

**PETSEC ENERGY LTD**  
Annual Report 2017

**HUMMER  
DEVELOPMENT  
COMMENCES  
PRODUCTION**

Offshore Louisiana  
Federal Waters USA



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## Annual General Meeting

To be held at: 11 a.m. (AEST) on Thursday, 17 May 2018, at the Museum of Sydney, corner of Bridge and Phillip Streets, Sydney.

## Capital Structure

At 20 February 2018

### Australia

Exchange	ASX
Ticker	PSA
Shares on issue	322.3 million
Share price	A\$0.11
Market capitalisation	A\$35.5 million

### USA


Exchange	OTC Pink Sheets
Ticker	PSJEY

### Petsec Energy Ltd ABN 92 000 602 700

The Company is listed on the Australian Stock Exchange (symbol: PSA) and traded over the counter in the USA as American Depositary Receipts (ADRs) (symbol: PSJEY). Its corporate office is in Sydney, Australia, its USA operations offices are in Houston, Texas and Lafayette, Louisiana, its Middle East and North Africa (MENA) operations offices are in Dubai, United Arab Emirates (UAE) and Sana'a, Yemen.





A photograph of an offshore oil and gas production platform at sea. The platform is a complex structure of pipes, valves, and metal frameworks, extending from the water's surface. The water is a deep blue, and the sky is a lighter blue. The platform is illuminated by warm, yellow lights, creating a strong contrast with the cool blue tones of the water and sky. The image is framed by a large, semi-transparent blue circle that overlaps the top and right sides of the page.

Petsec Energy's corporate objective is to increase shareholder value by increasing the net asset value of the Company through successful oil and gas exploration, development, and production...

Image: Main Pass 270/273/274  
Hummer Project: Main Pass 270  
"B" production platform



# Corporate Objective and Strategy

## Objective

Petsec Energy's corporate objective is to increase shareholder value by increasing the net asset value of the Company through successful oil and gas exploration, development, and production, thereby building Petsec Energy into a significant mid-tier oil and gas exploration and production company, respected in the industry for its technical skills, timely and cost effective delivery of projects, and the integrity with which it conducts its business.

## Strategy

The Company's strategy to meet its corporate objective is to maximise the value of its current reserves, pursue participation in high quality, high impact exploration drilling opportunities, and to acquire leases with undeveloped or producing oil and gas reserves, which also hold significant development and exploration potential.

Historically the strategic and geographical focus has been predominately in Louisiana, USA. This focus shifted in 2014 to include oil reserve acquisitions in the MENA region. In the Republic of Yemen, the Company holds two leases: one with undeveloped oil resources and substantial exploration potential; and the second a production licence over five sizeable oil and gas discoveries, one of which is developed (An Nagyah) and was in production until late in February 2014. The Company will continue to identify and pursue additional developed and undeveloped reserves within the MENA region.

In the Republic of Yemen, the Company holds two leases: one with undeveloped oil resources and substantial exploration potential; and the second a production licence over five sizeable oil and gas discoveries.



Image: Mystic Bayou Field: Barge drill rig next to production and oil storage facilities

## Company Profile and History

Petsec Energy Ltd (the “Company”) is an independent oil and gas exploration and production company listed on the Australian Stock Exchange (symbol: PSA) and traded over the counter in the USA in the form of American Depositary Receipts (symbol: PSJEY).

The Company was established on 7th December 1967 and its registered Australian Company Number is: 000 602 700.

The Company through its wholly owned subsidiary companies Petsec Energy Inc. and Petsec Exploration and Production LLC has operations in the shallow waters of the Gulf of Mexico and onshore Louisiana, USA. The Company also owns interests onshore in the Republic of Yemen through its wholly owned subsidiary Petsec Energy (Middle Eastern) Limited.

The Company has been active in the USA since 1989 and has explored offshore in the Gulf of Mexico and onshore in Louisiana, and Texas. The Company has drilled over 100 wells in the USA and has enjoyed a success rate of 74%.

From 2002 to 2011, the Company was active in the Beibu Gulf, China, participating in the drilling of seven exploration wells resulting in three oil fields being discovered. The fields were sold in 2011.

In 2014, the Company determined that it wished to pursue both an exploration and an oil reserves acquisitions strategy. Following a strategic review, the Company identified the Middle East & North African (MENA) region as a growth area for the Company where licences with producing oil reserves or near development reserves, with associated high exploration potential, can be acquired at lower prices than those in the USA. In 2015, a non-operated interest in a large licence (Block 7) area was acquired in Yemen, which held a potentially large undeveloped

oilfield discovery and a number of drill prospects which held potentially very large oil reserves ranging up to 900 million barrels of oil. In early 2016, the Company acquired another licence Damis (Block S1) in Yemen, which held five oil and gas fields of which one field, the An Nagyah Oilfield had been developed and was producing until political unrest in 2014 caused it to be shut-in. Petsec has continued to negotiate for additional interests in these licenses and now has agreements to acquire and operate 100% interest in both blocks.

The Company’s corporate office is in Sydney, Australia and the Company’s operational offices are located in Houston, Texas, Lafayette, Louisiana, USA, in Dubai, UAE, and Sana’a, Yemen.



USA net 2P oil and gas reserves as of 1 January 2018 were 15.9 Bcf of gas and 1.137 MMbbl of oil (equivalent to 3.8 MMboe) with an NPV<sub>10</sub> value of US\$34.8 million.

## 2017 Year in Review

### Corporate

- Completion of the non-renounceable rights issue announced on 24 November 2016, raising A\$11 million at A\$0.15 per share, by the placement of 20 million shortfall shares at A\$0.15 per share pursuant to the underwriting agreement.
- Redemption date extended from 5 July 2018 to 23 January 2019 on US\$15 million secured convertible note facility.
- Restructure of the Company's USA Management and reduction in operational staff.

### Operations

#### USA: Development

**Hummer Gas/Oil Field, Gulf of Mexico, Main Pass 270/273/274, 50 miles South of the mouth of the Mississippi River**

Petsec: 12.5% working interest (net revenue interest: 10.26354%) + ORRI: 0.00441%

Main Pass Block 270 B-1, Hummer discovery well in the shallow waters of the Gulf of Mexico, brought into production:

- The Hummer Gas/Oil Field was discovered by the Main Pass Block 270 B-1 (previously Main Pass 270 #3) well in late 2015.
- A 4 pile jacket was fabricated and installed during summer 2016 and the well was successfully tested at rates exceeding

20 MMcfpd and 400 bopd during November 2016. The well was then suspended pending construction of the deck, production facilities and pipelines.

- A turnkey contract was awarded in January 2017 for the design, engineering, modification, fabrication and installation of the deck and production facilities, with initial capacity of 50 MMcfpd and 1,000 bopd capacity to accommodate the B-1 well, and for the planning, installation and hook-up of the pipelines connecting the platform to gas and oil sales pipelines.
- Installation of the Main Pass 270 "B" platform deck facilities and pipeline hook-up was completed during the first half of November 2017.
- The well was brought into production on 21 November 2017, and is currently producing at 17 MMcfpd and 340 bopd on a restricted choke.

#### Production

The Company holds an interest in three producing fields - the Jeanerette and Mystic Bayou Fields, onshore Louisiana, and the Hummer Gas/Oil Field offshore Gulf of Mexico, USA.

- Production for the year of 347 MMcfe was attributable to the Mystic Bayou Field and the Hummer Gas/Oil Field, which commenced production in late November 2017.
- USA net 2P oil and gas reserves as of 1 January 2018 were 15.9 Bcf of gas and 1.137 MMbbl of oil (equivalent to 3.8 MMboe) with an NPV<sub>10</sub> value of US\$34.8 million (Cawley, Gillespie & Associates).

#### MENA

**Block 7, Al Barqa Permit, Yemen**  
Petsec: 35% working interest (29.75% participating interest)

- The Company acquired an initial 35% working interest in 2015 and subsequently entered into agreements to acquire the remaining 65% working interest pending customary approvals from the Yemen Government.
- The block of 5,000 square kilometres (1,235,527 acres) contains the undeveloped Al Meashar oil discovery made in 2010 which holds target resources of 11 MMbbl to 50 MMbbl of oil. The two discovery wells, on limited production test flowed at 200 to 1,000 bopd. The block also contains an inventory of eight leads and prospects, holding mapped target sizes ranging from 2 MMbbl to 900 MMbbl, which are defined by 2D and 3D seismic surveys.



Images: Main Pass 270/273/274 Hummer Project: Main Pass 270 "B" production platform



**Damis (Block S-1) Production Licence, Yemen****Petsec: 100% working interest (82.5% participating interest)**

- The block of 1,152 square kilometres (284,665 acres), located in the Marib/Shabwah Oil Basin, was acquired by the Company in early 2016.
- The block contains five sizeable oil and gas discoveries including the developed/productive An Nagyah Oilfield complete with surface facilities to process and transport 20,000 bopd. The An Nagyah Oilfield commenced production in 2005 with an estimated 50 MMbbls of which half remains. The field has been shut-in since 2014 due to the political situation in the country.
- The An Nagyah Oilfield was estimated by DeGolyer and MacNaughton's reserve engineers, using the proposed trucking production rate of 5,000 bopd over the remaining period of the production licence, to deliver gross 2P reserves of 12.8 MMbbl, of which 5.6 MMbbl of oil was attributed to Petsec Energy. The NPV<sub>10</sub> of that 5.6 MMbbl was US\$155.4 million, at 1 January 2016 forward oil prices.
- The block also contains significant additional resource potential in the four undeveloped fields (Osaylan, An Naeem, Wadi Bayhan and Harmel fields) which have been defined by nine wells and 3D seismic and hold target resources of 34 MMbbl of oil and 550 Bcf of gas.
- The internationally recognised Yemen Government led by President Hadi had requested in late 2016, that oil producers in Southern Yemen restart production as soon as possible, using the Yemen Government's facilities in the Shabwah and Masila areas until such times as the Marib Pipeline is permitted to be operational. To meet this request by the Hadi Government, the Company started making preparations and field operational changes to restart production from the An Nagyah Oilfield.
- In March 2017, the Company announced the execution of a contract for the manufacture and delivery of oil tanker truck loading equipment to be installed at the An Nagyah Central Processing Facility (CPF) within the Company's Damis (Block S-1) Production Licence in Yemen.
- The purchase of the oil loading hardware was a key component of preparations for the restart of production and delivery of crude via a trucking operation from the An Nagyah Oilfield.
- The An Nagyah Oilfield restart of production operations was suspended in mid-2017 due to the absence of Yemen government approvals required for the change in development plan to a crude oil trucking operation, and access to Yemen Government owned facilities.
- The Company for six months engaged with the local tribesmen, the administration for the Province of Shabwah and the Hadi Administration in Aden, Yemen and Riyadh, Saudi Arabia in an attempt to secure the necessary approvals to gain access to Yemen Government facilities and cost recovery of the new development plan.
- In December 2017, in Riyadh, Saudi Arabia, at lengthy meetings with Yemen officials from the Hadi Administration, Petsec's investment in Yemen was welcomed and encouraged. Officials at the highest level confirmed that the process of providing formal approvals supporting the Company's planned operations was in train.
- On the 24 December 2017, the Yemeni President announced the appointment of a new Minister of Oil and Minerals, Mr. Aws Al-Oud, an engineer from the Ministry of Oil and Minerals, and known to the Company. He has subsequently engaged with the Company to achieve the approvals required.
- At such time as the Yemen Government delivers the necessary approvals to support oil production and delivery to Yemen Government owned facilities, the operations to restart oil production at the An Nagyah Oilfield and transport production by truck can recommence.

**Financial**

Net production:

**347MMcfe**

11% ↑

Gas equivalent average sales price realised (US\$):

**\$3.79Mcfe**

9% ↑

Net oil and gas revenues (after royalties): (US\$)

**\$1.3M**

18% ↑

EBITDAX: negative (US\$)

**\$6.8M**

(previous corresponding period: negative US\$9.3 million).

Impairment, abandonment, exploration and work-over expense (US\$)

**\$4.0M**

90% ↑

Depreciation, depletion and amortisation (DD&amp;A) expense: (US\$)

**\$1.4M**

(US\$4.08/Mcfe) 61% ↑

Unit operating costs: (US\$)

**\$23.39/Mcfe**

(previous corresponding period: US\$33.95/Mcfe).

Net loss after tax: (US\$)

**\$12.0M**

(previous corresponding period: US\$13 million).

Acquisition, exploration and development expenditures: (US\$)

**\$5.1M**

7% ↓

Cash at 31 December 2017: (US\$)

**\$3.5M**

73% ↓

# Chairman's Report



**Dear Shareholder,**  
**Following the discovery of the substantial Hummer Gas/Oil Field in the Gulf of Mexico, USA, and the acquisition of the developed An Nagyah Oilfield in Yemen, in 2016, our objective in 2017 for your Company was to develop the Hummer Field and bring it into production, and to restart oil production at the An Nagyah Oilfield.**

The net 2P reserves in the USA, to the Company at the first of January 2018, were 15.9 Billion cubic feet ("Bcf") of gas and 1.137 million barrels of oil ("MMbo") having a net present value ("NPV") of US\$34.8 million, using a 10% discount rate. This NPV is the equivalent of 14 cents per share.

In Yemen, the An Nagyah Oilfield reserves are 5.648 million barrels of oil which had an NPV of US\$155 million at the lower oil prices extant on 1 January 2016.

I am pleased to report that in 2017 The Hummer Gas/Oil Field production platform and facilities were completed and the discovery well was brought into production on 21 November 2017. The well is currently producing 17 million cubic feet of gas a day and 340 barrels of oil, from a single reservoir, on a restricted choke.

The well tested at over 20 million cubic feet a day ("MMcfd") and 400 barrels of oil a day ("bopd"), using a 16/64th choke and similar reservoirs along trend have exceeded 25 million cubic feet of gas per day and 1,000 bopd.

The Company's second objective, which was to restart production in the An Nagyah Oilfield in Yemen at 5,000 bopd, moving up to 10,000 bopd, was not accomplished in the year but we have reason to be hopeful that it will be accomplished in the 2018 year, either by trucking, as was the intention in 2017, or through the Marib Pipeline to which the An Nagyah Oilfield is connected, as it is the intention of the Saudi Coalition to liberate the Port of Hodeidah, where the Marib Terminus is located, as soon as possible, and the Coalition military is fast approaching Hodeidah.

The An Nagyah Oilfield and all the other Marib oil fields have been shut-in since mid-2015 due to the Saudi led Coalition embargo on oil liftings from Ras Isa, the Red Sea terminus of the Marib Pipeline through which all Marib oil flows, as it has been under control of the Houthi rebel movement.

The Masila Basin, to the East of the Marib, restarted production in August 2016, piping oil to the Southern port of Ash Shihr, on the Arabian Coast, near the city of Mukalla. In October 2016, the internationally recognised Yemen Government led by President Hadi requested all oil producers in the Marib Basin to restart production as soon as possible, trucking crude to the Yemen Government's facilities in the Shabwah and Masila areas until such times as the Marib Pipeline is permitted to be operational.

To meet this request by the Hadi Government, the Company, starting in late 2016, made preparations including the construction of a 5,000 bopd truck loading facility, to restart 5,000 bopd production from currently suspended wells in the An Nagyah Oilfield, with the expectation of producing oil by mid-2017, and to truck that oil 530 kilometres East to the Masila Basin Pipeline Hub.



USA net 2P oil and gas reserves as of 1 January 2018 were 15.9 Bcf of gas and 1.137 MMbbl of oil (equivalent to 3.8 MMboe) with an NPV<sub>10</sub> value of US\$34.8 million.

While operational personnel and trucking was available, Hadi Government approvals, to change the development plan from using the Marib Pipeline to Ras Isa to instead trucking oil to the Masila Pipeline, and to access the Government owned Masila unloading, pipeline, storage and lifting facilities, have yet to be granted. The Company has continuously been advised by the Yemen Authorities that these approvals would be forthcoming in due course.

As approvals were not received by mid-2017 the Company suspended operations at An Nagyah, and actively engaged with the local tribesmen, the administration for the Province of Shabwah and the Hadi Administration in Aden, Yemen, and Riyadh, Saudi Arabia to secure the required approvals for change of the approved development plan in order to permit trucking, and access to Yemen Government facilities.

Discussions were elevated to a senior level and late in the year a series of constructive formal and informal meetings were held with senior officials from the Hadi Administration in Riyadh, Saudi Arabia. The Company was welcomed to operate in Yemen and encouraged to invest, and we were assured the approvals would be shortly forthcoming.

Subsequent to our meetings in Riyadh, a new Minister for Oil and Minerals was announced, Mr. Aws Al-Oud, an engineer, a long serving and high ranking technocrat from the Ministry, and well known to the Company.

The Ministry is now engaged with the Company and we trust the required approvals will soon be apparent.

