(4,448)
Total liabilities	(10,747)	(4,448)
Net assets / (liabilities)	391	(77)

	Year ended December 31, 2012 $'000	December 31, 2011 $'000
Revenue	3,243	-
Expenses	(2,630)	-
Profit before tax	613	-
Tax	(231)	-
Profit after tax	382	-
50% share of joint venture profit before tax	191	-

A net book value of assets included under "Non current assets" amounting to $4,282,419 has been pledged by the Joint Venture as security for the bank loan facility (note 20.1).

18 Inventories

	December 31, 2012 $'000	December 31, 2011 $'000
Raw materials	908	851
Refined product - Uzbekistan	1,138	1,076
Oil - Kazakhstan	-	98
	2,046	2,025

(tabular amounts in thousands of US dollars)

19 Cash and cash equivalents

	December 31, 2012 $'000	December 31, 2011 $'000
Cash at bank and in hand	1,750	7,281
Short-term deposits	-	3,465
	1,750	10,746

Cash at bank balances earn interest at floating rates based on daily bank deposit rates. Short term deposits are made for varying periods of between one day and three months, depending on the cash requirements of the Company, and earn interest at the respective short term deposit rates.

20 Financial liabilities

20.1 Borrowings

	Effective interest rate	Maturity date	December 31, 2012 $'000	December 31, 2011 $'000
Current				
New well loans – Uzbekistan	7% to 15.36% p.a.	2012	-	6,360
Rig loans – Option A	19.95% p.a.	2013	5,637	2,036
Rig loans – Option B	19.54% p.a.	2013	1,711	-
Kazakh loan	16.47% to 16.56% p.a.	2013	6,277	-
			13,625	8,396
Non-current				
Rig loans – Option B	19.54% p.a.	2013/2014	1,311	1,632
Kazakh loan	16.47% to 16.56% p.a.	2013/2016	2,377	-
			3,688	1,632
			17,313	10,028

New well loans – Uzbekistan

These were repaid in full during the first quarter of 2012.

Rig loans

In December 2011, the Company closed on the first tranche of a maximum $10 million loan facility amounting to US$3,965,240, which is secured by the ZJ70 and ZJ30 rigs and other equipment. This facility gives lenders the choice of two methods of repayment designated Option A and Option B.

(tabular amounts in thousands of US dollars)

The remaining two tranches of the $10 million facility (i.e. a total of $6,034,760) were closed during the first quarter of 2012.

Under Option A, which has a term of one year, lenders have the option to receive monthly repayments on an interest only basis followed by a single balloon repayment of the principal amount to be paid at the maturity date.

Option B, which has a term of two years, gives lenders the right to receive equal monthly instalments, incorporating interest and capital, together with a single balloon repayment of half of the principal amount to be paid at the maturity date.

These borrowings are held at amortized cost and their carrying amounts approximate to their fair value at the balance sheet date. The interest payable on the borrowed funds is 12% per annum under both options.

In addition, lenders were granted warrants to acquire ordinary shares of the borrower equal to half of each $100,000 principal amount of the loan advanced to the Company. As at December 31, 2012, a total of 5,000,000 warrants had been issued to lenders.

Such warrants will be exercisable at a 25% premium to the price of the volume weighted average CAD price of the shares on the TSX for the 5-day period prior to the day the borrower receives the funds in its bank account.

The Company has recorded a total discount to the $10 million loan in the amount of $1,011,213 based on the relative fair value of the warrants. The loan was then amortised using the effective rate interest method. Lenders have security over the shares of Imperial Oilfield Services Limited which has no other assets except the drilling rigs and associated equipment.

During December 2012, following the agreement of all loan holders, Tranche 1 Option A loan holders with loans maturing in December 2012 rolled over their loans for a further period of one year. The original loans were de-recognised and the new loans were recognised at fair value. The associated warrants were re-issued at an exercise price of CAD0.64. Furthermore extensions of warrant expiry dates were granted to all loan holders, except two officers of the company who were re-issued with warrants upon expiry of the original warrants. The difference between the carrying value of the old loan and the fair value of the new loan amounted to a loss of $232,898, which was recognised in the consolidated statement of comprehensive income.

Based on the borrowing rates currently available to the Company for long term borrowings with similar terms and average maturities (17.44%), the fair value of the financial borrowings approximate their carrying value in both current and comparative years.

Subsequent to the year end, there were further rollovers of the two tranches of loan closed in the first quarter of 2012 (see note 30).

(tabular amounts in thousands of US dollars)

Kazakh loan

On June 29, 2012 the Company announced that it had secured a loan facility from a Kazakh bank to fund capital expenditures in Kazakhstan (the "bank loan facility").