### USA Development

The Company holds an interest in three producing fields in the USA – the Jeanerette and Mystic Bayou Fields, onshore Louisiana, and the Hummer Gas/Oil Field offshore Gulf of Mexico, USA, all defined by a single well each. While Mystic has further development potential, it is the Hummer Project which holds the greatest upside for the Company as the field apparently extends over a strike of some 10 kilometres, over three offshore blocks, and has been defined by one well in the North West corner.

Current net 2P oil and gas reserves to the Company at 1 January 2018 based on these three wells were 15.9 Bcf of gas and 1.137 MMbo having a net present value (NPV<sub>10</sub>) of US\$34.8 million.

The Hummer Prospect was generated by Petsec Energy in 2010 and was successfully drilled, logged and the well temporarily suspended in late 2015, the “B” production platform and facilities constructed in 2017 and first production on 21 November 2017.

## Chairman's Report continued

The initial design production capacity of the "B" platform facilities is 50 MMcfd plus 1,000 bopd which will accommodate the discovery well, Main Pass 270 B-1. Production capacity can be easily expanded to accommodate increased production from additional wells expected to be drilled from the "B" platform and any proximal well head platforms.

The Hummer Gas/Oil Field is a substantial oil and gas discovery with five reservoirs covering a large prospective area with an apparent strike length of some 10 kilometres, extending over three offshore lease blocks of Main Pass 270, 273 and 274, which cover 15,000 acres. Future drilling on the Hummer Project should provide considerable development upside for the Company.

The Hummer Development represents a valuable asset for the Company that will not only generate significant cash flow, but also deliver exciting development, exploration and growth opportunities for the Company in the future.

Petsec Energy owns a 12.5% working interest in the Hummer discovery in the three Main Pass leases.

### MENA Opportunity

The political situation in Yemen and the seeming incapacity of the bureaucracy to execute straightforward administrative matters, has clouded shareholders view as to the great potential value the Company holds in Yemen.

The Company's interests in Damis (Block S-1), and Block 7, provides early and substantial production (5,000 to 10,000 bopd) from the An Nagyah Oilfield, and substantial development from five other discovered oil fields, plus defined exploration potential the largest prospect of which is 900 MMbo.

The oil fields of Yemen have not been subject to the conflict and the only reason the Marib Basin fields are not in production is because of the Saudi Coalition embargo on oil lifting at the Marib Pipeline Terminus.

The Damis (Block S-1) acquisition added developed net (of all costs and taxes) proved and probable (2P) reserves to the Company of well in excess of 5.6 million barrels of oil from the developed/productive An Nagyah Oilfield, which held a NPV of US\$155 million based on a proposed trucking limit of 5,000 bopd, using a 10% discount rate and 1 January 2016 forward oil sales prices. The field has 15 productive wells currently shut-in, has produced up to 12,000 bopd, and has facilities that can

process 20,000 bopd, which are connected by an 80,000 bopd pipeline to the Marib Export Pipeline (350,000 bopd) to the export terminus of Ras Isa on the Red Sea. Restarting the facilities and opening the shut-in wells is a relatively straight forward process, and without obstruction, production could be achieved within 6 months of Yemen Government approvals.

The Damis (Block S-1) also holds an additional four discovered oil and gas fields, defined by some 15 wells, which hold target resources of 34 MMbbl of oil and 550 Bcf of gas which are yet to be developed. These assets when developed have the ability to completely transform the Company and create material value for shareholders.

In addition to the Damis (Block S-1) acquisition, the Block 7 acquisition holds the potentially large Al Meashar oil discovery with a target resource of 11 MMbbl to 50 MMbbl of oil, and eight prospects and leads each holding target resource potential of up to 900 MMbbl of oil. The Al Meashar oil discovery is 14 kilometres from the Habban Oilfield operated by OMV, which has estimated recoverable reserves of 300 million barrels of oil, and was producing 23,000 bopd, until the Marib Pipeline shut-in in 2015. The two fields have similar oil qualities from the same reservoir rocks.



In 2018, in the USA, we shall concentrate on maximising production from the now producing Hummer Gas/Oil Field, and evaluating further development opportunities that the Hummer Main Pass 270/273/274 Blocks present. In Yemen, we will continue to work with the Yemen Government towards delivering the approvals required to restart the An Nagyah Oilfield and bring the oil field into production as soon as possible.

#### Outlook 2018

The outlook for oil and gas has continued to improve since our last annual report. I am pleased to say that oil prices have rallied substantially over the course of 2017 to above US\$60/bbl, thankfully up from US\$30/bbl in 2016, and gas prices have consolidated at current levels of US\$3/Mcf. The strength in oil prices has been due to stronger consumption as the World recovers economically and the two great emerging countries China and India continue to grow at high rates.

On 26 February 2018, oil prices were trading at approximately US\$67/bbl for Brent and US\$64/ bbl for WTI, and U.S. gas prices were trading in the order of US\$2.68/MMBtu. Our current reserves are highly economic at current prices.

Recent economic data across the globe showing healthy growth for the USA, China and the EU would suggest that demand for both oil and gas will continue to grow and this should be reflected in stronger pricing over the course of 2018.

In 2018, in the USA, we shall concentrate on maximising production from the now producing Hummer Gas/Oil Field, and evaluating further development opportunities that the Hummer Main Pass 270/273/274 Blocks present. In Yemen, we will continue to work with the Yemen Government towards delivering the approvals required to restart the An Nagyah Oilfield and bring the oil field into production as soon as possible.

In closing, the Board and I would like to thank you, our shareholders, for your ongoing support, particularly through the disappointment of the lack of Yemen Government approvals which has unnecessarily delayed restart of oil production in Yemen.

I look forward to providing further details on our progress at the AGM to be held in May 2018, and more particularly, hopefully Yemen Government approvals for An Nagyah and a clear timetable for restart of production.



**TN Fern**  
Chairman and  
Managing Director

# Operations Review

## USA Production

Petsec Energy holds an interest in three producing fields – the Jeanerette and Mystic Bayou Fields, onshore Louisiana, and the Hummer Gas/Oil Field offshore Gulf of Mexico, USA.

Production was derived from the Mystic Bayou Field, onshore Louisiana USA and the Main Pass Block 270 B-1 well on the Hummer Field, which commenced initial production 21 November 2017.

**Adeline Sugar Factory No. 4 Well, Jeanerette Field**  
12.5% W.I. (NRI: 9.22%)

The Adeline Sugar Factory (“ASF”) No. 4 well located in the Jeanerette Field, St Mary Parish, Louisiana, was discovered and brought into production in June 2014.

The ASF No. well was shut-in in mid-November 2015 due to high water production and a restriction in the tubing due to salt build-up. The well has produced on an intermittent basis since that time, and it’s the operator’s intention to continue with intermittent production for the near-term.

**Williams No.2 Alt. Well, Mystic Bayou Field**  
25.0% W.I. (NRI: 18.5%)

The Williams No. 2 Alt. well, a gas/oil discovery drilled in mid-2015, is located on the Mystic Bayou Field, St Martin Parish, Louisiana was brought into production on 31 August 2015.

The well contributed 283 MMcfe of the Company’s total production volume of 347 MMcfe for the year.

**Main Pass Block 270 B-1 well – Hummer Gas/Oil Field (Main Pass 270/273/274)**

12.5% W.I. (NRI: 10.26354%) + ORRI: 0.00441%

The Main Pass Block 270 B-1 well on the Hummer exploration prospect in 215 feet of water, offshore Louisiana (federal waters) was drilled during the second half of 2015 and brought into production on 21 November 2017.

The well contributed 64 MMcfe of the Company’s total production volume of 347 MMcfe for the year. The well has averaged gross daily production rates of 16.0 MMcfpd and 328 bcpd since commencement of production, and is currently producing at a rate of approximately 17 MMcfpd and 340 bcpd.

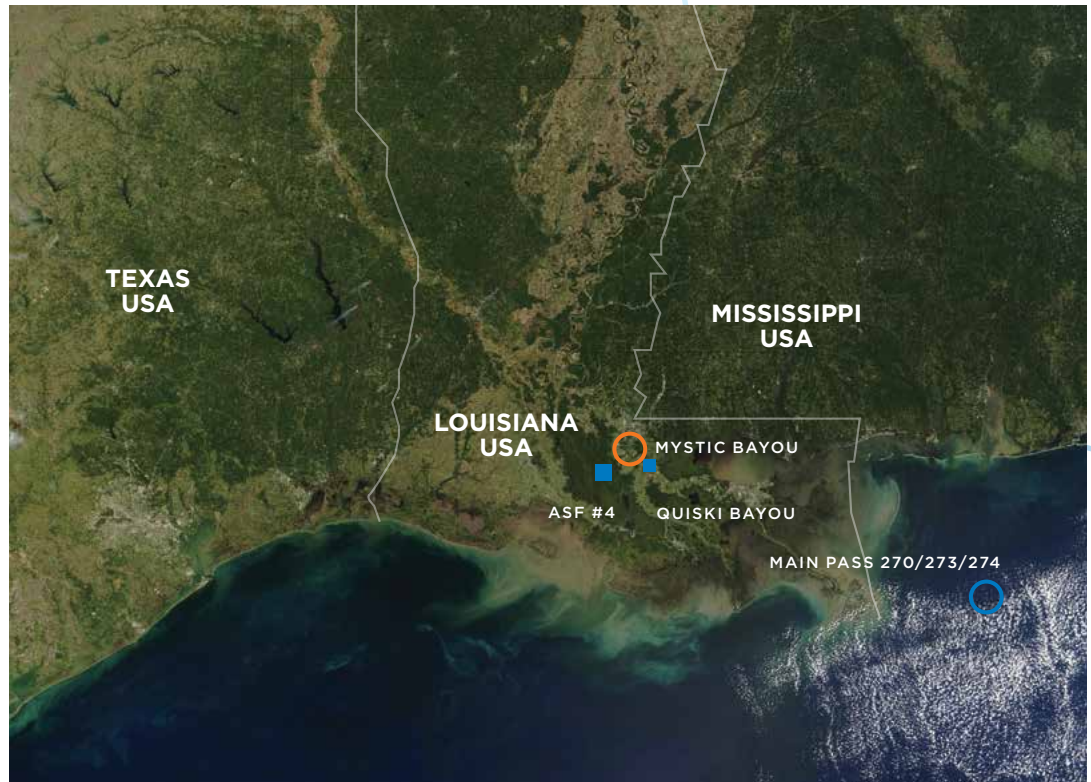
Testing of the well returned a rate in excess of 20 MMcfpd and 400 bopd on a 16/64th inch choke. Similar reservoirs along trend have produced at even higher rates, so there is some room to increase production rates over time.



Image: Main Pass 270/273/274  
Hummer Project: Main Pass 270  
“B” production platform



Mystic Bayou

Main Pass 270/273/274  
Hummer Project:  
Main Pass 270 "B"  
production platform

Petsec Energy Gulf of Mexico and Louisiana Gulf Coast, USA exploration and production leases

The Company produced net to its revenue interest 307 million cubic feet of gas and 6,689 barrels of oil/condensate (equivalent to 347 MMcfe) in the twelve months to 31 December 2017.

### Development

**Main Pass Block 270 B-1 well – Hummer Gas/Oil Field (Main Pass 270/273/274)**

12.5% W.I. (NRI: 10.26354%) + ORRI: 0.00441%

The Hummer Gas/Oil Field structural trend extends over 10 kilometres through Main Pass Blocks 270,273 and 274, which cover 15,000 acres in the Gulf of Mexico, offshore Louisiana, USA. The Hummer Project discovery well, Main Pass 270 B-1, was drilled, logged and temporarily suspended in late 2015.

Logs from the discovery well indicate five potential reservoir intervals, one of which was completed for production. All five sands are expected to be targets of future drilling for expansion of the Hummer Project in the three blocks.

The Main Pass 270 "B" platform jacket was installed over the well, and the well was completed and production tested in a single reservoir, late 2016. Following the production test the well was suspended pending installation of the deck, production facilities and pipelines. In early November 2017 the Main Pass 270 "B" Platform deck facilities and pipelines were successfully installed and the well was brought into production on 21 November 2017.

The initial design capacity of the "B" platform facilities of 50 MMcfpd plus 1,000 bopd which will accommodate the discovery well, Main Pass 270 B-1. The facilities were designed with space available on the deck to expand production capacity and accommodate increased production from additional wells expected to be drilled from the "B" platform and any proximal well head platforms.

## MENA

### (Middle East and North Africa) – Yemen

The Company has been focussed on securing government approvals to access Yemen Government owned pipeline, storage and shipping facilities, in order to allow the re-start of oil production from the An Nagyah Oilfield using trucks to transport crude to those government facilities until such times as the Marib Pipeline is returned to operation.

The oilfield is located within the Company's Damis (Block S-1), in Yemen, which the Company acquired in the first quarter of 2016. The Marib Export Pipeline which transported all Marib Basin oil production, has not been in operation since 2015 due to the Gulf Coast Coalition led embargo on oil liftings from the Red Sea terminal of Ras Isa, as it has been under control of the Houthi rebel movement. This has forced the Company to look at alternative transport options including trucking to the Masila Basin Pipeline Hub to the East of our blocks and export via the Ash Shihr Terminal on the Gulf of Aden coastline.

The internationally recognised Yemen Government led by President Hadi has requested in late 2016 that oil producers in Southern Yemen restart production as soon as possible, using the Yemen Government's facilities in the Shabwah and Masila areas until such times as the Marib Pipeline is permitted to be operational. To meet this request by the Hadi Government the Company, starting in late 2016, made preparations and field operational changes to restart production from the An Nagyah Oilfield.

The Company also engaged with the local tribesmen, the administration for the Province of Shabwah and the Hadi Administration to secure the approvals for change of the approved development plan in order to permit trucking, and access to Yemen Government facilities. Discussions have been elevated to a senior level and late in the year a series of constructive formal and informal meetings were held with senior officials from the Hadi Administration in Riyadh, Saudi Arabia.

Officials from the Hadi administration welcomed and encouraged Petsec's investment in Yemen and confirmed that the process of providing formal approvals supporting the Company's planned operations was in train. On the 24 December 2017, the Yemeni President announced the appointment of a new Minister of Oil and Minerals, Mr. Aws Al-Oud, an engineer from the Ministry of Oil and Minerals, and known to the Company. The new minister has subsequently engaged with the Company to effect the required approvals.

At such time as the government delivers the necessary approvals to support Marib oil production to allow truck delivery to

Yemen Government owned facilities, the operations to restart oil production at the An Nagyah Oilfield can recommence, prior to the reopening of the Marib pipeline to the Ras Isa terminal of the Red Sea coast.

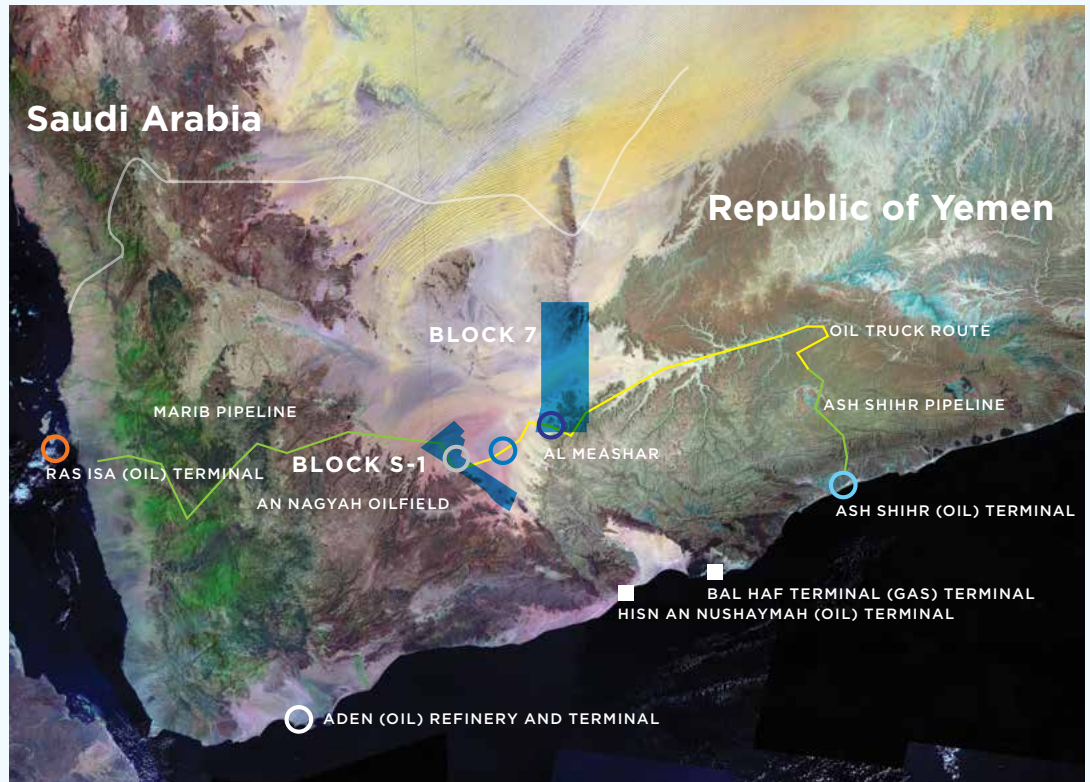
**Block 7, Al Barqa Permit, Republic of Yemen**  
**Petsec: 35% working interest**  
**(29.75% participating interest)**

Block 7 is an onshore exploration permit covering an area of 5,000 square kilometres (1,235,527 acres) located approximately 340 kilometres East of Sana'a, 80 kilometres North East of the Company's Damis (Block S-1) licence, and 14 kilometres West of OMV's Habban Oilfield. The block contains the Al Meashar oil discovery as well as an inventory of eight potential prospect/lead targets ranging in size from 2 to 900 MMbbl oil gross, defined by 2D and 3D seismic surveys.