The bank loan facility was arranged by Eurasia Gas Group LLP, with the Company's consent, and is a bank loan to Eurasia Gas Group LLP, the Company's joint venture partner in Aral Oil Terminal LLP, whereby Eurasia Gas Group LLP draws down on the bank loan facility entirely at the direction and discretion of the Company and funds are transferred to the Company's subsidiary, TAG. The bank loan facility has a term of up to four years depending on the Company's requirements and bears an interest rate of between 12% and 15% per annum on sums drawn down.

A formal loan agreement was signed with Eurasia Gas Group LLP for 2.35 billion KZT with a drawdown period of one year from the date of first drawdown (May 31, 2012). Repayment and interest terms are agreed for each drawdown, upon drawdown.

As at December 31, 2012, 675 million KZT ($4,510,072) of funds had been advanced to the Company in relation to the loan agreement, with a repayment period over 4 years and monthly repayments of both principal and interest (at 16.1%). By December 31, 2012, 150 million KZT had been repaid. Of the total funds drawn, $3,393,220 is outstanding as at December 31, 2012, with $1,017,340 presented as current and $2,375,880 presented as non current liabilities.

During the last quarter of 2012, a further 810 million KZT ($5,385,620) was advanced by Eurasia Gas Group LLP, the formal terms of which had not been finalised by December 31, 2012, therefore the amount has been presented as a current liability in full.

In case oil production is suspended for more than 30 days, the outstanding amount is to be repaid to Eurasia Gas Group LLP within 30 days from the receipt of its notice of return.

Based on the borrowing rates currently available to the Company for long term borrowings with similar terms and average maturities (17.44%), the fair value of the financial borrowings approximate their carrying value.

Certain assets have been pledged by both TAG and AOT as security for the above-mentioned bank loan facility (note 13) which represents a financial guarantee to the Company. The value of this guarantee has been assessed as nil, primarily due to the credit worthiness of Eurasia Gas Group LLP.

20.2 Derivative financial instrument - warrants

	December 31, 2012 $'000	**December 31, 2011 $'000**
Balance, beginning of year	264	405
Issued during the year	778	233
Fair value loss on extension of warrants	233	-
Fair value gain	(752)	(374)
Balance, end of year	523	264

(tabular amounts in thousands of US dollars)

The warrant liability represents the financial liability relating to share warrants where the shares are denominated in a currency that is not the Company's functional currency. These warrants were issued in connection with the two rig loans described in note 20.1.

As the warrants are denominated in foreign currency, there is a written option for the holder to exchange the foreign currency denominated warrant for a fixed number of functional currency denominated shares. This option is a derivative financial instrument and was initially recognised at fair value and subsequently measured at fair value through profit and loss.

The fair value of the liability is estimated using the Black-Scholes pricing model using the following average assumptions:

	December 31, 2012	**December 31, 2011**
Weighted average fair value	$0.09	$0.10
Risk free rate	1.06%	0.92%
Expected term	1 year	1.11 years
Volatility	76.5%	56%
Dividend	Nil	Nil

The following table summarizes the warrant activity for the years ended December 31, 2012 and December 31, 2011.

	Number of warrants	**Weighted average exercise price $**
Outstanding at January 1, 2011	2,779,452	2.36
Granted	1,982,620	0.79
Expired	(2,141,154)	2.80
Outstanding at December 31, 2011	2,620,918	0.79
Exercisable at December 31, 2011	2,620,918	0.79
Outstanding at January 1, 2012	2,620,918	0.79
Granted	4,100,000	0.90
Expired	(945,918)	1.05
Outstanding at December 31, 2012	5,775,000	0.81
Exercisable at December 31, 2012	5,775,000	0.81

Of the warrants outstanding and exercisable at the end of the year, 307,620 relate to warrants granted to the Company's officers.

There are no performance conditions attached to the warrants and all the granted warrants were immediately vested. Warrants are equity settled share based payment transactions.

(tabular amounts in thousands of US dollars)

In estimating expected volatility, the Company considers the historical volatility of its own share price over the most recent period that is commensurate with the expected warrant term.

The following table lists the warrants outstanding at December 31, 2012 by exercise price.