The Al Meashar Oilfield (target resource of 11 MMbbl to 50 MMbbl<sup>1</sup>) contains two suspended discovery wells which in 2010-11, delivered flow rates ranging from 200 to 1,000 bopd in short-term testing of the wells. The oil exists in the same reservoirs and has a similar quality of oil to that of the Habban Oilfield.

<sup>1</sup>Source: Oil Search Limited





Petsec Energy Middle East and North Africa exploration and production leases

Ras Isa Oil Terminal aerial view



Road transport to oil pipeline facilities East of An Nagyah Oilfield



Ash Shihr Oil Terminal aerial view



Damis (Block S-1) Yemen – An Nagyah Oilfield production facilities



Block 7 Yemen – Al Meashar Oilfield discovery well



Crude oil transport to market



Petsec currently holds a government approved non-operating 35% working interest (29.75% participating interest) in the Block 7 Joint Venture and expects to acquire from Oil Search Limited (ASX: OSH) its 40% working interest (34% participating interest) in Block 7 and operatorship.

The Company also has an agreement with KUFPEC to acquire their 25% working interest in Block 7. The KUFPEC and Oil Search transactions brings the Company's potential interest in the block to 100% pending customary approvals from the Government.

**Damis (Block S-1), Production Licence Republic of Yemen**  
**Petsec: 100% working interest (82.5% participating interest)**

The Company acquired a 100% working interest (82.5% participating interest) in the block in early 2016.

Damis (Block S-1) of 1,152 square kilometres (284,665 acres) is located approximately 80 kilometres to the Southwest of Block 7 and holds five sizeable oil and gas discoveries – the developed and productive (until suspended in 2014), An Nagyah Oilfield, and a further four undeveloped oil and gas fields – Osaylan, An Naeem, Wadi Bayhan, and Harmel.

The four undeveloped fields hold substantial oil and gas resources in excess of 34 million barrels of oil and 550 Bcf of gas<sup>1</sup> representing substantial potential future growth of reserves and production for the Company.

The An Nagyah Oilfield audited reserves are assessed to be 12.8 MMbbl (2P) gross of which the financial net to Petsec Energy is 5.6 MMbbl of oil, having an NPV<sub>10</sub> value of US\$155 million as of 1 January 2016.

This estimate is based on producing no more than the proposed initial restart production rate of 5,000 bopd for trucking purposes, over the remaining period of the production licence. The block contains significant existing infrastructure, including the An Nagyah Oilfield facilities, which have the capacity to handle production of 20,000 bopd, and are connected by an 80,000 bopd pipeline to the Marib Hub and into the Marib pipeline of 350,000 bopd capacity to the 3.5 MMbbl oil storage terminal on the island of Ras Isa on the Red Sea coast near the port of Hodeidah.

The An Nagyah Oilfield which had initial reserves of 50 MMbbl of recoverable oil, commenced production in 2005, produced at rates exceeding 12,000 bopd and produced approximately 25 MMbbl until it was shut-in at the end of February 2014 following a declaration of Force Majeure. The field was producing at a restricted rate of over 5,600 bopd at the time of shut-in. The previous operator declared Force Majeure due to the political situation in Yemen and the resulting inability to ship oil from the export pipeline terminus at Ras Isa because of the Yemen Government/Saudi Coalition embargo on crude oil liftings.

The An Nagyah production facility has been well maintained during the shut-in period and remains in good condition. The facilities are connected to the Marib Pipeline which delivers crude oil to the Ras Isa island terminal which is near the Red Sea port of Hodeidah. The crude oil export terminal at Ras Isa has been closed since March 2015 due to the Hadi Government Coalition embargo on oil shipments because the rebels control the nearby port of Hodeidah. Yemen Government forces are currently moving on Hodeidah to clear the rebels and restore oil lifting from Ras Isa.

The Company in response to a request made by the Hadi Government in late 2016, to truck Marib crude to government owned facilities in the Masila Basin which can pipe crude to the South to the Ash Shihr terminal near Mukalla on the Arabian Coast, has been pursuing an alternative transport option to the Marib Pipeline, which would allow An Nagyah oil production to be trucked 530 kilometres East to the Masila Basin Pipeline Hub. The Company is planning to commence production at 5,000 bopd and within 12 months increase production to 10,000 bopd, from currently suspended wells.

As part of the trucking strategy the Company contracted with leading U.S. engineering firm S&S Technical Inc. to manufacture of a 5,000 bopd oil tanker loading equipment to be installed at the An Nagyah CPF. The manufacture and assembly testing of the equipment was completed in the second quarter 2017. The truck loading equipment is disassembled and packed for shipping. Timing of shipment is predicated on receipt of the Hadi Government approvals to truck to the Yemen Government owned Masila Basin facilities.

The restart of oil production from An Nagyah and transport of crude oil by way of truck to the Masila Basin oil loading facilities or other export terminals, including the Aden Refinery, remains subject to the receipt of Hadi Government approvals to use those government facilities.

<sup>1</sup>Source: Wood Mackenzie Asia Pacific Pty Ltd [November 2015]

Image: Damis (Block S-1)  
Yemen – An Nagyah Oilfield  
crude oil tank farm





## Oil and Gas Reserves

### Petsec Energy Group Net Reserves as of 1 January 2018

Oil Equivalent (Mboe <sup>1</sup> )	Net Proved Reserves <sup>3</sup>	Net Probable Reserves <sup>3</sup>	Net Proved and Probable Reserves <sup>3</sup>
<b>USA Reserves<sup>2</sup></b>			
Reserves as of 1 January 2017	2,754.1	1,117.7	3,871.8
Additions/(revisions)	339.4	(381.3)	(41.9)
Production	(58.9)	-	(58.9)
<b>USA reserves as of 1 January 2018</b>	<b>3,034.6</b>	<b>736.4</b>	<b>3,771.0</b>
<i>Developed</i>	<i>1,227.3</i>	<i>-</i>	<i>1,227.3</i>
<i>Undeveloped</i>	<i>1,807.3</i>	<i>736.4</i>	<i>2,543.7</i>
<b>Yemen Reserves<sup>2</sup></b>			
Reserves as of 1 January 2017	4,540.0	1,108.0	5,648.0
Additions/(revisions)	-	-	-
<b>Yemen reserves as of 1 January 2018</b>	<b>4,540.0</b>	<b>1,108.0</b>	<b>5,648.0</b>
<i>Developed</i>	<i>4,540.0</i>	<i>1,108.0</i>	<i>5,648.0</i>
<i>Undeveloped</i>	<i>-</i>	<i>-</i>	<i>-</i>
<b>Total Petsec Group Reserves</b>			
<b>Total Petsec Group Reserves as of 1 January 2018</b>	<b>7,574.6</b>	<b>1,844.4</b>	<b>9,419.0</b>
<i>Developed</i>	<i>5,767.3</i>	<i>1,108.0</i>	<i>6,875.3</i>
<i>Undeveloped</i>	<i>1,807.3</i>	<i>736.4</i>	<i>2,543.7</i>

1. Mboe = One thousand barrels of oil equivalent (using a ratio of approximately six thousand cubic feet of natural gas to one barrel of oil).
2. The USA and Yemen reserve assessments presented in the table above and throughout this report are consistent with the announcement released to the ASX on 22 February 2018. The Company confirms that it is not aware of any new information or data that materially affects the information included in these announcements, and that all the material assumptions and technical parameters underpinning the estimates therein continue to apply and have not materially changed.  
The U.S. reserves are stated for the Jeanerette, Mystic Bayou and Main Pass Block 270/273 fields. U.S. 2P reserves were 15.9 Bcf of gas and 1.137 MMbbl of oil. The Yemen reserves are stated only for oil for the An Nagyah Oilfield only and are unchanged from the assessment announced to the ASX on 15 March 2016.
3. Net reserves means those reserves representing the Company's net revenue interest (or net economic interest) which is the Company's working interest less royalties payable in the USA, and after all costs - operational, government taxes and government participation in Yemen, according to the terms of the Participating Agreement with the Yemen government.

To ensure accuracy and compliance of reserves estimations, the Company has put in place a robust process that incorporates the following governance arrangements and internal controls:

- At least once a year, as part of the year-end reporting procedures, the Company's producing oil and gas reserves are to be reviewed by an external, independent expert. The independent verified reserves are to be used as the basis for depreciation, depletion and amortisation calculations.
- All releases or reports containing statements of reserves are to be in accordance with ASX listing rules, requiring sign-off for content and context by an appropriately qualified person and in accordance with the Company's Reserves Policy.

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# Directors' and Financial Report For the Year Ended 31 December 2017

## The Secretary

Petsec Energy Ltd  
PO Box R204  
Royal Exchange NSW 1225  
+61 (2) 9247 4605

# Directors' Report

## For the year ended 31 December 2017

The directors present their report together with the Financial Report of Petsec Energy Ltd ("the consolidated entity"), being Petsec Energy Ltd (the Company) and its subsidiaries, for the financial year ended 31 December 2017 and the independent auditor's report thereon.

### 1. Directors

The names and particulars of the qualifications and experience of each director during or since the end of the financial year are:

#### Terrence N Fern

##### Chairman and Managing Director

Mr Fern has been a director since 1987 and has over 45 years of extensive international experience in petroleum and minerals exploration, development and financing. He holds a Bachelor of Science degree from the University of Sydney and has followed careers in both exploration geophysics and natural resource investment. Mr Fern was formerly a director of TSX and ASX listed company OceanaGold Corporation from 2006 until June 2011.

#### David A Mortimer AO

##### Non-executive Director

Chairman of the Audit Committee and the Nomination and Remuneration Committee

Mr Mortimer was appointed to the Board in 1985 and has over 40 years of corporate finance and management experience. He was a senior executive of TNT Limited Group from 1973, serving as Finance Director and then as Chief Executive Officer until his resignation in October 1997. He is presently Chairman of Opera Australia, Buildcorp Advisory Board and is Chairman of the Senate Investment and Commercialisation Committee. Mr Mortimer is a Director of MySale Group PLC and is on the CEDA's Board of Governors.

Mr Mortimer holds a Bachelor of Economics degree (First Class Honours) from the University of Sydney and was a Fellow of the University of Sydney Senate from 2010 to December 2017. He is a fellow of the Australian Institute of Company Directors. Mr Mortimer's other roles include Governor of the Australia Israel Chamber of Commerce, Chairman of the Sydney University Football Club Foundation and Chairman of the Australian Schoolboys Rugby Foundation.

Mr Mortimer was formerly a director and Chairman of ASX listed company Leighton Holdings Limited from 1997 until August 2011 and Chairman of Australia Post from 2006 to 2012. He was a foundation shareholder and Chairman of Crescent Capital Partners until 31 December 2017 and was a member of the Grant Samuel Advisory Board until December 2017. He has held many directorships and has chaired listed and unlisted companies as well as written three major reports for Governments.

#### Alan P Baden

##### Non-executive Director

Member of the Audit Committee and the Nomination and Remuneration Committee

Mr Baden was appointed to the Board in May 2013 and is a U.S. citizen, resident in Houston, Texas. He is Of Counsel with the legal firm of Thompson & Knight and has over 40 years of experience in the U.S. oil and gas industry, with a focus on mergers and acquisitions, public and private financings, and U.S. capital market activities, representing U.S. and foreign E&P companies, master limited partnerships and other energy companies. He has been recognised by his peers to be a leading lawyer in oil and gas transactions and in securities and corporate finance.

Mr Baden holds a Juris Doctor Degree from Case Western Reserve University, and a Bachelor of Science (Economics) Degree from the Wharton School of the University of Pennsylvania.

### 2. Executive Officers

#### Ross A Keogh

##### President of PEI and Group Chief Financial Officer

Mr Keogh joined the Company in 1989 and has over 35 years of experience in the oil and gas industry. Between 1979 and 1989, Mr Keogh worked in the financial accounting and budgeting divisions of Total Oil Company and as Joint Venture Administrator for Bridge Oil Limited in Australia. Mr Keogh holds a Bachelor of Economics degree, with a major in Accounting, from Macquarie University in Sydney. Mr Keogh was appointed Chief Financial Officer in November 1998 until April 2002, and appointed President of PEI in April 2002. Mr Keogh took on the extended role of Group Chief Financial Officer in February 2012, in addition to his current role of President of PEI.

#### Maki Petkovski

##### Chief Executive Officer of Petsec Energy (Middle Eastern) Limited

Mr Petkovski joined the Company in March 2015 as the Chief Executive Officer of Petsec Energy (Middle Eastern) Limited. Mr Petkovski has over 25 years of experience in the international upstream oil and gas business sector and has held various managerial and senior technical roles with large E&P companies including BP, Ampolex Ltd and most recently with Oil Search Ltd where he was responsible for managing Oil Search's MENA portfolio.

Mr Petkovski holds a Bachelor of Applied Science (Geology) degree from the University of Technology, Sydney.

#### Paul Gahdmar

##### Company Secretary and Group Financial Controller

Mr Gahdmar joined the Company in 1999 as the Financial Accountant of the Petsec Energy Ltd group and has since held a number of management positions within the Company. Mr Gahdmar was appointed as the Company Secretary of Petsec Energy Ltd in 2008 and has 25 years of experience in corporate accounting and finance in listed companies within the mining and resources industry. Mr Gahdmar holds a Master of Business and Technology degree from The University of New South Wales and a Diploma in Investor Relations from the Australasian Investor Relations Association. Mr Gahdmar is a Fellow of the Institute of Public Accountants and a Member of the Australian Institute of Company Directors.



## Directors' Report Continued

### For the year ended 31 December 2017

### 3. Directors' meetings

The Board has a formally constituted Audit Committee and a Nomination and Remuneration Committee, of which Mr Mortimer and Mr Baden (non-executive directors) are members. Mr Mortimer chairs both committees.

The number of directors' meetings (including meetings of committees of directors) and number of meetings attended by each of the directors of the Company during the financial year are:

	Regular Board Meetings	Additional Board Meetings	Audit Committee Meetings	Nomination & Remuneration Committee Meetings
<b>Total number held during the year</b>	<b>8</b>	<b>-</b>	<b>4</b>	<b>2</b>
T N Fern <sup>1</sup>	8	-	4	2
D A Mortimer	8	-	4	2
A P Baden	8	-	4	2

<sup>1</sup> Mr Fern attended the Audit and Nomination & Remuneration Committee meetings as an invitee.

### 4. Remuneration report

The Remuneration Report is set out on pages 25 to 31 and forms part of the Directors' Report for the financial year ended 31 December 2017.

### 5. Principal activities

The principal activities of the consolidated entity during the course of the year were oil and gas development and production onshore and coastal waters of the Louisiana Gulf Coast region, and the shallow waters of the Gulf of Mexico, USA and in the MENA region.

There have been no significant changes in the nature of these activities during the year.

### 6. Financial review

The consolidated entity incurred a net loss after tax for the twelve months ended 31 December 2017 of US\$12.0 million (previous corresponding period: net loss after tax of US\$13.0 million) after the recognition of an impairment provision against its Yemen oil and gas assets of US\$4.0 million and depreciation, depletion and amortisation ("DD&A") expense of US\$1.4 million.

The US\$4.0 million impairment provision recognised against its Block S-1 and Block 7, Yemen assets, was required due to the inability to recommence production and activities in Yemen as a result of the ongoing conflict. This impairment provision may be reversed in the future once a successful resolution to the conflict is achieved and production at the An Nayah Oilfield has been restarted.

Net oil and gas revenues of US\$1.3 million were generated for the current period, from production of 347 million cubic feet of gas equivalent ("MMcfe") at an average natural gas equivalent sales price of US\$3.79/Mcfe. This was 21% higher than the net oil and gas revenues achieved in the previous corresponding period of US\$1.1 million, mainly due to the higher production volumes, following the commencement of initial production from the Main Pass Block 270 B-1 well on 21 November 2017, coupled with higher commodity sales prices received.