Exercise price $	Warrants outstanding	Weighted average remaining term (in years)	Warrants exercisable	Weighted average remaining term (in years)
CAD1.18	25,000	0.70	25,000	0.70
CAD1.15	75,000	0.68	75,000	0.68
CAD1.14	576,551	1.49	576,551	1.49
CAD1.11	457,000	0.94	457,000	0.94
CAD1.09	273,829	1.54	273,829	1.54
CAD1.08	150,000	1.32	150,000	1.32
CAD0.95	75,000	0.65	75,000	0.65
CAD0.88	50,000	0.64	50,000	0.64
CAD0.86	40,000	0.64	40,000	0.64
CAD0.85	75,000	1.31	75,000	1.31
CAD0.84	1,220,000	0.87	1,220,000	0.87
CAD0.62	400,000	0.79	400,000	0.79
CAD0.61	200,000	0.42	200,000	0.42
CAD0.64	1,232,620	1.01	1,232,620	1.01
CAD0.65	325,000	0.44	325,000	0.44
CAD0.58	100,000	1.47	100,000	1.47
CAD0.59	500,000	1.46	500,000	1.46
	5,775,000	1.02	5,775,000	1.02

20.3 Derivative financial instruments - interest rate swap

The interest rate swap represents the derivative financial instrument entered into in connection with the Uzbekistan loan financing disclosed in note 20.1 completed in 2009. This instrument is a derivative financial instrument and was initially recognised at fair value and subsequently measured at fair value through profit and loss. The Company measured the fair value of the liability by applying a valuation technique based on the discounted estimated future net cash flows expected to be derived from the instrument. A discounted cash flow (DCF) method requires management to estimate future cash flows associated with the instrument and then discount those amounts to present value at a rate of return that considers the relative risk of the cash flows (5%). During 2010, a significant fluctuation occurred in the fair value of the interest rate swaps due to a significant decline in expected production from well NUR 116, which resulted in a fair value gain as disclosed below. The asset balance at the end of the year represents the saving in interest expense.

On October 19, 2009, the Company closed a loan financing for $4.1million with a group of investors in connection with the drilling of well NU116 in Uzbekistan. A coupon of 10% per annum was due

(tabular amounts in thousands of US dollars)

for the first two months, which was the expected drilling time of the well. Thereupon the lenders received a 6% per annum coupon and 6.25% of the revenue received by the Uzbekh entity (Baker Hughes Cyprus Limited) from sales of the net production from the new well for every $1 million invested, calculated monthly and payable quarterly in arrears over a period of up to 24 months. If the well did not produce, the investor received only the 6% per annum coupon on the funds invested. $1.05 million of this loan was repaid early to enable the lenders to participate in the new loan secured against drilling equipment. The royalty entitlement was identified as an embedded derivative and required to be separated from the loan note. Accordingly the royalty entitlement has been accounted for as a derivative financial instrument – interest rate swap.

On December 14, 2009 in connection with the drilling of the above well NU116 in Uzbekistan, the Company approved the issue of loan notes to a maximum value of $3 million at an issue rate of $0.88 per note and redemption value of $1, resulting in an effective rate of 6.5%. By December 31, 2009, $1m loan notes had been places with a further $2m placed in February 2010. A royalty of 11.25% is payable to the loan note holders calculated on sales of net production from the new well. The royalty entitlement was identified as an embedded derivative and required to be separated from the loan note. Accordingly the royalty entitlement has been accounted for as a derivative financial instrument – interest rate swap.

	December 31, 2012 $'000	**December 31, 2011 $'000**
Balance, beginning of year	630	1,472
Fair value (loss)	(630)	(842)
Balance, end of year	-	630

The interest rate swap expired in 2012 upon repayment of the loan.

20.4 Derivative financial instruments – foreign currency hedge contracts

On May 12, 2011 the Company took out foreign currency hedge contracts to hedge exposure to the USD/GBP exchange rate. The contracts were in the form of a put option to sell US dollars with a strike price of $1.6495, with a clause that if a barrier level in the foreign currency exchange rate of $1.5675 was breached on the date of expiry, the option converted to a forward contract at the strike price of $1.6495. The fair value of the foreign currency contract was calculated using a valuation technique based on observable market inputs. Should the foreign currency exchange rate on the date of expiry be above the barrier of $1.5675 then no settlement would be required. Should the USD/GBP foreign currency rate be above $1.6495 then the options could be exercised at a gain to the Company.

This arrangement expired at the end of April 2012.

(tabular amounts in thousands of US dollars)

20.5 Finance costs / (income)

The net finance cost / (income) comprises:

	Year ended December 31, 2012 $'000	**Year ended December 31, 2011 $'000**
Finance costs	1,289	149
Finance income	(206)	(1,249)
	1,083	(1,100)

21 Trade and other payables

	December 31, 2012 $'000	**December 31, 2011 $'000**
Current		
Trade payables	4,487	6,065
Accruals	2,586	3,002
Other creditors	1,158	1,112
	8,231	10,179
Non-current		
Other non-current payables	351	547

Trade payables are non-interest bearing and are normally settled on 30 day terms. Accruals represent mainly fees outstanding to the drilling contractor in Uzbekistan and professional fees. Other current creditors consist mainly of local taxes in the Republic of Kazakhstan and the current portion of the Kyzyloi historical costs.

Included within other non-current payables are accruals for non-interest bearing historical costs due to the Government of Kazakhstan on the Kyzyloi and Akkulka contracts in Kazakhstan.

Kyzyloi

The principal amount of the historical cost liability outstanding at December 31, 2012 was $216,220 (2011 –$389,916) and this is to be repaid in quarterly instalments by March 2014. The liability is measured at amortised cost using the effective interest rate method, using an assumed market rate of interest (10%) on initial recognition. The carrying value of the liability is $200,904 (2011 – $344,692) of which $158,715 (2011 – $143,788) is current. Based on the borrowing rates currently available to the Company for loans with similar terms and average maturities (17.44%), the fair value of the liability approximates its carrying value (2011 – approximated carrying value).

(tabular amounts in thousands of US dollars)

Akkulka

Upon signature of the Akkulka gas production contract on December 23, 2009, the historical cost liability in relation to this field became due. The principal amount of the historical cost liability outstanding at December 31, 2012 was $602,797 (2011: $713,197) and this is to be repaid in quarterly instalments by June 2018. The liability is measured at amortised cost using the effective interest rate method, using an assumed market rate of interest (22%) on initial recognition. The carrying value of the liability is $345,940 (2011: $375,990) of which $37,228 (2011: $30,051) is current.

Based on the borrowing rates currently available to the Company for loans with similar terms and average maturities (17.44%), the fair value of the liability approximates its carrying value (2011 - approximated carrying value).

22 Asset retirement obligations

	Year ended	
	December 31, 2012 $'000	**December 31, 2011 $'000**
At January 1	386	192
Additional obligations incurred	10	21
Additional obligations through acquisition of subsidiary	-	89
Change in estimated cash flow	131	63
Liabilities settled	(25)	-
Unwinding of discount due to passage of time	22	21
	524	386

The Company makes provision for the future cost of decommissioning oil and gas production facilities and pipelines on a discounted basis. These costs are expected to be incurred between 2013 and 2023. The provision has been estimated using existing technology at current prices, escalated at 5.4% (2011 – 5.4%) and discounted at 7.4% (2011 – 7.4%). The economic life and the timing of the asset retirement obligation are dependent on Government legislation, commodity prices and the future production profiles of the project. In addition, the estimated cash outflows are subject to inflationary and/or deflationary pressures in the cost of third party service provision. The undiscounted amount of liability at December 31, 2012 is $764,351 (2011 - $472,281).

(tabular amounts in thousands of US dollars)

23 Capital and reserves

Share capital and share premium

	Number	December 31, 2012 Number	December 31, 2011 Number
Authorized			
Ordinary shares with a par value of $0.10 each		700,000,000	700,000,000
Preference shares with a par value of $0.10 each		50,000,000	50,000,000

Ordinary equity share capital Allotted and fully paid	**Number**	**Share capital $'000**	**Share Premium $'000**
At January 1, 2011	260,629,769	26,063	297,222
Issued during the year for cash	26,062,975	2,606	9,503
At December 31, 2011	286,692,744	28,669	306,725
At January 1, 2012	286,692,744	28,669	306,725
Issued during the year in connection with the exercise of share options	15,000	2	11
Cost of share issue	-	-	(11)
At December 31, 2012	286,707,744	28,671	306,725

As at December 31 2012, a total of 34,388,129 (December 31, 2011 – 31,115,572) ordinary shares are reserved under the Company's Long Term Stock Incentive Plan and Warrants granted by the Company. Details of the options and warrants are given in note 9.

The preference shares have the rights as set out in the Memorandum and Articles of Association approved at the AGM on April 24, 2008. Significant terms related to preference shares are summarised below:

- May be issued in one or more series;
- Are entitled to any dividends in priority to the ordinary shares;
- Confer upon the holders thereof rights in a winding-up priority to the ordinary shares;

(tabular amounts in thousands of US dollars)

- And may have such other rights, privileges and conditions (including voting rights) as the Board may determine prior to the first allotment of any series of preference shares, provided that if a series of preference shares has no or limited voting rights it shall be designated as such by the Board.

There are currently no preference shares outstanding (2011 – None).

On December 9, 2011, the Company completed a private placement of 26,062,975 Ordinary Shares for gross proceeds of $13,001,981. The net proceeds of the Offering were to enable Tethys to purchase an additional 34% of shares in SSEC and to carry out additional work on the Beshtentak oilfield in Tajikistan.

Other reserves

Other reserves comprise of option reserves and warrant reserves as set out in the Statement of Changes in Equity. The Option and Warrant Reserves relate to stock options and warrants issued to employees under the Long Term Incentive Plan, details of which are discussed in note 9.