Net production for the current period of 347 MMcfe was 11% higher than the previous corresponding period of 313 MMcfe due to the commencement of initial production from the Main Pass Block 270 B-1 well.

The consolidated entity realised an average net gas equivalent sales price of US\$3.79/Mcfe in the current period, 9% higher than the US\$3.48/Mcfe achieved for the previous corresponding period, reflecting the improved commodity price environment. The consolidated entity received an average sales price of US\$3.22/Mcf and US\$49.19/bbl for its natural gas and oil/condensation production, respectively. This compares to US\$2.66/Mcf and US\$43.86/bbl received respectively, in the previous corresponding period.

Lease operating expense of US\$0.8 million (previous corresponding period: US\$3.1 million) and geological, geophysical and administrative ("GG&A") expense of US\$7.3 million (previous corresponding period: US\$7.5 million), reflecting the reduced level of activities in the MENA region and various cost cutting initiatives implemented during the second half of the year.

On a unit-basis, lease operating expense was US\$2.27/Mcfe (previous corresponding period: US\$9.97/Mcfe) and GG&A expense was US\$21.12/Mcfe (previous corresponding period: US\$23.98/Mcfe).

The consolidated entity recorded negative earnings before interest, income tax, depreciation, depletion and amortisation, and exploration expense ("EBITDAX") of US\$6.8 million for the current period (previous corresponding period: negative EBITDAX of US\$9.3 million).

Depreciation, depletion and amortisation ("DD&A") expense was US\$1.4 million in the current period (previous corresponding period: US\$0.8 million).

## Financial position

At 31 December 2017, the Company held cash deposits of US\$3.5 million (A\$4.5 million). This was US\$9.6 million lower than the previous corresponding period cash balance of US\$13.1 million, reflecting the Company's low oil and gas revenue base in combination with the payment of the Company's share of the Hummer project development, and plug & abandonment work at Main Pass 19. The cash deposits which are predominantly held in US dollars included secured deposits of US\$0.2 million.

During the second half of the year, the Company as part of its ongoing cost reduction initiatives has streamlined its executive management teams in both the U.S. and MENA businesses, as well as further and continuing operational cost reductions pending restart of the An Ngyah Oilfield on receipt of Yemen Government approvals. These cost reductions together with the commencement of production from the Hummer Gas/Oil Field will moderate demand on the Company's cash balance in 2018.

## 7. Operations review

Petsec Energy Ltd (the "Company") is an independent oil and gas exploration and production company listed on the Australian Stock Exchange (ASX Ticker: PSA) and is traded over the counter in the USA in the form of American Depositary Receipts (symbol: PSJEY). The Company has operations in the shallow waters of the Gulf of Mexico and onshore Louisiana, USA and in the Republic of Yemen.

### USA

#### Production

Petsec Energy holds interests in three producing fields – the Jeanerette and Mystic Bayou Fields, onshore Louisiana, and the Hummer Gas/Oil Field offshore Gulf of Mexico, USA. The Company produced 347 MMcfe in the twelve months to 31 December 2017, primarily from the Mystic Bayou Field, onshore Louisiana USA and the Main Pass Block 270 B-1 well on the Hummer Field, which commenced initial production 21 November 2017.

#### Williams No.2 well – Mystic Bayou Field

*Petsec: 25% working interest (18.5% net revenue interest)*

The Williams No.2 gas/condensate discovery well on the Mystic Bayou Field in St. Martin Parish, Louisiana was drilled and brought into production on 31 August 2015.

The well contributed 283 MMcfe to production for the year.

#### Adeline Sugar Factory No. 4 Well – Jeanerette Field

*Petsec: 12.5% working interest (9.2% net revenue interest)*

The Adeline Sugar Factory ("ASF") No. 4 well located in St. Mary Parish, Louisiana was drilled and brought into production in June 2014. The well was shut-in in mid-November 2015 due to high water production and a restriction in the tubing due to salt build-up. The well has produced on an intermittent basis since that time, and it's the operator's intention to continue with intermittent production for the near-term.

#### Main Pass Block 270 B-1 well – Hummer Gas/Oil Field (Main Pass 270/273/274)

*Petsec: 12.5% working interest (10.26354% net revenue interest) + ORRI: 0.00441%*

The Main Pass Block 270 B-1 well on the Hummer exploration prospect in 215 feet of water, offshore Louisiana (federal waters) was drilled during the second half of 2015 and brought into production on 21 November 2017. The well contributed 64 MMcfe to production for the year.

The well has averaged gross daily production rates of 16.0 MMcfpd and 328 bcpd since commencement of production, and is currently producing at a rate of approximately 17 MMcfpd and 340 bcpd.

#### Development

#### Main Pass Block 270 B-1 well – Hummer Gas/Oil Field (Main Pass 270/273/274)

*Petsec: 12.5% working interest (10.26354% net revenue interest) + ORRI: 0.00441%*

The Hummer Gas/Oil Field extends over Main Pass Blocks 270,273 and 274, which cover 15,000 acres in the Gulf of Mexico, offshore Louisiana, USA. The Hummer Project discovery well, Main Pass 270 B-1, was drilled, logged and temporarily suspended in late 2015.

Logs from the discovery well indicate five potential sands/reservoirs in the well, one of which was completed for production. These untested sands will be targets of future drilling for expansion of the Hummer Project across the three blocks.

The Main Pass 270 "B" platform jacket was installed over the well, and the well was completed and production tested in a single reservoir in late 2016. Following the production test the well was suspended pending installation of the deck, production facilities and pipelines. In early November 2017 the Main Pass 270 "B" Platform deck facilities and pipelines were successfully installed and the well was brought into production on 21 November 2017.

The initial design capacity of the "B" platform facilities is for production rates of 50 MMcfpd plus 1,000 bopd which will accommodate the discovery well, Main Pass 270 B-1. The facilities were designed with space available on the deck to expand production capacity and accommodate increased production from additional wells expected to be drilled from the "B" platform and any proximal well head platforms.

### MENA

#### Yemen

The Company has been focused on securing government approvals to access Yemen Government owned pipeline, storage and shipping facilities, in order to allow the re-start of oil production from the An Ngyah Oilfield using trucks to transport crude to those government facilities until such times as the Marib Pipeline is returned to operation.

## Directors' Report Continued

### For the year ended 31 December 2017

## 7. Operations review (continued)

### MENA (continued)

The oilfield is located within the Company's Damis (Block S-1), in Yemen, which the Company acquired in the first quarter of 2016. The Marib Export Pipeline which transported all Marib Basin oil production, has not been in operation since 2015 due to the Gulf Coast Coalition led embargo on oil liftings from the Red Sea terminal of Ras Isa, as it has been under control of the Houthi rebel movement. This has forced the Company to look at alternative transport options including trucking to the Masila Basin Pipeline Hub to the East of our blocks and export via the Ash Shihr Terminal on the Gulf of Aden coastline.

The internationally recognised Yemen Government led by President Hadi requested in late 2016 that oil producers in Southern Yemen restart production as soon as possible, using the Yemen Government's facilities in the Shabwah and Masila areas until such times as the Marib Pipeline is permitted to be operational. To meet this request by the Hadi Government the Company starting in late 2016, made preparations and field operational changes to restart production from the An Nagyah Oilfield. The Company also engaged with the local tribesmen, the administration for the Province of Shabwah and the Hadi Administration to secure the approvals for change of the approved development plan in order to permit trucking, and access to Yemen Government facilities. Discussions have been elevated to a senior level and late in the year a series of constructive formal and informal meetings were held with senior officials from the Hadi Administration in Riyadh, Saudi Arabia.

Officials from the Hadi administration welcomed and encouraged Petsec's investment in Yemen and confirmed that the process of providing formal approvals supporting the Company's planned operations was in train. On 24 December 2017, the Yemeni President announced the appointment of a new Minister of Oil and Minerals, Mr Aws Al-Oud, an engineer from the Ministry of Oil and Minerals, and known to the Company. The new minister has subsequently engaged with the Company to effect the required approvals.

At such time as the government delivers the necessary approvals to support Marib oil production to allow truck delivery to Yemen Government owned facilities, the operations to restart oil production at the An Nagyah Oilfield can recommence, prior to the reopening of the Marib Pipeline to the Ras Isa terminal of the Red Sea coast.

#### **Damis (Block S-1) Production Licence, Republic of Yemen**

*Petsec: 100% working interest (82.5% participating interest)*

The Company acquired a 100% working interest (82.5% participating interest) in the block in early 2016.

Damis (Block S-1) of 1,152 square kilometres (284,665

acres) is located approximately 80 kilometres to the Southwest of Block 7 and holds five sizeable oil and gas discoveries – the developed and productive (until suspended in 2014), An Nagyah Oilfield, and a further four undeveloped oil and gas fields – Osaylan, An Naeem, Wadi Bayhan, and Harmel.

The four undeveloped fields defined by nine wells and 3D seismic hold substantial oil and gas resources in excess of 34 million barrels of oil and 550 Bcf of gas<sup>1</sup> representing substantial potential future growth of reserves and production for the Company.

The An Nagyah Oilfield audited reserves are assessed to be 12.8 MMbbl (2P) gross of which the financial net to Petsec Energy is 5.6 MMbbl of oil, having an NPV<sub>10</sub> value of US\$155 million as of 1 January 2016. This estimate is based on producing no more than the proposed initial restart production rate of 5,000 bopd for trucking purposes, over the remaining period of the production licence. The block contains significant existing infrastructure, including the An Nagyah Oilfield facilities, which have the capacity to handle production of 20,000 bopd, and are connected by an 80,000 bopd pipeline to the Marib Hub and into the Marib pipeline of 350,000 bopd capacity to the 3.5 MMbbl oil storage terminal on the island of Ras Isa on the Red Sea coast near the port of Hodeidah.

The An Nagyah Oilfield which had initial reserves of 50 MMbbl of recoverable oil, commenced production in 2005, produced at rates exceeding 12,000 bopd and produced approximately 25 MMbbl until it was shut-in at the end of February 2014 following a declaration of Force Majeure. The field was producing at a restricted rate of over 5,600 bopd at the time of shut-in. The previous operator declared Force Majeure due to the political situation in Yemen and the resulting inability to ship oil from the export pipeline terminus at Ras Isa because of the Yemen Government/Saudi Coalition embargo on crude oil liftings.

The An Nagyah production facility has been well maintained during the shut-in period and remains in good condition. The facilities are connected to the Marib Pipeline which delivers crude oil to the Ras Isa island terminal which is near the Red Sea port of Hodeida. The crude oil export terminal at Ras Isa has been closed since March 2015 due to the Hadi Government Coalition embargo on oil shipments because the rebels control the nearby port of Hodeida. Yemen Government forces are currently moving on Hodeida to clear the rebels and restore oil lifting from Ras Isa.

<sup>1</sup> Source: Wood Mackenzie Asia Pacific Pty Ltd (November 2015).



The Company in response to a request made by the Hadi Government in late 2016, to truck Marib crude to government owned facilities in the Masila Basin which can pipe crude to the South to the Ash Shihr terminal near Mukalla on the Arabian Coast, has been pursuing an alternative transport option to the Marib Pipeline, which would allow An Nagyah oil production to be trucked 530 kilometres East to the Masila Basin Pipeline Hub. The Company is planning to commence production at 5,000 bopd and within 12 months increase production to 10,000 bopd, from currently suspended wells.

As part of the trucking strategy the Company contracted with leading U.S. engineering firm S&S Technical Inc. for the manufacture of a 5,000 bopd oil tanker loading facility to be installed at the An Nagyah CPF. The manufacture and assembly testing of the equipment was completed in the second quarter 2017. The truck loading equipment is disassembled and packed for shipping. Timing of shipment is predicated on receipt of the Hadi Government approvals to truck to the Yemen Government owned Masila Basin facilities.

The restart of oil production from An Nagyah and transport of crude oil by way of truck to the Masila Basin oil loading facilities or other export terminals, including the Aden Refinery, remains subject to the receipt of Hadi Government approvals to use those government facilities.

#### **Block 7, Al Barqa Permit, Republic of Yemen**

*Petsec: 35% working interest (29.75% participating interest)*

Block 7 is an onshore exploration permit covering an area of 5,000 square kilometres (1,235,527 acres) located approximately 340 kilometres East of Sana'a, 80 kilometres North East of the Company's Damis (Block S-1) licence, and 14 kilometres West of OMV's Habban Oilfield. The block contains the Al Meashar oil discovery as well as an inventory of eight potential prospect/lead targets ranging in size from 2 to 900 MMbbl oil gross, defined by 2D and 3D seismic surveys.

The Al Meashar Oilfield (target resource of 11 MMbbl to 50 MMbbl<sup>1</sup>) contains two suspended discovery wells which in 2010-11, delivered flow rates ranging from 200 to 1,000 bopd in short-term testing of the wells. The oil exists in the same reservoirs and has a similar quality of oil to that of the Habban Oilfield, located 14 kilometres to the West, with estimated reserves of 300 MMbbl of oil, which was producing 23,000 bopd prior to shut-in in 2015.

Petsec currently holds a government approved non-operating 35% working interest (29.75% participating interest) in the Block 7 Joint Venture and expects to acquire from Oil Search Limited (ASX: OSH) its 40% working interest (34% participating interest) in Block 7 and operatorship.

The Company also has an agreement with KUFPEC to acquire their 25% working interest in Block 7. The KUFPEC and Oil Search transactions brings the Company's potential interest in the block to 100% pending customary approvals from the Government.

## **8. Objectives, strategy and future performance**

It is the consolidated entity's objective to increase the value of the Company and thus shareholder value through successful oil and gas exploration, development, and production, and through acquisitions. The consolidated entity's strategy to meet the above objective is to produce its current reserves, pursue participation in high quality, high impact exploration drilling opportunities in the Gulf Coast onshore Louisiana and offshore Gulf of Mexico, USA. The consolidated entity also intends to explore opportunities to acquire onshore producing oil and gas reserves in MENA which hold significant development, exploitation potential.

The consolidated entity's strategy takes into account the expected operating and market conditions, together with general economic conditions, which are inherently uncertain. The consolidated entity has structured and proactive risk management and internal control systems in place to manage material risks. Certain of those risks are inherent to the consolidated entity's business, such as drilling for, producing and marketing oil and gas. Although the consolidated entity is committed to minimising its risk exposure, many risks are largely beyond the control of the consolidated entity and its directors. Moreover, other more general risks associated with the vicissitudes of commercial life, political change, and cyclical economic conditions are risks that the consolidated entity cannot control. The following are those risks which management and the Board consider to be material business risks that could adversely affect the achievement of the financial prospects of the Company discussed above:

### **Drilling and Production Risks**

Drilling for oil and natural gas is subject to numerous risks. Paramount is the risk that drilling operations will not result in the discovery of commercially productive oil or natural gas reservoirs. Also, projects are subject to economic risks. Before beginning a drilling project, the Company can only estimate the cost of drilling and completing wells as many indeterminable factors can affect the total cost. For example, oil and natural gas drilling and production activities may be extended, shortened, delayed or cancelled as a result of a variety of factors, many of which are beyond the Company's control. These risks may negatively impact the economics of drilling projects. In part, these factors include:

- Unexpected drilling conditions including abnormal geological pressure or irregularities in formations;
- Equipment failures or accidents;
- Weather conditions, including hurricanes and other tropical weather disturbances;
- Shortages in experienced labour;
- Shortages, delays in the delivery, or high cost of drilling rigs and equipment;
- Constraints on access to transportation systems (pipelines) delaying sale of oil and natural gas;
- Reduction or losses of resources or reserves;
- Acquiring and maintaining title to its interests;
- Unresolved landowner or regulatory issues; and
- Inability of third-party joint venture partners to participate in or fund their share of drilling and production activities.

1 Source: Oil Search Limited.

## Directors' Report Continued

### For the year ended 31 December 2017

## 8. Objectives, strategy and future performance (continued)

### Operating Risks

The exploration for and development and production of oil and natural gas involves a variety of industry operating risks. If any of these industry-operating risks occur, the Company could have substantial losses. Substantial losses could include injury or loss of life, severe damage to or destruction of property, natural resources and equipment, pollution or other environmental damage, clean-up responsibilities, regulatory investigation and penalties and suspension of operations. These risks include:

- Fire, explosions, blow-outs and surface cratering;
- Lost or damaged oilfield drilling pipe and service tools;
- Casing or cement failures;
- Environmental hazards caused by oil spills, natural gas leaks, pipeline ruptures or discharges of toxic gases; and
- Hazards of marine operations such as capsizing, collision and adverse weather and sea conditions.