24 Non-controlling interest

As a result of the transaction described in note 25 whereby the Company increased its interest from 51% to 85%, thereby gaining overall control of SSEC, a 15% non-controlling interest has arisen as follows:

	December 31, 2012 $'000	**December 31, 2011 $'000**
Balance at December 31/ December 13, 2011	8,918	-
Fair value of identifiable net assets	-	4,888
Fair value uplift arising from debt waiver	-	4,080
Share of loss for the year / period	(481)	(50)
Balance at December 31, 2012	8,437	8,918

25 Acquisition of subsidiary

Acquisition

On December 13, 2011, the Company obtained control of SSEC by acquiring a further 34% of the shares and voting interests in the company. As a result, the Company's equity interest in SSEC increased from 51% to 85%.

Increased control in SSEC provided the Company with an 85% stake in prospective resources together with increased benefits arising from the Production Sharing Contract.

(tabular amounts in thousands of US dollars)

Between the date of acquisition and the balance sheet date, SSEC contributed $55,430 to Company revenue and a loss of $336,549 for the period. If the acquisition of SSEC had been completed on the first day of the financial year, Company revenues for the period would have increased by $513,135 and the Company loss would have been increased by $693,721. In determining these amounts, management has assumed that the fair value adjustments, determined provisionally, that arose on the date of acquisition would have been the same if the acquisition had occurred on January 1, 2011.

The following summarises the major classes of consideration transferred, and the recognised amounts of assets acquired and liabilities assumed at the acquisition date.

Consideration transferred

	Fair value $'000
Consideration at December 13, 2011	
Cash consideration	7,000
Non cash consideration	4,080
	11,080

Non cash consideration

At the time of acquisition, SSEC owed the Company $66,772,000 with respect to a loan (note 16). As part of the arrangement to increase the Company's interest in SSEC, it was agreed to waive an amount of $49,920,000 with respect to the loan between SSEC and the Company. The fair value of the joint venture partner's benefit from the loan waiver is the fair value of 15% of the amount waived, representing the future benefit that the joint venture partner will now receive from future distributions by SSEC. The Company involved an independent external expert to fair value 15% of the amount of $49,920,000 that was waived. The fair value of the 15% loan waiver was calculated as $4,080,000. This was estimated by applying the Tajik specific weighted average cost of capital of 16.39% to the loan repayments based on anticipated future cashflows.

Recognised amounts of identifiable assets acquired and liabilities assumed

	Fair value $'000
Cash and cash equivalents	215
Intangible assets	75,096
Property, plant and equipment	1,868
Inventory	1
Current trade and other payables	(2,151)
Provision for asset retirement obligation	(89)
	74,940

The following fair values had been determined on a provisional basis at the date of acquisition:

- The fair value of intangible assets (SSEC's exploration assets) has been determined provisionally, with the assistance of independent valuation experts.

(tabular amounts in thousands of US dollars)

- SSEC's operations are subject to environmental regulations. The Company has conducted an assessment of site restoration provisions arising from these regulations and has recognised a provisional amount in its initial accounting. However, the Company will continue its review of these matters during the measurement period.

  At December 31, 2012, there has been no new information about facts and circumstances that existed at the acquisition date that would necessitate any adjustment to the above amounts.

Settlement of pre-existing relationship

At the time of acquisition, SSEC owed the Company $66,772,000 with respect to a loan (note 16). As per IFRS 3.B52, at the acquisition date this pre-existing loan relationship was effectively terminated as part of the acquisition. The fair value of the loan at the acquisition date was $42,349,176. The difference of $24,422,750 between the book value and the fair value was as a result of the below market interest rate charged on the loan. The loss was recognised as a fair value loss on the pre-existing loan relationship in the consolidated financial statements of the Company.

	Fair value $'000
Cash consideration transferred	7,000
Fair value of loan relationship terminated	42,351
Non cash consideration	4,080
Total consideration	53,431
Non-controlling interest, based on their proportionate interest in the recognised amounts of the asset and liabilities of SSEC	4,888
Fair value of pre-existing interest in SSEC	16,621
Fair value of identifiable net assets	(74,940)
Goodwill	nil

Gain on disposal

The remeasurement to fair value of the Group's existing 51% interest in SSEC resulted in a gain as follows:

	December 13, 2011
	$'000
Fair value of 51% in SSEC at December 13, 2011	16,621
Carrying value of investment	10,760
Gain on previously held interest in SSEC	27,381

The fair value of the 51% investment in SSEC at December 13, 2011 is based on the fair value of net identifiable assets at December 13, 2011, after deduction of the fair value of the loan relationship terminated between the Company and SSEC. This gain has been recognised in the consolidated statement of comprehensive income.

(tabular amounts in thousands of US dollars)

Cost of investment

	December 13, 2011
	$'000
Deferred gain	(3,699)
Unrealised profit on other operating income from SSEC	(5,706)
Cumulative losses from SSEC	(1,355)
Carrying value of investment	(10,760)

The Company had deferred a gain of $3,699,000 on the disposal of its three Tajik subsidiaries to SSEC. As such this forms part of the net investment in SSEC and is included within the carrying value of the investment. This is presented gross in the 2010 Statement of Financial Position.

During 2010 and 2011, a drilling rig together with associated equipment, all owned by the Company, was rented to a subsidiary of SSEC on commercial terms. In accordance with the shareholder's agreement, the amounts receivable in respect of the rental are to be added to the loan due from that entity. When preparing the 2010 annual financial statements and the interim financial statements for Q1 2011, these amounts were eliminated in full rather than proportionate to the Company's equity accounted interest and no income was recognised. Following progress made on the EOL09 well, as set out in more detail on page 13 of the Management's Discussion and Analysis document, the directors reconsidered this matter at June 30, 2011 and considered it appropriate that the income be included for the period to December 13, 2011 – the date that SSEC became a subsidiary (note 16.)

Accordingly, other operating income for the period to December 13, 2011 includes $7,374,090 in respect of these transactions, of which $3,835,320 relates to the year ended December 31, 2010. The invoices have not been settled and there is consequently no impact on the Company's cash flows. There is also no impact on tax expense as a result of this income being recognised.

Per IAS 31 'Interests in Joint Ventures', profits on transactions with jointly controlled entities are eliminated to the extent of the investor's interest in the jointly controlled entity. Accordingly the Company eliminated $5,705,910 against the carrying value of its investment in SSEC.

As per the Production Sharing Contract ('PSC') signed on June 13, 2008, between Kulob Petroleum Limited, a subsidiary of Tethys Petroleum Limited, and the Ministry of Energy and Industry of the Republic of Tajikistan, Kulob Petroleum Limited is not liable for any tax arising on its operations in Tajikistan which are associated with the PSC. Consequently there is no tax impact from this transaction.

There were no further acquisitions during 2012.

(tabular amounts in thousands of US dollars)

26 Related party transactions

All subsidiaries, as listed below, have been consolidated into these consolidated financial statements A list of the investments in subsidiary undertakings (all of whose operations comprise Exploration, Development, Production, Service or Holding Companies in one class of business – Oil and Gas), including the name, proportion of ownership interest, country of operation and country of registration, is given below.

Subsidiaries	Percentage	Country of registration	Country of operation
Tethys Kazakhstan SPRL	100%	Belgium	Belgium
Transcontinental Oil Transportation SPRL	100%	Belgium	Belgium
Amu Darya Petroleum Limited	100%	BVI	BVI
Pamir Logistics Company Limited	100%	BVI	Tajikistan
Tethys Services Guernsey Limited	100%	Guernsey	Guernsey
Tethys Uzbekistan Limited	100%	Cayman Islands	Uzbekistan
Karakalpak Oil & Gas Limited	100%	Cayman Islands	Uzbekistan
Chegara Production Limited	100%	Cayman Islands	Uzbekistan
TransOxiana Petroleum Limited	100%	Cayman Islands	Cayman Islands
Tethys Afghanistan Holdings Limited	100%	Cayman Islands	Dormant
Bactria Petroleum Limited	100%	Cayman Islands	Cayman Islands
Tethys Production Uzbekistan Limited	100%	Cayman Islands	Uzbekistan
Tethys Tajikistan Limited	100%	Cayman Islands	Tajikistan
Imperial Oilfield Services Limited	100%	Cayman Islands	Cayman Islands
Tethyda Limited	100%	Cyprus	Dormant
Baker Hughes (Cyprus) Limited (t/a Tethys Production Uzbekistan Limited)	100%	Cyprus	Uzbekistan
Tethys Aral Gas LLP	100%	Kazakhstan	Kazakhstan
Kul-Bas LLP	100%	Kazakhstan	Kazakhstan
Tethys Munai Gaz LLP	100%	Kazakhstan	Dormant
Tethys Services Kazakhstan LLP	100%	Kazakhstan	Kazakhstan
AOE Tykhe SA	100%	Luxembourg	Dormant
Asia Oilfield Equipment BV	100%	Netherlands	Tajikistan
AOE Telesto BV	100%	Netherlands	Dormant
Tethys Uzbekistan BV	100%	Netherlands	Netherlands
Tethys Services Limited	100%	United Kingdom	United Kingdom
Tethys Petroleum Incorporated	100%	USA	USA
Tethys Afghanistan Incorporated	100%	USA	Dormant
Seven Stars Energy Corporation	85%	BVI	Tajikistan
Seven Stars Petroleum Products Limited	85%	BVI	Tajikistan
Sogdiana Petroleum Limited	85%	Cayman Islands	Tajikistan
Kulob Petroleum Limited	85%	Cayman Islands	Tajikistan
Tethys Services Tajikistan Limited	85%	Tajikistan	Tajikistan
Jointly controlled entities			
Aral Oil Terminal	50%	Kazakhstan	Kazakhstan

(tabular amounts in thousands of US dollars)

Vazon Energy Limited

Vazon Energy Limited ("Vazon") is a corporation organized under the laws of the Bailiwick of Guernsey, of which Dr. David Robson, Executive Chairman and President, is the sole owner and managing director.