### Marketing and Sales Risks

The marketing and sale of oil and natural gas is subject to the risk of adverse commodity price fluctuations that impact cash flow. Some factors that affect commodity prices include:

- Relatively minor changes in the supply of and demand for oil and natural gas;
- Market uncertainty;
- The level of consumer product demand;
- Weather conditions;
- Domestic and foreign governmental regulations;
- The price and availability of alternative fuels;
- Technological advances affecting oil and natural gas consumption;
- Political and economic conditions in oil producing countries, particularly those in the Middle East;
- Policies of the Australian, U.S. and Yemen governments;
- The foreign supply of oil and natural gas;
- The price of oil and natural gas imports; and
- General economic conditions.

To reduce the impact of price fluctuations, from time to time, the Company has used derivative financial instruments, such as natural gas swaps, puts and costless collars, on a portion of its future production. However, such hedging activities may not be sufficient to protect the Company against the risk of price declines and may limit income and liquidity if prices rise.

- Hedging activities that are intended to reduce the risk of downward price fluctuations on a portion of our future production may limit the Company's potential income if oil and gas prices rise above a level established by its hedge instruments.

- Hedging counterparties require collateral when the mark-to-market value of our hedge instruments is in the counterparties' favour and exceeds the Company's credit limits with such counterparties. As a result, the Company may be required to provide substantial security to the counterparties when commodity prices change significantly. The security provided may be in the form of cash or letters of credit, and thus, could have a significant impact on the Company's liquidity.

### Exchange Rate Risks

Adverse exchange rate variations between the U.S. dollar and the Australian dollar may impact upon cash balances held in Australian dollars. Since most of the Company's operations are conducted in U.S. dollars, the Company generally maintains a substantial portion of its cash balances in U.S. dollar accounts. Occasionally, however, it may have some cash deposits in Australian dollar accounts. Until these funds are converted into U.S. dollars, the U.S. dollar value of the deposits will change as the exchange rate between the two currencies fluctuates.

### Other Risks

Other factors can impact the environment in which the Company operates and thus can affect its ability to perform as desired. Such factors include:

- Changes in legislation and Government regulation both in the USA and in other countries in which the Company operates;
- Political and societal risks from wars, social and ethnic unrest, changes in government and insurgencies in the districts, regions and countries in which the Company operates;
- Environmental risks from existing and new regulations and standards being applied in the jurisdictions in which the Company operates;
- General economic conditions in the USA and Australia;
- Stock market conditions in Australia; and
- Availability of capital.

## 9. Dividends

Directors do not recommend the payment of a dividend for the financial year ended 31 December 2017. No dividends were paid during the financial year.

## 10. Significant changes in state of affairs

There were no significant changes to the state of affairs of Petsec Energy during the financial year, other than those detailed in the "Financial review" and "Operations review" sections of this report.

## 11. Environmental regulation

The consolidated entity's oil and gas exploration and production activities are subject to significant environmental regulation under U.S. Federal and State legislation and Republic of Yemen legislation.

The consolidated entity is committed to achieving a high standard of environmental performance and compliance with all lease conditions. Directors are not aware of any breach of environmental compliance requirements relating to the consolidated entity's activities during the year.

## 12. Likely developments

The consolidated entity's focus in 2018 will be:

- USA – expanding oil and gas reserves in the Gulf Coast region.
- MENA – securing the necessary Hadi Government approvals to permit the completion of negotiations covering trucking, pipeline access, storage, and shipping contracts, necessary to restart An Nayah oil production.

## 13. Directors' interests

The relevant interest of each director in the shares or options over such instruments issued by the Company, as notified by the directors to the Australian Securities Exchange in accordance with S205G (1) of the *Corporations Act 2001*, at the date of this report is as follows:

Director	Ordinary Shares	Options over Ordinary Shares
T N Fern	37,876,361	Nil
D A Mortimer	12,241,098	Nil
A P Baden	Nil	Nil

## 14. Share options

### Options granted to directors and officers of the Company

As at 31 December 2017, there were 3,700,000 share options and 1,000,000 options over ordinary shares in Petsec Energy Ltd on issue.

During or since the end of the financial year:

- 1,000,000 options over ordinary shares were granted under the Employee Option Plan to key management personnel of the Company as part of their remuneration. No share options were granted under the Employee Share Plan.
- 3,000,000 share options were forfeited under the Employee Share Plan.

During or since the end of the financial year, no ordinary shares have been issued by the Company as result of the exercise of options.

## 15. Indemnification and insurance of officers

During the year ended 31 December 2017, the Company maintained policies of insurance in respect of directors and officers liability. The policies insure persons who are directors or officers of the Company and its controlled entities against certain costs and expenses which may be incurred by them in defending proceedings and against other liabilities which may arise from their positions. The insured directors and officers are the directors, executive officers and secretaries of the Company and the directors, executive officers and secretaries of controlled entities.

The insurance contracts prohibit the disclosure of particulars of the premiums and the nature of the liabilities insured.

The Company has entered into Deeds of Indemnity and Access with directors on the terms approved by shareholders. The agreements stipulate that the Company will meet the full amount of any liabilities to another person that might arise from their position (except where the liability arises out of conduct involving a lack of good faith).

The Company has made during or since the end of the financial year no payments in relation to indemnification. The Company provides the normal indemnities to directors and officers in relation to the work carried out on behalf of or at the request of the Company.

## 16. Non-audit services

The Company's auditor, KPMG, may perform certain other services in addition to their statutory duties.

The Board considers the non-audit services provided during the year by the auditor and in accordance with advice provided by resolution of the audit committee, is satisfied that the provision of those non-audit services during the year by the auditor is compatible with, and did not compromise, the auditor independence requirements of the Corporation Act 2001 for the following reasons:

- All non-audit services were subject to the corporate governance procedures adopted by the Company and have been reviewed by the audit committee to ensure they do not impact the integrity and objectivity of the auditor; and
- The non-audit services provided do not undermine the general principles relating to auditor independence as set out in APES 110 *Code of Ethics for Professional Accountants*, as they did not involve reviewing or auditing the auditor's own work, acting in a management or decision-making capacity for the Company, acting as an advocate for the Company or jointly sharing risks and rewards.

Details of the amounts paid to the auditor of the Company, KPMG, and its related practices for audit and non-audit services provided during the year are set out in note 7 of the accompanying Financial Statements.



## Directors' Report Continued

### For the year ended 31 December 2017

#### 17. Lead auditor's independence declaration

The Lead Auditor's Independence Declaration is set out on page 32 and forms part of the Directors' Report for the financial year ended 31 December 2017.

#### 18. Rounding off

The Company is of a kind referred to in ASIC Corporations (Rounding in Financial/Directors' Reports) Instrument 2016/191 dated 24 March 2016 and in accordance with that Class Order, amounts in the Financial Report and Directors' Report have been rounded off to the nearest one thousand dollars, unless otherwise stated.

#### 19. Events subsequent to balance date

Subsequent to balance date, the Company entered into an agreement with the Registrar of the secured convertible note facility to extend the redemption date of the facility and to reinstate Tranche 2 of the facility which was not drawn down and allowed to lapse at the expiry date of 5 January 2018. The key terms of the variation agreement include:

##### Extension of redemption date of the facility

1. Redemption date amended from 23 January 2019 to 23 July 2019.
2. Interest rate of 12.5% per annum monthly compounding for the period 1 January 2018 to 23 January 2019 will increase to 15% per annum monthly compounding from 23 January 2019 to 23 July 2019.
3. Conversion price to be reduced from 15 cents per share to 12.5 cents per share.
4. A note extension facility fee of 5 million fully paid shares in Petsec Energy Ltd at a value of 10 cents per share.
5. The expiry date of the unlisted options previously issued to Sing Rim Pte Ltd, for underwriting the Petsec Energy Ltd rights issue in November 2016, to be extended from 23 January 2019 to 23 July 2020, and the exercise price reduced from 15 cents per share to 12.5 cents per share.

##### Reinstatement of Tranche 2 - US\$5 million

Tranche 2 of the convertible note facility which provides access to a further US\$5 million is subject to the following conditions precedent to issue, and is at the discretion of the Registrar:

- (a) 40% of Tranche 2 on clear indication based upon publicly available information that crude oil has commenced to flow freely within the Republic of Yemen and crude oil has been shipped and sold in material amounts from that Country.
- (b) 10% for each 100,000 barrels of crude oil net to the Group which has been produced in Yemen and transported and stored at the shipping terminal ready for sale, up to a total of 40% of Tranche 2.
- (c) 10% for every 100,000 barrels of crude oil shipped and sold by the Group from Yemen, up to a total of 20% of Tranche 2.
- (d) Conversion: Maximum of 100% of the interest owing on the notes from Tranche 2 and 50% of the advance made under Tranche 2.
- (e) Conversion price: 12.5 cents per share.
- (f) Interest rate: 12.5% per annum compounded monthly.
- (g) Facility fee: 5 million fully paid shares in Petsec Energy Ltd at such times as the facility is drawn.
- (h) Drawdown: Expires on 23 January 2019.
- (i) Redemption date: 23 July 2019.

Other than the matter disclosed above, there has not arisen in the interval between the end of the financial year and the date of this report any item, transaction or event of a material and unusual nature likely, in the opinion of the directors of the Company, to affect significantly the operations of the consolidated entity, the results of those operations, or the state of affairs of the consolidated entity, in future years.

This report is made with a resolution of the directors:



T N Fern  
Director

Sydney, 27 February 2018

## 20. Remuneration Report – Audited

### 20.1 Introduction

This Remuneration Report forms part of the Directors' Report. It outlines the overall remuneration strategy, framework and practices adopted by the Company and the consolidated entity ("Petsec Energy Group") for the year ended 31 December 2017 and has been prepared in accordance with Section 300A of the *Corporations Act 2001* and its regulations.

In accordance with the *Corporations Act 2001*, remuneration details are disclosed for the Petsec Energy Group's Key Management Personnel.

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Petsec Energy Group. Key management personnel comprise the directors of the Company and senior executives of the Petsec Energy Group, whose names appear in the tables in section 20.5 of this report.

### 20.2 Executive summary

The Board's remuneration policy is to provide fair and market competitive levels of remuneration for all employees, including directors and key management personnel in order for the Company and the Petsec Energy Group to benefit by attracting and retaining a high quality team.

The Company has a Nomination and Remuneration Committee to assist the Board in the implementation and administration of the remuneration policy – refer to section 20.3, below.

The key developments during the year in the implementation and administration of the remuneration policy included:

- The annual review of key management personnel performance.
- Annual review of the Nomination & Remuneration Committee Charter.

### 20.3 Nomination and Remuneration Committee

The Nomination and Remuneration Committee oversees the appointment and induction process for directors and committee members, and the selection, appointment and succession planning process of the Company's Chief Executive Officer. The Committee makes recommendations to the Board on the appropriate skill mix, personal qualities, expertise and diversity of each position. When a vacancy exists or there is a need for particular skills, the Committee in consultation with the Board determines the selection criteria based on the skills deemed necessary.

The Committee reviews and makes recommendations to the Board on compensation packages and policies applicable to the executive officers and directors of the Petsec Energy Group. It is also responsible for oversight of diversity, employee share and option schemes, incentive performance packages, superannuation entitlements, retirement and termination entitlements, fringe benefits policies, deeds of access and indemnity, and professional indemnity and liability insurance policies.

Executive compensation and other terms of employment are reviewed annually by the Nomination and Remuneration Committee having regard to performance against goals set at the start of the year, relevant corporate information and where appropriate independent expert advice.

The Nomination and Remuneration Committee comprised the following members during the year:

- D A Mortimer (Chairman) – Independent Non-executive Director
- A P Baden – Independent Non-executive Director

The Board policy is that the Nomination and Remuneration Committee will comprise a majority of non-executive directors and a non-executive chairman.

The Nomination and Remuneration Committee meets at least twice a year and as required. The Committee met two times during the year and the Committee members' attendance record is disclosed in the table of directors' meetings.

The Nomination and Remuneration Committee's Charter is available on the Company's website [www.petsec.com.au](http://www.petsec.com.au).

### 20.4 Principles of compensation

Compensation levels for key management personnel are competitively set to attract and retain appropriately qualified and experienced directors and senior executives. The Nomination and Remuneration Committee obtains peer comparisons and/or independent advice on the appropriateness of compensation packages of the Petsec Energy Group, given trends in comparative companies both locally and internationally and the objectives of the Company's compensation strategy.

The compensation structures explained below are designed to attract suitably qualified candidates, reward the achievement of the Company's objectives, and achieve the broader outcome of creation of value for shareholders.

The compensation structures take into account:

- The capability and experience of the key management personnel; and
- The ability of key management personnel to control the relevant performance of their segment of operation.

Compensation packages include a mix of fixed compensation and performance-based incentives, including equity-based incentives as set out below.

In addition to their salaries, the Petsec Energy Group also provides non-cash benefits to its key management personnel as set out below, and contributes to several post-employment defined contribution superannuation plans in Australia and also matches contributions made by U.S. based key management personnel to a voluntary savings plan under Section 401(k) of the U.S. tax code.

#### Fixed compensation

Fixed compensation consists of base compensation (which is calculated on a total cost basis and includes any FBT charges related to employee benefits), as well as employer contributions to superannuation funds in Australia and employer matching contributions to voluntary savings plans under Section 401(k) of the U.S. tax code. Non-cash benefits comprise employer payments towards U.S. health, dental and vision plans, as well as life and salary continuance insurance benefits.

## Directors' Report Continued

### For the year ended 31 December 2017

## 20. Remuneration Report – Audited (continued)

### 20.4 Principles of compensation (continued)

The Nomination and Remuneration Committee reviews compensation levels and other terms of employment annually through a process that considers individual, segment and overall performance of the Company against goals set at the start of the year. In addition, where necessary, external consultants provide analysis and advice to ensure the directors' and senior executives' compensation is competitive in the market place.

#### Performance-linked compensation

Performance-linked compensation includes both short-term and long-term incentives and is designed to reward key management personnel for meeting or exceeding the Company's financial objectives and agreed individual objectives. The short-term incentive (STI) is an "at risk" bonus provided in the form of cash or ordinary shares in the Company, while the long-term incentive (LTI) is provided as either shares or options over ordinary shares of the Company under the rules of the Employee Share and Option Plans approved by shareholders at the Annual General Meeting held on 19 May 2016 (see note 17(b) to financial statements). The maximum number of securities in aggregate that may be issued under the Employee Share and Option Plans is 15,033,435.

#### Short-term incentive

Short-term incentives are provided to key management personnel through discretionary bonuses as determined and granted by the Company's Nomination and Remuneration Committee. Factors considered by the Committee when granting discretionary bonuses include personal performance, the achievement of strategic objectives, and the retention and motivation of employees.

No short-term incentives were awarded to key management personnel during the year.

#### Long-term incentive

Certain key management personnel are also provided with long-term incentives through participation in the Company's Employee Share and Option Plans, subject to the approval of the Committee. Key management personnel are typically offered options on an annual basis with the exercise price of the shares or options based on the weighted average market price of the Company's ordinary shares for the five trading days preceding the date of issue, subject to a minimum exercise price of 20 cents.

During the year, the Company issued 1,000,000 options over ordinary shares under its shareholder approved Employee Option Plan ("EOP") to Mr Krenzke as long-term incentive compensation (see note 20.7 of the Remuneration Report). The options are exercisable at 20 cents per share and have an expiry date of 1 June 2019. The designated exercise period will be from 1 December 2018 through to the expiry date and is conditional on the Company share price trading at a VWAP (volume weighted average price) above 25 cents per share for 30 days or longer.

#### Consequences of performance on shareholder wealth

In considering the Group's performance and benefits for shareholder wealth, the remuneration committee have regard to the following indices in respect of the current financial year and the previous four financial years.

	2017	2016	2015	2014	2013
Profit/(loss) attributable to owners of the company	<b>(\$11,964,000)</b>	(\$13,024,000)	(\$10,605,000)	(\$1,048,000)	(\$15,210,000)
Dividend paid	-	-	-	-	-
Closing share price as at 31 December	<b>\$0.105</b>	\$0.17	\$0.078	\$0.115	\$0.09
Change in share price	<b>(\$0.065)</b>	\$0.092	(\$0.037)	\$0.025	(\$0.09)

Net profit/(loss) amounts for 2013 to 2017 have been calculated in accordance with Australian Accounting Standards (AASBs).



### Service and employment agreements

Remuneration and other terms of engagement of executive employees are formalised in service agreements that are unlimited in term but capable of termination by varying periods of notice or by payment of an amount in lieu of notice. The service agreements generally outline the components of compensation paid, but do not prescribe how compensation levels are modified from year-to-year. Compensation levels are reviewed each year in light of cost-of-living changes, performance and changes in the scope of the role performed by the executive and changes required to meet the principles of the compensation policy.

The Managing Director, Mr Fern, is engaged via a company of which Mr Fern is a director. The Company may terminate this agreement without cause by giving not less than twelve months' notice, or pay an amount equal to the fees for twelve months in lieu of notice. Mr Fern may terminate the agreement with not less than six months' notice. In the event of a breach of the agreement by the Company, Mr Fern may terminate the agreement by giving one month's notice and would be entitled to a payment equal to fees for a twelve-month period.

The Chief Executive Officer of Petsec Energy (Middle Eastern) Limited, Mr Petkovski and the Group Chief Financial Officer and President of Petsec Energy Inc., Mr Keogh ("senior executives") have employment agreements that are capable of termination without cause by the company by a lump sum payment equal to one times their annual Base Salary. The senior executives may terminate the agreement without cause by giving the company at least 120 days' notice in writing. In the event of a breach of the agreement by the Company, the senior executives may terminate their agreement by giving 30 days' notice and would be entitled to receive a lump sum payment equal to one times their annual base salary at that time.

Other executives have service agreements which are capable of termination by the Company without cause by the payment of between one and three months' notice, or are "at-will" employment contracts entered into in the USA where either party may terminate the employment relationship at any time and for any reason without any further liability, except as required by law.

### Non-executive directors

Directors' fees are set having regard to periodic advice from external remuneration consultants, market surveys and the level of fees paid relative to those of other comparable companies. Directors' fees for the 2017 year were unchanged from the 2016 year and comprise base fees, plus statutory superannuation for Australian directors. Directors are also entitled to reasonable travel, accommodation and other expenses incurred in attending meetings or while engaged on Company business.

Non-executive directors do not receive performance-related compensation. Directors' fees cover all main Board activities and membership of committees and are subject to the aggregate limit of A\$300,000 approved by shareholders at the 1996 Annual General Meeting.

Non-executive directors appointed prior to 2003 are entitled to receive a retirement benefit equivalent to the remuneration received in the three years prior to retirement. Incoming non-executive directors are not entitled to retirement benefits.

## Directors' Report Continued

### For the year ended 31 December 2017

## 20. Remuneration Report – Audited (continued)

### 20.5 Directors' and Executive Officers' Remuneration Report

Details of the nature and amount of remuneration for the key management personnel consisting of each director and executive officer of the Company and the consolidated entity are:

		Short-term benefits			Post-employment benefits		Share-based payment		Total US\$	Proportion of remuneration performance related %	Accounting fair value as proportion of remuneration %
		Salary & fees US\$	Short-term incentive/retention cash bonus US\$	Other benefits US\$	Service agreements US\$	Super-annuation benefits US\$	Termination benefits US\$	Accounting fair value US\$			
<b>Directors<sup>1</sup></b>											
<b>Executive</b>											
T N Fern <sup>1</sup> Chairman, Managing Director (Note 1)	2017	-	-	<b>44,434</b>	<b>551,160</b>	-	-	-	<b>595,594</b>	-	-
	2016	-	-	41,645	534,240	-	-	-	575,885	-	-
<b>Non-executive</b>											
D A Mortimer <sup>1</sup> Director	2017	<b>49,758</b>	-	-	-	<b>4,727</b>	-	-	<b>54,485</b>	-	-
	2016	48,230	-	-	-	4,582	-	-	52,812	-	-
A P Baden Director	2017	<b>50,000</b>	-	-	-	-	-	-	<b>50,000</b>	-	-
	2016	50,000	-	-	-	-	-	-	50,000	-	-
M S Lober Director (Note 2)	2017	-	-	-	-	-	-	-	-	-	-
	2016	19,086	-	-	-	-	-	-	19,086	-	-
<b>Total directors remuneration</b>	2017	<b>99,758</b>	-	<b>44,434</b>	<b>551,160</b>	<b>4,727</b>	-	-	<b>700,079</b>	-	-
	2016	117,316	-	41,645	534,240	4,582	-	-	697,783	-	-

<sup>1</sup> Australian-based directors' remuneration amounts are actually paid in Australian dollars and presented in US dollars at the following average FX rates i) 2017 – 0.7655 ii) 2016 – 0.7420.

Details of the nature and amount of remuneration for the key management personnel consisting of each director of the Company and executive officer of the Company and the consolidated entity are:

		Short-term benefits				Post-employment benefits		Share-based payment		Proportion of remuneration performance related %	Accounting fair value as proportion of remuneration %
		Salary & fees US\$ Note 4	Short-term incentive/retention cash bonus <sup>B</sup> US\$ Note 5	Other benefits US\$ Note 6	Service agreements US\$	Super-annuation /401K benefits US\$	Termination benefits US\$	Accounting fair value US\$ Note 7	Total US\$		
<b>Executives</b>											
R J Smith Chief Executive Officer of Petsec Energy Inc. (PEI)	2017	129,167	-	14,615	-	6,458	310,000	-	460,240	-	-
	2016	310,000	-	33,427	-	13,250	-	-	356,677	-	-
R A Keogh President, PEI and Group Chief Financial Officer	2017	301,808	-	35,916	-	13,500	-	-	351,224	-	-
	2016	296,135	-	33,457	-	13,250	-	-	342,842	-	-
R Krenzke Executive Vice President Exploration, PEI	2017	122,316	-	18,065	-	6,042	290,000	-	436,423	-	-
	2016	292,231	-	38,842	-	13,250	-	-	344,323	-	-
M Petkovski <sup>A</sup> Chief Executive Officer of Petsec Energy (Middle Eastern) Limited (Note 3)	2017	-	-	33,426	267,925	-	-	12,876	314,227	-	4.1
	2016	-	23,014	24,992	259,700	-	-	16,396	324,102	7.1	5.1
P Gahdmar <sup>A</sup> Company Secretary, Group Financial Controller	2017	151,016	-	14,945	-	13,283	-	3,012	182,256	-	1.7
	2016	148,024	-	8,024	-	12,875	-	3,246	172,169	-	1.9
<b>Total executive remuneration</b>	2017	704,307	-	116,967	267,925	39,283	600,000	15,888	1,744,370	-	0.9
	2016	1,046,390	23,014	138,742	259,700	52,625	-	19,642	1,540,113	1.5	1.3
<b>Total directors and executive officer remuneration</b>	2017	804,065	-	161,401	819,085	44,010	600,000	15,888	2,444,449	-	0.6
	2016	1,163,706	23,014	180,387	793,940	57,207	-	19,642	2,237,896	1.0	0.9

A Australian-based executive officers' remuneration amounts are actually paid in Australian dollars and presented in US dollars at the following average FX rates i) 2017 - 0.7655 ii) 2016 - 0.7420.

B Bonuses accrued in respect of 2016 year were paid in 2016.



## Directors' Report Continued

### For the year ended 31 December 2017

## 20. Remuneration Report – Audited (continued)

### 20.5 Directors' and Executive Officers' Remuneration Report (continued)

#### Notes

1) Included in service agreements above is an amount of US\$551,160 (2016: US\$534,240) which was paid or is payable to, a company of which Mr Fern is a director.

During the year, a company of which Mr Fern is a director provided management services to the Company and its controlled entities. The dealings were in the ordinary course of business and on normal terms and conditions.

2) Mr Lober resigned from his position on the Board and its Committees on 19 May 2016.

3) Included in service agreements above is an amount of US\$267,925 (2016: US\$259,700) which was paid, or is payable to a company of which Mr Fern is a director and through which Mr Petkovski provided services.

4) Salary and fees for certain specified executives includes the movement during the reporting period of accruals for annual leave and long service leave.

5) Short-term incentive/retention cash bonuses represent discretionary bonus amounts granted based on a number of factors including personal performance, the achievement of strategic objectives, retention and motivation of employees.

6) Other benefits represent amounts paid on behalf of the Managing Director and Executive Officers in respect of insurance, car parking, fringe benefits and sign-on bonuses.

7) The fair value of options and shares is calculated at the date of the grant using the Black-Scholes model and allocated to each reporting period over the period from grant date to vesting date.

During the year, US\$600,000 was paid as termination payments to key management personnel for the year ended 31 December 2017 (2016: Nil).

The following table sets out the factors and assumptions used in determining the fair value of the shares or options issued to key management personnel.

Grant date	Expiry date	Average fair value per option	Exercise price	Price of shares on grant date	Average estimated volatility	Risk-free interest rate	Dividend yield
26/03/12 <sup>1</sup>	26/03/22	A\$0.116	A\$0.20	A\$0.235	75.7%	3.56%	-
26/6/15 <sup>2</sup>	24/06/21	A\$0.006	A\$0.20	A\$0.10	67.0%	2.06%	-
23/02/16 <sup>3</sup>	24/02/21	A\$0.005	A\$0.20	A\$0.09	58.1%	1.75%	-
4/09/17 <sup>4</sup>	1/06/19	A\$0.005	A\$0.20	A\$0.097	76.3%	2.01%	-

1 Issued to P Gahdmar. Shares vest between 1 January 2013 – 1 January 2015 at a minimum share price of A\$0.20.

2 Issued to M Petkovski. Shares vest between 24 June 2016 – 24 June 2020 at a minimum share price of between A\$0.25–A\$0.45.

3 Issued to P Gahdmar. Shares vest between 24 February 2017 – 24 February 2020 at a minimum share price of between A\$0.25–A\$0.40.

4 Issued to R Krenzke. Options vest on 1 December 2018 at a minimum share price of A\$0.25.

### 20.6 Analysis of short-term incentive/retention cash bonuses included in remuneration

Amounts included in remuneration for the financial year, within the table included in note 20.5 of this Directors' Report, represent the amount that vested in the financial year based on a number of factors including achievement of personal goals, satisfaction of specified performance criteria, retention and motivation of employees.

No amounts vest in future financial years in respect of the short-term incentives and bonus schemes for the 2017 year.

No amounts were forfeited due to the performance or service criteria not being met in relation to the current financial year.

### 20.7 Equity instruments

#### Options over equity instruments granted as compensation

All options refer to options over ordinary shares of Petsec Energy Ltd, which are exercisable on a one-for-one basis under the Employee Share Plan and Employee Option Plan.

During 2017:

1. No shares were granted to key management personnel under the Employee Share Plan (2016: 800,000) and no shares vested (2016: nil).

2. 1,000,000 options were granted to key management personnel under the Employee Option Plan (2016: Nil).

The movement during the reporting period in the number of shares and options under the Employee Share Plan and Employee Option Plan held, directly, indirectly or beneficially, by each key management person, including their related parties, is as follows:

	Held at 1 January 2017	Granted as compensation	Exercised	Other changes <sup>1</sup>	Held at 31 December 2017	Vested during the year	Vested and exercisable at 31 December 2017
<b>Directors</b>							
T Fern	2,000,000	-	-	(2,000,000)	-	-	-
D Mortimer	-	-	-	-	-	-	-
A Baden	-	-	-	-	-	-	-
<b>Executives</b>							
R Smith <sup>2</sup>	-	-	-	-	-	-	-
R Keogh	-	-	-	-	-	-	-
R Krenzke <sup>3</sup>	-	1,000,000	-	-	1,000,000	-	-
M Petkovski <sup>4</sup>	2,500,000	-	-	-	2,500,000	-	-
P Gahdmar <sup>5</sup>	1,200,000	-	-	-	1,200,000	-	-

1 Other changes represent shares and options that expired or were forfeited during the year.

2 Mr Smith retired from the Company effective 31 May 2017.

3 Mr Krenzke transitioned from fulltime employment to a consultancy with the Company effective 1 June 2017. Options exercisable upon reaching a minimum share price of A\$0.25.

4 Shares exercisable upon reaching a minimum share price of between A\$0.25 to A\$0.45.

5 Shares exercisable upon reaching a minimum share price of between A\$0.20 to A\$0.40.

No shares or options under the Employee Share Plan and Employee Option Plan are held by key management personnel related parties.

#### Exercise of options granted as compensation

No shares were issued on the exercise of options previously granted as compensation to key management personnel during the reporting period (previous corresponding period: Nil).

#### Movements in shares

The movement during the reporting period in the number of ordinary shares in Petsec Energy Ltd held, directly, indirectly or beneficially, by each key management person, including their related parties, is as follows:

	Held at 1 January 2017	Granted as compensation	Purchases	Received on exercise of options	Sales/ Disposal of relevant interest	Held at 31 December 2017
<b>Directors</b>						
T Fern	37,876,361	-	-	-	-	37,876,361
D Mortimer	12,241,098	-	-	-	-	12,241,098
A Baden	-	-	-	-	-	-
M Lober	-	-	-	-	-	-
<b>Executives</b>						
R Smith <sup>1</sup>	-	-	-	-	-	-
R Keogh	1,612,500	-	-	-	-	1,612,500
R Krenzke <sup>2</sup>	250,000	-	-	-	-	250,000
M Petkovski	1,500,000	-	-	-	(895,500)	604,500
P Gahdmar	400,000	-	-	-	-	400,000

1 Mr Smith retired from the Company effective 31 May 2017.

2 Mr Krenzke transitioned from fulltime employment to a consultancy with the Company effective 1 June 2017.

#### Modification of terms of equity-settled share-based payment transactions

No terms of equity-settled share-based payment transactions (including options granted as compensation to key management personnel) have been altered or modified by the issuing entity during the reporting period or the prior period.

# Lead Auditor's Independence Declaration

## under Section 307C of the Corporations Act 2001



### Lead Auditor's Independence Declaration under Section 307C of the Corporations Act 2001

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To the Directors of Petsec Energy Ltd.

I declare that, to the best of my knowledge and belief, in relation to the audit for the financial year ended 31 December 2017 there have been:

- (i) no contraventions of the auditor independence requirements as set out in the *Corporations Act 2001* in relation to the audit; and
- (ii) no contraventions of any applicable code of professional conduct in relation to the audit

A handwritten signature in blue ink that reads 'KPMG'.

KPMG

A handwritten signature in blue ink, appearing to be 'D. Camilleri'.

Daniel Camilleri  
*Partner*  
Sydney  
27 February 2018



# Consolidated statement of profit and loss and other comprehensive income

For the year ended 31 December 2017

	Note	2017 US\$'000	2016 US\$'000
Revenues from sale of oil & gas		1,316	1,116
Royalties paid		-	(25)
<b>Net revenues after royalties</b>		<b>1,316</b>	1,091
Other income/(expenses)	5	24	196
Lease operating expenses		(788)	(3,121)
Geological, geophysical and administrative expenses		(7,329)	(7,505)
Depreciation, depletion, and amortisation		(1,416)	(791)
Exploration and work-over expense		-	(936)
Dry hole and impairment expense		(3,988)	(1,203)
Change in rehabilitation provision		491	-
Financial income	8	47	23
Financial expenses	8	(321)	(778)
<b>Profit/(loss) before income tax</b>		<b>(11,964)</b>	(13,024)
Income tax benefit/(expense)	9	-	-
<b>Profit/(loss) from continuing operations</b>		<b>(11,964)</b>	(13,024)
<b>Profit/(loss) for the period</b>		<b>(11,964)</b>	(13,024)
<b>Other comprehensive income/(loss)</b>			
<i>Items that may be reclassified subsequently to profit or loss:</i>			
Foreign exchange translation differences		582	(295)
<b>Total comprehensive income/(loss) for the period</b>		<b>(11,382)</b>	(13,319)
	Note	US Cents 2017	US Cents 2016
<b>Earnings/(loss) per share</b>			
Basic and diluted earnings/(loss) per share	10	(3.8)	(5.5)

The statement of profit and loss and other comprehensive income is to be read in conjunction with the notes to the consolidated financial statements set out on pages 37 to 64.

## Consolidated statement of changes in equity

### For the year ended 31 December 2017

<i>In thousands of USD</i>	Share capital US\$'000	Translation Reserve US\$'000	Share-based compensation US\$'000	Option Reserve US\$'000	Accumulated losses US\$'000	Total Equity US\$'000
Balance at 1 January 2016	186,541	1,404	13	-	(164,164)	23,794
<b>Total comprehensive income for the period</b>						
Profit/(loss) for the period	-	-	-	-	(13,024)	(13,024)
<b>Other comprehensive income</b>						
Foreign exchange translation difference	-	(295)	-	-	-	(295)
Total other comprehensive income/(loss)	-	(295)	-	-	-	(295)
Total comprehensive income/(loss) for the period	-	(295)	-	-	(13,024)	(13,319)
<b>Transactions with owners, recorded directly in equity</b>						
<b>Contributions by and distributions to owners</b>						
Share issue/(cancelled)	7,187	-	-	-	-	7,187
Option issue	-	-	-	416	-	416
Vesting of share options	5	-	(5)	-	-	-
Share-based payments expense	-	-	23	-	-	23
Total transactions with owners	7,192	-	18	416	-	7,626
Balance at 31 December 2016	193,733	1,109	31	416	(177,188)	18,101
<b>Balance at 1 January 2017</b>	<b>193,733</b>	<b>1,109</b>	<b>31</b>	<b>416</b>	<b>(177,188)</b>	<b>18,101</b>
<b>Total comprehensive income/(loss) for the period</b>						
Profit/(loss) for the period	-	-	-	-	(11,964)	(11,964)
<b>Other comprehensive income/(loss)</b>						
Foreign exchange translation differences	-	547	-	35	-	582
Total other comprehensive income/(loss)	-	547	-	35	-	582
Total comprehensive income/(loss) for the period	-	547	-	35	(11,964)	(11,382)
<b>Transactions with owners, recorded directly in equity</b>						
<b>Contributions by and distributions to owners</b>						
Share issue/(cancelled)	244	-	-	-	-	244
Vesting of share options	14	-	(14)	-	-	-
Share-based payments expense	-	-	22	-	-	22
Total transactions with owners	258	-	8	-	-	266
<b>Balance at 31 December 2017</b>	<b>193,991</b>	<b>1,656</b>	<b>39</b>	<b>451</b>	<b>(189,152)</b>	<b>6,985</b>

The statement of changes in equity is to be read in conjunction with the notes to the consolidated financial statements set out on pages 37 to 64.