Tethys has a management services contract with Vazon that came into effect from June 27, 2007 whereby the services of Dr. Robson and other Vazon employees are provided to the Company. The total cost charged to Tethys for services from Vazon in the year ended December 31, 2012 was $2,432,239 (2011 – $3,295,754). As at the date of these consolidated financial statements, the services of Dr. Robson and only two other Vazon employees are provided to the Company. The remainder of the employees previously employed by Vazon have been transferred to Tethys Services Guernsey Limited.

On June 13, 2012, the Company and Vazon amended the Deed of Guarantee and Indemnity dated December 10, 2009, between the two companies, whereby the Company guarantees to indemnify Vazon for certain payments related to the management services provided by Vazon under the management services contract.

The guarantee comprises a charge over the assets of one of the Company's subsidiaries, Tethys Tajikistan Limited ("TTL), equalling amounts owing under the management services contract from time to time. At December 31, 2012, the amount owed to Vazon by the Company was $438.

Oilfield Production Consultants Limited

Oilfield Production Consultants (OPC) Limited and Oilfield Production Consultants (OPC) USA LLC have one common director with the Company. Total fees for the year ended December 31, 2012 were $66,150 (2011 – $11,422). OPC participated in the 2011 loan financing described in note 20, advancing $200,000 under Option B of the facility. As a result, OPC received 100,000 warrants valued at a fair value of $15,030. The loan was advanced under the same conditions and terms afforded to non-related parties. As a result of agreeing to the rollover, discussed in note 20, the term of the warrants was extended which did not result in any change in fair value.

Related party transactions with key management personnel

Two officers of the Company participated in the 2011 loan financing described in note 20 for which they received 75,000 and 232,620 warrants at a fair value of $6,143 and $21,983 respectively. Loans advanced were $150,000 and GBP300,000 respectively and were rolled over upon maturity of their one year term for a further term of one year under the same conditions and terms afforded to non-related parties, except that the warrants originally issued were not extended. Upon rollover, there was a re-issue of 75,000 and 232,620 warrants were issued at a fair value of $2,940 and $25,891 respectively.

On July 6, 2012, Ambassador Khalilzad was appointed a director of the Company. His company, Khalilzad Associates provides consultancy services with respect to business development. Total fees for these services amounted to $154,078 for the year ended December 2012.

(tabular amounts in thousands of US dollars)

Dr. David Robson has a close family member employed by the Company on standard terms and conditions.

During the year, an interest bearing loan of GBP32,278 was advanced to a Board Director at an interest rate of 3%. As at December 31, 2012 the loan remained unpaid.

Two further non-interest bearing loans of $50,960 and $76,251 were advanced to two officers during the year (2011 - $51,374 to one officer). Balances outstanding at the year end were $21,368 and $50,682 respectively (2011 - $9,531).

Remuneration of key management personnel

The remuneration of the key management personnel of the Company is set out below in aggregate.

	Year ended December 31, 2012 $'000	Year ended December 31, 2011 $'000
Salaries and short-term employee benefits	4,914	4,273
Share-based payments	2,329	3,799
	7,243	8,072

Two officers of the Company participated in the 2011 loan financing described in note 20 for which they received 75,000 and 232,620 warrants valued at a fair value of $6,143 and $21,983 respectively. Loans advanced were USD150,000 and GBP300,000 respectively for a one year term under the same conditions and terms disclosed in note 20.1 afforded to external parties.

During December 2012, these loans were rolled over upon maturity, whereupon the same number of warrants were re-issued at a fair value of $2,940 and $25,891 respectively.

Transactions with affiliates or other related parties including management of affiliates are recorded at their exchange amount.

Related party transactions with SSEC are disclosed in note 7 – Other Operating Income.

27 Changes in working capital

	Year ended December 31, 2012 $'000	Year ended December 31, 2011 $'000
Trade and other receivables	(2,225)	(1,798)
Inventories	(21)	96
Trade and other payables	(1,948)	1,391
Change in non-cash working capital	(4,194)	(311)
Non-cash transactions	73	329
Net changes in non-cash working capital	(4,121)	18

(tabular amounts in thousands of US dollars)

In 2011, the principal non-cash transaction is related to the issue of shares as consideration for the acquisition discussed in note 23.

Net changes in non-cash working capital are categorized as follows:

	Year ended December 31, 2012 $'000	December 31, 2011 $'000
Operating activities	(1,842)	(664)
Investing activities	(2,279)	682
Balance	(4,121)	18

28 Commitments and contingences

Kazakhstan

Akkulka Production Contract

On December 23, 2009, TAG and MEMR signed the Akkulka Production Contract giving TAG exclusive rights to produce gas from the Akkulka Block for a period of nine years. Contingent upon commencement of commercial production on the Akkulka contractual territory, an amount of $2,698,531 will be due to the Kazakhstan Government as a reimbursement of historical costs previously incurred by the Government in relation to the contractual territory, payable upon signature of the Akkulka oil production contract. A work program commitment for 2012 has been agreed at $2,718,000 against which payments of $1,575,267 have been made to date.

Kyzyloi Production Contract

On August 9, 2012 a work program commitment for 2012 was agreed at $2,930,900 against which payments of $2,229,079 have been made to date. A work program for 2013 has also been agreed at $2,519,000.

Akkulka Exploration Contract

On August 9, 2012 a work program commitment for 2012 was agreed at $12,025,000 against which payments of $15,625,753 have been made to date. Work programs for 2013 to end of March 2015 have been agreed totalling $19,142,000.

Kul-Bas Exploration and Production Contract

The Kazakhstan Government is to be compensated for the historical costs related to the contractual territory in the amount of $3,275,780. The Company has previously paid an amount of $49,137 in relation to this balance. If and when commercial production commences, $88,666 is due in quarterly

(tabular amounts in thousands of US dollars)

instalments until the remaining historical costs of $3,226,643 have been paid in full. With respect to 2012, a minimum work program amounting to $1,780,000 has been agreed, of which $839,863 has been paid during the year. On September 5, 2012 a further work program for 2013 was agreed at $4,200,000.

29 Operating leases

Leases as a lessee:

Operating leases consist primarily of leases for offices. Lease commitments are as follows:

December 31, 2012	**Total $'000**	**Less than 1 year $'000**	**1 – 3 years $'000**	**Greater than 3 years $'000**
Operating leases	1,612	913	407	292

2012 expenditure on lease commitments included in the consolidated statement of comprehensive income amounted to $1,331,186.

December 31, 2011	**Total $'000**	**Less than 1 year $'000**	**1 – 3 years $'000**	**Greater than 3 years $'000**
Operating leases	1,055	670	290	95

2011 expenditure on lease commitments included in the consolidated statement of comprehensive income amounted to $920,117.

30 Subsequent events

Kazakh loan

In January 2013, the Kazakh loan arrangement discussed in note 20 was terminated and replaced by way of an arrangement whereby funds are advanced to the Company and repaid as a deduction against oil revenue. Terms of the arrangement are principally the same (i.e. repayment is over four years with monthly repayments of both principal and interest) and therefore under IFRS, the amounts advanced will continue to be treated as a loan.

Gas sales contract

On January 31, 2013, the Company announced that it had effectively doubled the net price of the gas that it is selling in Kazakhstan. Two gas supply contracts have been signed by TAG with Intergas Central Asia JSC, a wholly owned subsidiary of the Kazakh State company KazTransGas JSC, for the Kyzyloi and Akkulka natural gas fields. The contracts are for annual volumes up to 150 million cubic metres at an increased net price of USD65 per 1,000 cubic metres (or USD1.84 per 1,000 cubic feet) of gas (USD72.8 per 1,000 cubic metres or USD2.06 per 1,000 cubic feet including VAT) net of marketing and distribution costs, and run through to December 31, 2013.

Extension of Kul-Bas Exploration and Production Contract

On February 28, 2013, the Company announced it had extended the exploration period for the Kul-Bas Exploration and Production Contract by a further two years until November 11, 2015. The Kul-Bas contract area surrounds the Akkulka contract area which contains the Company's producing oil and gas fields. This extension gives further time to explore this attractive area, which has several prospects and leads.

Rig loan rollover

With respect to the rig loans discussed in note 20, one year loans amounting to $6,034,760 from lenders who elected for Option A in February and March 2012 have been successfully rolled over in 2013 for a further twelve months. A total of 1,811,051 associated warrants were re-issued at exercise prices of CAD0.92 and CAD0.71. Furthermore extensions of warrant expiry dates were granted to all loan holders, except two officers of the company who were re-issued with warrants upon expiry of the original warrants, as discussed in notes 2 and 20.