# Consolidated statement of financial position

## As at 31 December 2017

	Note	2017 US\$'000	2016 US\$'000
<b>ASSETS</b>			
<b>Current assets</b>			
Cash and cash equivalents		3,264	9,504
Restricted cash deposits		-	3,368
Trade and other receivables	11	524	4,566
Prepayments		324	187
Crude inventories		-	190
<b>Total current assets</b>		<b>4,112</b>	<b>17,815</b>
<b>Non-current assets</b>			
Restricted cash deposits		222	205
Property, plant and equipment		152	184
Oil and gas properties	12(a)	15,679	16,810
Exploration and evaluation properties	12(b)	-	358
<b>Total non-current assets</b>		<b>16,053</b>	<b>17,557</b>
<b>Total assets</b>		<b>20,165</b>	<b>35,372</b>
<b>LIABILITIES</b>			
<b>Current liabilities</b>			
Trade and other payables	14	3,162	12,229
Rehabilitation provisions	18	-	546
Employee benefits provisions		192	181
<b>Total current liabilities</b>		<b>3,354</b>	<b>12,956</b>
<b>Non-current liabilities</b>			
Trade and other payables	14	3,699	-
Secured borrowings	15	5,568	3,299
Fair value of derivative instruments	16	178	764
Rehabilitation provisions	18	179	68
Employee benefits provisions		202	184
<b>Total non-current liabilities</b>		<b>9,826</b>	<b>4,315</b>
<b>Total liabilities</b>		<b>13,180</b>	<b>17,271</b>
<b>Net assets</b>		<b>6,985</b>	<b>18,101</b>
<b>EQUITY</b>			
Issued capital	19	193,991	193,733
Reserves	19	2,146	1,556
Accumulated losses		(189,152)	(177,188)
<b>Total equity</b>		<b>6,985</b>	<b>18,101</b>

The statement of financial position is to be read in conjunction with the notes to the consolidated financial statements set out on pages 37 to 64.

## Consolidated statement of cashflows

For the year ended 31 December 2017

	Note	2017 US\$'000	2016 US\$'000
<b>Cashflows from operating activities</b>			
Cash receipts from customers		1,300	1,383
Cash payments for royalties		-	(30)
Cash payments to suppliers and employees		(9,629)	(8,268)
Interest received		47	23
Restricted deposits <sup>1</sup>		3,373	93
<b>Net cash used in operating activities</b>	29	<b>(4,909)</b>	(6,799)
<b>Cashflows from investing activities</b>			
Payments for property, plant and equipment		(55)	(138)
Payments for oil and gas, exploration and evaluation properties		(4,198)	(2,727)
<b>Net cash used in investing activities</b>		<b>(4,253)</b>	(2,865)
<b>Cashflows from financing activities</b>			
Proceeds from shares issued - net of transaction costs		1,957	5,521
Proceeds from drawdown of convertible note facility		492	4,508
<b>Net cash from financing activities</b>		<b>2,449</b>	10,029
Net (decrease)/increase in cash and cash equivalents		(6,713)	365
Cash and cash equivalents at 1 January		9,504	9,140
Effects of exchange rate changes on cash held		473	(1)
<b>Cash and cash equivalents at 31 December</b>		<b>3,264</b>	9,504

<sup>1</sup> Relates to cash previously used to guarantee certain future rehabilitation obligations (see note 23 - Contingencies and Legal Matters for further details).

The statement of cashflows is to be read in conjunction with the notes to the consolidated financial statements set out on pages 37 to 64.



# Notes to the Financial Statements

For the year ended 31 December 2017

## 1. Reporting entity

Petsec Energy Ltd (the “Company”) is a company domiciled in Australia. The registered office of the Company is Level 27, Governor Macquarie Tower, One Farrer Place Sydney NSW 2000. The consolidated financial statements of the Company as at and for the year ended 31 December 2017 comprise the Company and its subsidiaries (together referred to as the “consolidated entity”).

The financial report is presented in United States dollars, which is the consolidated entity’s choice of presentation currency.

The Group is a for-profit entity and is primarily involved in oil and gas exploration and production with operations in the shallow waters of the Gulf of Mexico and onshore Louisiana, USA, and in the Republic of Yemen.

## 2. Basis of preparation

### (a) Statement of compliance

The financial report is a general purpose financial report which has been prepared in accordance with Australian Accounting Standards (“AASBs”) (including Australian Interpretations) adopted by the Australian Accounting Standards Board (“AASB”) and the *Corporations Act 2001*. The consolidated financial report of the consolidated entity and the financial report of the Company comply with International Financial Reporting Standards (“IFRSs”) and interpretations adopted by the International Accounting Standards Board (IASB).

The Board of Directors approved the financial statements on 27 February 2018.

### (b) Basis of measurement

The consolidated financial statements have been prepared on the historical cost basis except for the following:

- Derivative financial instruments are measured at fair value;

The methods used to measure fair values are discussed further in note 4.

The consolidated entity is of a kind referred to in ASIC Corporations (Rounding in Financial/Directors’ Reports) Instrument 2016/191 and in accordance with that instrument, all financial information presented in US dollars has been rounded to the nearest thousand unless otherwise stated.

### (c) Use of estimates and judgements

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

In particular, information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amount recognised in the financial statements are described in note 3 (d) – Exploration, evaluation properties and oil and gas properties, note 3(l) Rehabilitation provision and note 3 (q) – Income tax.

The estimated recoverable amount of oil and gas assets is based on discounted cash flow projections which are based on estimates and assumptions that are subject to change. Key assumptions include the ultimate prices realised on the sale of oil and gas and the reserves ultimately recovered. A sustained deterioration in prices or reduction in reserves may result in future asset impairments.

### (d) Going concern basis of preparation

The financial statements of the consolidated entity have been prepared on the basis of a going concern. The going concern basis of preparation assumes that an entity will realise its assets and discharge its liabilities in the normal course of business.

The directors have approved cash flow projections which support the going concern basis of preparation. The preparation of these projections incorporate a number of assumptions and judgements and include cash saving initiatives adopted across the group and the extension of the convertible note facility, as discussed in note 32. The Directors have concluded that the range of possible outcomes considered in preparing the cashflow projections do not give rise to a material uncertainty casting significant doubt on the Group’s ability to continue as a going concern.

The cash flow projections do not include the income and expenditure associated with the restart of production from the An Nayah Oilfield in Yemen and further drilling on the Hummer Gas/Oil Field in the USA.

# Notes to the Financial Statements

For the year ended 31 December 2017

## 3. Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements, and have been applied consistently by the Company and consolidated entity.

### (a) Basis of consolidation

#### (i) Subsidiaries

Subsidiaries are entities controlled by the Company. The Company controls an entity when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. The accounting policies of subsidiaries have been changed when necessary to align them with the policies adopted by the consolidated entity.

In the Company's financial statements, investments in subsidiaries are carried at cost, less accumulated impairments.

#### (ii) Joint operating arrangements

Joint operating arrangements are those legal entities over whose activities the consolidated entity has joint control, whereby the Company has rights to the assets and obligations for the liabilities relating to the arrangement. The interest of the consolidated entity in unincorporated joint operating arrangements and jointly operated assets are brought to account by recognising in its financial statements the Company's share of the arrangements underlying assets and liabilities, and the expenses it incurs and its share of income that it earns from the sale of goods or services by the joint arrangements.

#### (iii) Transactions eliminated on consolidation

Intra-group balances and any unrealised gains and losses or income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

#### (iv) Loss of control

Upon the loss of control, the consolidated entity derecognises the assets and liabilities of the subsidiary, any non-controlling interests and the other components of equity related to the subsidiary. Any surplus or deficit arising on the loss of control is recognised in profit or loss. If the consolidated entity retains any interest in the previous subsidiary, then such interest is measured at fair value at the date that control is lost. Subsequently, it is accounted for as an equity-accounted investee or as an available-for-sale financial asset depending on the level of influence retained.

### (b) Foreign currency

#### (i) Functional and presentation currency

Items included in the financial statements of each of the consolidated entity's subsidiaries are measured using the currency of the primary economic environment in which the subsidiary operates ("the functional currency"). The functional currency of the Company and its Australian subsidiaries is Australian dollars (A\$) and the functional currency of the Company's overseas subsidiaries is United States dollars (US\$).

The financial statements are presented in United States dollars. The consolidated entity believes the US dollar is the best measure of performance for Petsec Energy Ltd because oil and gas, the consolidated entity's dominant sources of revenue, are priced in US dollars and the consolidated entity's main operations are based in jurisdictions where most of the costs incurred are denominated in US dollars.

Prior to consolidation, the results and financial position of each entity within the group are translated from the functional currency into the group's presentation currency as follows:

- Assets and liabilities are translated at the closing rate at the date of that balance sheet;
- Income and expenses are translated at average exchange rates (unless this is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions);
- Components of equity are translated at the historical rates; and
- All resulting exchange differences are recognised as a separate component of equity.

#### (ii) Foreign currency transactions and balances

Foreign currency transactions are translated into the functional currency at the exchange rates prevailing at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated to the respective functional currency at the foreign exchange rate ruling at that date. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the statement of comprehensive income.

Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

Foreign exchange gains and losses arising from a monetary item receivable from or payable to a foreign operation, the settlement of which is neither planned nor likely in the foreseeable future, are considered to form part of a net investment in a foreign operation and are recognised directly in equity in the foreign currency translation reserve (FCTR).

### **(c) Derivative financial instruments and hedging activities**

The consolidated entity's revenues are exposed to changes in commodity prices. From time to time, the consolidated entity enters into derivative financial instruments to manage a portion of its oil and gas sales price risks.

The consolidated entity does not hold derivative financial instruments for speculative purposes.

Derivative financial instruments are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured to their fair value each reporting date. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. The consolidated entity designates certain derivatives as hedges of highly probable forecast transactions (cash flow hedges).

The consolidated entity documents at the inception of the transaction the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. The consolidated entity also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions have been and will continue to be highly effective in offsetting changes in fair values or cash flows of hedged items.

#### **(i) Cash flow hedge**

Changes in the fair value of the derivative-hedging instrument designated as a cash flow hedge are recognised directly in equity to the extent that the hedge is effective. To the extent that the hedge is ineffective, changes in fair value are recognised in the statement of comprehensive income.

If the hedging instrument no longer meets the criteria for hedge accounting, expires or is sold, terminated or exercised, then hedge accounting is discontinued prospectively. The cumulative gain or loss previously recognised in equity remains there until the forecast transaction occurs. When the hedged item is a non-financial asset, the amount recognised in equity is transferred to the carrying amount of the asset when it is recognised. In other cases the amount recognised in equity is transferred to the income statement in the same period that the hedged item affects profit or loss.

#### **(ii) Derivative financial instruments that do not qualify for hedge accounting**

Certain derivative financial instruments do not qualify for hedge accounting. Changes in the fair value of any derivative financial instrument that does not qualify for hedge accounting are recognised immediately in the statement of profit and loss.

Other derivative financial instruments are recognised initially at fair value; attributable transaction costs are recognised in profit or loss as incurred. Subsequent to initial recognition, derivatives are measured at fair value and changes therein are recognised immediately in profit or loss.

### **(d) Exploration, evaluation properties and oil and gas properties**

Exploration and evaluation expenditure is accumulated in respect of each separate area of interest. The consolidated entity's capitalisation policy for its natural gas and crude oil exploration and development activities is to capitalise expenditure of productive exploratory wells, development drilling and productive wells, and expenditure to acquire mineral interests. Exploration expenditure, including personnel costs, certain geological and geophysical expenses including seismic costs where exploration rights have not been obtained for oil and natural gas leases, are charged to expense as incurred. Exploratory drilling expenditures are initially capitalised, but charged to expense if and when the well is determined not to have found reserves in commercial quantities.

Exploration and evaluation expenditures relating to an area of interest are capitalised where exploration rights have been obtained. This expenditure is carried forward only to the extent that they are expected to be recouped through successful development and exploitation, or sale of the area, or where exploration and evaluation activities have not yet reached a stage which permits a reasonable assessment of the existence of economically recoverable reserves, and active and significant exploration operations are continuing. This expenditure is not subject to amortisation. Once management has determined the existence of economically recoverable reserves for an area of interest, expenditure is reclassified from exploration and evaluation to oil and gas properties on the balance sheet. Oil and gas properties are amortised using a units-of-production method, as further discussed in note 3(e).

Exploration and evaluation properties and oil and gas properties are assessed for impairment when facts and circumstances suggest that the carrying amount of the asset may exceed its recoverable amount. In the event that indicators of impairment are present, an impairment loss is recorded based on the higher of an asset's fair value less costs to sell and value in use (see note 3(g)). When an area of interest is abandoned or the directors decide that it is not commercial, any accumulated costs in respect of that area are written off in the financial period the decision is made.

#### **(e) Amortisation of oil and gas properties**

Oil and gas properties in the production phase are amortised on a units-of-production method based on the ratio of actual production to remaining proved and probable reserves (2P). Remaining 2P reserves are measured at the lower of 2P reserves estimated by external independent petroleum engineers and internal estimates.

Amortisation is not charged on costs carried forward in respect of areas of interest in the development phase until commercial production commences.

# Notes to the Financial Statements

For the year ended 31 December 2017

## 3. Significant accounting policies (continued)

### (f) Property, plant and equipment

#### (i) Recognition and measurement

Items of property, plant and equipment are measured at cost less accumulated depreciation and impairment losses.

Cost includes expenditures that are directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the asset to a working condition for its intended use, and the costs of dismantling and removing the items and restoring the site on which they are located. Purchased software that is integral to the functionality of the related equipment is capitalised as part of the equipment.

When parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items (major components) of property, plant and equipment.

Gains and losses on disposal of an item of property, plant and equipment are determined by comparing the proceeds from disposal with the carrying amount of property, plant and equipment and are recognised net within "other income" in profit and loss.

#### (ii) Leased assets

Leases in terms of which the consolidated entity assumes substantially all the risks and rewards of ownership are classified as finance leases. Lease payments are accounted for as described in accounting policy 3(n).

#### (iii) Subsequent costs

The cost of replacing part of an item of property, plant and equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the consolidated entity and its costs can be measured reliably. The costs of the day-to-day servicing of property, plant and equipment are recognised in the income statement as incurred.

#### (iv) Depreciation and amortisation

Depreciation of property, plant and equipment is recognised in the statement of comprehensive income on a straight-line basis over the estimated useful lives of each part of an item. Leased assets are depreciated over the shorter of the lease term and their useful lives. Assets are depreciated or amortised from the date of acquisition or, in respect of internally constructed assets, from the time an asset is completed and held ready for use.

Depreciation methods, useful lives and residual values are reassessed at the reporting date. When changes are made, adjustments are reflected prospectively in current and future periods only.

The estimated useful lives or the amortisation method used for each class of asset in the current and comparative periods are as follows:

	2017	2016
<b>Property, plant and equipment</b>		
Furniture and fittings	<b>5 – 8 years</b>	5 – 8 years
Office equipment	<b>3 – 4 years</b>	3 – 4 years
Leasehold improvements	<b>5 – 7 years</b>	5 – 7 years

### (g) Impairment – Non-financial assets

The carrying amounts of the consolidated entity's and the Company's non-financial assets, other than deferred tax assets (see note 3(q)), are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists then the asset's recoverable amount is estimated. For intangible assets that have indefinite lives or that are not yet available for use, recoverable amount is estimated at each reporting date.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. A cash-generating unit is the smallest identifiable asset group that generates cash flows that largely are independent from other assets or groups. Impairment losses are recognised in the income statement. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amount of the other assets in the unit (group of units) on a *pro rata* basis.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessment of the time value of money and the risks specific to the asset.

The measurement of recoverable amount for the consolidated entity's exploration, evaluation and oil and gas properties expenditure requires significant estimation and judgement. Note 12 provides further details of the key assumptions adopted by the consolidated entity in measuring the recoverable amounts of exploration, evaluation and oil and gas properties expenditure.

Impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.



### (h) Trade and other receivables

Trade receivables, which generally have 30-60 day terms, are recognised and carried at original invoice amount less an allowance for any uncollectible amounts.

An estimate for doubtful debts is made when collection of the full amount is no longer probable. Bad debts are written off when identified.

### (i) Cash and cash equivalents

Cash and cash equivalents in the balance sheet comprise cash at bank and on hand and short-term deposits with an original maturity of three months or less.

For the purposes of the Statement of Cash Flows, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts.

### (j) Interest-bearing loans and borrowings

All loans and borrowings are initially recognised at cost, being the fair value of the consideration received net of debt issue costs associated with the borrowing.

After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost using the effective interest method. Amortised cost is calculated by taking into account any issue costs, and any discount or premium on settlement.

### (k) Borrowing costs

Borrowing costs comprise interest payable on borrowings calculated using the effective interest rate method, lease finance charges, amortisation of discounts or premiums relating to borrowings, and the unwinding of discounts on the rehabilitation provisions. Borrowing costs relating to oil and gas properties under development are capitalised as a cost of development up to the date production commences. The actual borrowing costs are capitalised where funds are borrowed specifically for oil and gas properties under development. Borrowing costs on general funding are capitalised based on the weighted average borrowing rate.

### (l) Provisions

A provision is recognised if, as a result of a past event, the consolidated entity has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability.

Where discounting is used, the increase in the provision due to the passage of time is recognised as a finance cost.

### Rehabilitation

The consolidated entity recognises a provision for the legal obligation associated with the retirement of long-lived assets that results from the acquisition, construction, development, and (or) the normal operation of oil and natural gas properties. The initial recognition of a liability for rehabilitation, which is discounted using a risk-free interest rate, increases the carrying amount of the related long-lived asset by the same amount as the liability. In periods subsequent to initial measurement, period-to-period changes in the liability are recognised for the passage of time (unwinding of discount) as a borrowing cost. Additionally, the capitalised asset retirement cost is subsequently allocated to expense on a units-of-production basis over its estimated useful life.

Changes in the estimate of the liability arising from revised timing or estimated cost-to-complete the rehabilitation are recognised with a corresponding adjustment to the relevant long-lived asset.

The rehabilitation provision requires significant estimation and judgement. These estimates include:

- Expected method of remediation;
- Forecast costs-to-complete the future remediation; and
- Anticipated timing of the remediation work.

The consolidated entity monitors the estimates and judgements involved in measuring this provision.

### (m) Employee benefits and director benefits

#### (i) Short-term employee benefits

Liabilities for employee benefits for wages, salaries, annual leave, sick leave and bonuses represent present obligations resulting from employees' services provided to reporting date which are expected to be wholly settled by the Company within the next financial year. Such liabilities are calculated at undiscounted amounts based on remuneration wage and salary rates that the consolidated entity expects to pay as at reporting date including related on-costs, such as workers' compensation insurance and payroll tax.

#### (ii) Long-term employee benefits

The provision for employee benefits for long service leave represents the present value of the estimated future cash outflows to be made resulting from employees' services provided to reporting date.

The provision is calculated using expected future increases in wage and salary rates including related on-costs and expected settlement dates based on turnover history and is discounted using the rates attaching to national government bonds at reporting date which most closely match the terms of maturity of the related liabilities.

#### (iii) Defined contribution pension plans

The Company and other controlled entities contribute to several defined contribution pension plans. Obligations for contributions to defined contribution pension plans are recognised as an expense in the statement of comprehensive income when they are due.

# Notes to the Financial Statements

For the year ended 31 December 2017

## 3. Significant accounting policies (continued)

### (m) Employee benefits and director benefits (continued)

#### (iv) Share-based compensation transactions

Share-based compensation benefits are provided to employees of the consolidated entity, including directors, via the Company's Employee Option Plan and Employee Share Plan.

The grant date fair value of options granted to employees is recognised as an employee expense, with a corresponding increase in equity, over the period in which the employees become unconditionally entitled to the options.

### (n) Leases

Leases in terms of which the consolidated entity assumes substantially all the risks and rewards of ownership are classified as finance leases. Upon initial recognition the leased asset is measured at an amount equal to the lower of its fair value and the present value of the minimum lease payments. Subsequent to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to that asset.

Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly against income.

Leases where the lessor retains substantially all the risks and benefits of ownership of the asset are classified as operating leases. Operating lease payments are recognised as an expense in the statement of profit and loss on a straight-line basis over the lease term. Lease incentives received are recognised as an integral part of the total lease expense, over the term of the lease.

### (o) Revenue and other income recognition

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the consolidated entity and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

#### Sale of oil and gas

Revenues from the sale of oil and gas is recognised when the product is in the form in which it is to be delivered and an actual physical quantity has been provided or allocated to a purchaser pursuant to a contract. Revenue from oil and gas sales is measured at the fair value of the consideration receivable.

Revenue from oil and gas royalties is recognised on an accrual basis in accordance with the terms of underlying royalty agreements. Revenue from oil and gas royalties is measured at the fair value of the consideration receivable.

#### Sale of non-current assets

Gains or losses on sale of non-current assets are recognised as other income at the date control of the asset passes to the buyer, usually when an unconditional contract of sale is signed.

#### Interest income

Interest income is recognised as the interest accrues (using the effective interest method, which is the rate that discounts estimated future cash receipts through the expected life of the financial instrument).

### (p) Earnings per share

The consolidated entity presents basic and diluted earnings per share (EPS) data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Company by the weighted average number of ordinary shares outstanding during the period. Diluted EPS is determined by adjusting the profit or loss attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares, which comprise share options granted to employees.

### (q) Income tax

Income tax expense comprises current and deferred tax. Income tax expense is recognised in the statement of comprehensive income except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for the following temporary differences: the initial recognition of assets or liabilities that affect neither accounting nor taxable profit nor differences relating to investments in subsidiaries to the extent that they will probably not reverse in the foreseeable future. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which the temporary difference or tax losses can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

### (r) Segment reporting

An operating segment is a distinguishable component of the consolidated entity whose information is reviewed regularly by the CEO, the consolidated entity's chief decision making officer, and that is engaged in providing related products or services which are subject to risk and rewards that are different to other segments.

### (s) Changes in accounting policies

The consolidated entity has consistently applied the accounting policies set out in note 3(a) through (r) to all periods presented in these consolidated financial statements.

### (t) New standards and interpretations not yet adopted

A number of new standards, amendments to standards and interpretations are effective for annual periods beginning after 1 January 2018, and have not been applied in preparing these consolidated financial statements. Those which may be relevant to the consolidated entity are set out below. The consolidated entity does not plan to adopt these standards early.

#### (i) AASB 9 Financial Instruments

AASB 9, published in July 2014, replaces the existing guidance in AASB 139 *Financial Instruments: Recognition and Measurement*. AASB 9 includes revised guidance on the classification and measurement of financial instruments, including a new expected credit loss model for calculating impairment on financial assets, and the new general hedge accounting requirements. It also carries forward the guidance on recognition and derecognition of financial instruments from AASB 139.

AASB 9 is effective for annual reporting periods beginning on or after 1 January 2018, with early adoption permitted.

The consolidated entity does not expect a material impact on its consolidated financial statements resulting from the application of AASB 9.

#### (ii) AASB 15 Revenue from Contracts with Customers

AASB 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaces existing revenue recognition guidance, including AASB 118 *Revenue* and AASB 111 *Construction Contracts*.

AASB 15 is effective for annual reporting periods beginning on or after 1 January 2018, with early adoption permitted.

The consolidated entity does not expect a material impact on its consolidated financial statements resulting from the application of AASB 15.

The consolidated entity is assessing the impact to its consolidated financial statements resulting from the application of AASB9/15 and does not expect a material change.

#### (iii) AASB 16 Leases

AASB 16 *Leases* amends the accounting for leases. Lessees will be required to bring all leases on Balance Sheet as the distinction between operating and financing leases has been eliminated. Lessor accounting remains largely unchanged.

AASB 16 is effective for annual reporting periods beginning on or after 1 January 2019, with early adoption permitted if adopted in conjunction with AASB 15 for the same accounting period.

The consolidated entity will continue to assess the potential impact on its consolidated financial statements resulting from the application of AASB 16.

## 4. Determination of fair values

A number of the consolidated entity's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes based on the following methods. The Company has applied fair value methodologies that approximate the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Where applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

### Derivative Instruments

The fair values of derivative instruments are initially recognised at fair value on the date at which the derivative contracts are entered into and subsequently remeasured to fair value. On subsequent revaluation the derivatives are carried as assets when their fair value is positive and liabilities when their fair value is negative.

When the fair values of financial assets and financial liabilities recorded in the statement of financial position cannot be measured based on quoted prices in active markets, their fair value is measured using valuation techniques including discounted cash flow models. The inputs to these models are taken from observable markets where possible, but where this is not feasible, a degree of judgement is required in establishing fair values. Judgements include considerations of inputs such as liquidity risk, credit risk and volatility. Changes in assumptions relating to these factors could affect the reported fair value of financial instruments.

### Equity securities

The fair value of equity securities (level 3 category instruments) is determined using an option pricing model - the Black-Scholes-Merton formula - in arriving at an expected present value for options granted by the consolidated entity at period end. Measurement inputs include observable inputs, such as the share price on the measurement date, the exercise price of the instrument, share price target and the risk-free interest rate (based on government bonds), as well as unobservable inputs, such as expected volatility, expected term of the instruments, and expected dividends which represent management's best estimates at period end.

## Notes to the Financial Statements

For the year ended 31 December 2017

### 5. Other income and expenses

	2017 US\$'000	2016 US\$'000
<b>Other income and expenses</b>		
Production and project overhead income	18	70
Net foreign exchange gains	6	133
Net loss on disposal of property, plant and equipment	-	(7)
	<b>24</b>	196

### 6. Employee expenses

	2017 US\$'000	2016 US\$'000
Wages and salaries	2,044	1,486
Service agreements for executives	1,479	1,312
Bonuses	-	23
Contract labour	201	1,055
Superannuation & 401(k) plans	69	84
Share-based payment compensation	22	23
Other employee-related expenses	187	151
	<b>4,002</b>	4,134

### 7. Auditor's remuneration

	2017 US\$	2016 US\$
<b>Audit services:</b>		
<b>Auditors of the Company</b>		
KPMG Australia		
Audit and review of financial reports	105,500	90,375
KPMG UAE		
Audit of financial reports	12,720	12,000
	<b>118,220</b>	102,375

### 8. Finance income and expense

	2017 US\$'000	2016 US\$'000
Interest income - Other parties	47	23
Financial income	47	23
Interest expense	(309)	(674)
Unwinding of discount	(12)	(104)
Financial expense	(321)	(778)
Net financial income/(expense)	<b>(274)</b>	(755)



## 9. Income tax expense

	2017 US\$'000	2016 US\$'000
<b>Recognised in the statement of comprehensive income</b>		
<b>Deferred tax expense</b>		
Origination and reversal of temporary differences	-	-
Total income tax benefit/(expense) in the statement of comprehensive income	-	-
<b>Numerical reconciliation between tax expense and pre-tax net profit/(loss)</b>		
Profit/(loss) before tax	<b>(11,964)</b>	(13,024)
Income tax expense/(benefit) using the Australian corporation tax rate of 30% (2016: 30%)	<b>(3,589)</b>	(3,907)
Increase/(decrease) in income tax expense due to:		
Non-deductible expenses	<b>2,611</b>	2,407
Non-Australian income taxes assessed at different rate	<b>(147)</b>	(254)
Deferred tax movements not brought to account in current year	<b>1,125</b>	1,754
Under/(over) provided in prior years	-	-
Income tax expense/(benefit) on pre-tax net profit/(loss)	-	-

## 10. Earnings per share

The Company has only one type of security, being ordinary shares, included in the basic earnings per share calculation.

As at 31 December 2017, there were 3,700,000 (2016: 6,700,000) share options in Petsec Energy Ltd on issue under the Employee Share Plan ("ESP") and 1,000,000 (2016: Nil) options over ordinary shares in Petsec Energy Ltd on issue under the Employee Option Plan ("EOP").

During the year:

1. No share options were issued under the ESP (2016: 800,000) and 3,000,000 share options were cancelled (2016: Nil).
2. 1,000,000 options over ordinary shares were granted (2016: Nil) under the EOP. No share options were exercised or forfeited.

In determining potential ordinary shares, no share options or options over ordinary shares are dilutive (2016: Nil).

### Basic earnings/(loss) per share

The calculation of basic earnings/(loss) per share at 31 December 2017 was based on the loss attributable to ordinary shareholders of US\$11,964,000 (2016: Loss of US\$13,024,000) and a weighted average number of ordinary shares outstanding during the year ended 31 December 2017 of 313,345,217 (2016: 234,899,502), calculated as follows:

### Profit/(loss) attributable to ordinary shareholders

	2017 US\$'000	2016 US\$'000
Profit/(loss) for the period	<b>(11,964)</b>	(13,024)

### Weighted average number of shares (basic)

<i>In thousands of shares</i>	2017	2016
Issued ordinary shares at 1 January	<b>287,382</b>	224,762
Effect of shares issued in 2017 and 2016, respectively	<b>25,963</b>	10,138
Weighted average number of ordinary shares at 31 December	<b>313,345</b>	234,900

### Earnings/(loss) per share In USD cents

<i>In US cents</i>	2017	2016
Basic and diluted earnings/(loss) per share	<b>(3.8)</b>	(5.5)

# Notes to the Financial Statements

For the year ended 31 December 2017

## 11. Trade and other receivables

	2017 US\$'000	2016 US\$'000
<b>Current</b>		
Trade receivables	474	454
Other receivables	50	4,112
	<b>524</b>	4,566

## 12. Oil and gas, and exploration and evaluation properties

	2017 US\$'000	2016 US\$'000
<b>(a) Oil and gas properties</b>		
Balance at 1 January	16,810	6,443
Additions <sup>1</sup>	2,362	2,969
Capitalised interest <sup>2</sup>	1,308	141
Reclass from exploration and evaluation properties	-	8,250
Dry hole and impairment expense	(3,439)	(719)
Current year amortisation expense	(1,362)	(274)
Balance at 31 December	<b>15,679</b>	16,810
<b>(b) Exploration and evaluation properties</b>		
Balance at 1 January	358	6,556
Additions	-	2,573
Reclass to oil and gas properties	-	(8,250)
Dry hole and impairment expense	(358)	(521)
Balance at 31 December	<b>-</b>	358

1 The Company has renegotiated the acquisition of all the shares of West Yemen Oil (Block S-1), Inc. (formerly TG West Yemen Inc.), a wholly owned subsidiary of TransGlobe Energy Corporation ("TransGlobe"), which holds a 25% working interest in Block S-1. As a result of the negotiation, the 2nd tranche of the acquisition price was reduced by US\$1,375,000 in return for Petsec agreeing to pay TransGlobe US\$500,000 after 500,000 barrels have been produced from Block S-1.

2 Interest has been capitalised on specific borrowings in respect of oil and gas properties under development.

### Recoverable amount

The ultimate recoupment of costs carried forward for exploration and evaluation phases is dependent on the successful development and commercial exploitation or sale of the respective areas.

The estimated recoverable amount of all cash generating units in the development and production phases is determined by discounting the estimated future cash flows to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the assets. The consolidated entity utilises discounted future cash flows as estimated by independent petroleum engineers for this assessment.

The key assumptions used include:

- Estimated proved and probable reserves (2P reserves);
- For wells now in production - initial production rates based on current producing rates for those wells;
- For wells not currently in production - initial production rates based on test data and other related information;
- Estimated rates of production decline based on current trends;
- Hydrocarbon prices that the consolidated entity estimates to be reasonable taking into account historical prices, current prices, and prices used in making its exploration and development decisions;
- Operating costs directly applicable to the leases or wells and allocation of corporate overheads;
- Development costs based on authorisations for expenditure for the proposed work or actual costs for similar projects;
- Pre-tax discount rate of 10%.

### Risk of future impairments

- The determination of the estimated recoverable amount of Petsec's producing oil and gas properties is highly sensitive to a change in estimated recoverable reserves, oil and gas prices, discount rates and cost allocations.
- As a result of historical impairments, certain properties are carried at recoverable amounts. Consequently any reduction in recoverable reserves or a reduction in the oil or gas price may trigger the need for further impairment on these specific properties.

### Dry hole and impairment expense

The estimated recoverable amount of all oil and gas assets is based on value in use discounted cash flow projections that are based on a range of estimates and assumptions that are subject to change. Key assumptions include the ultimate prices realised on the sale of oil and gas and the reserves ultimately recovered. A sustained deterioration in prices or reduction in reserves may result in further future asset impairments.

During the current period, the consolidated entity recognised an impairment provision of US\$3,988,000 against its Block S-1 and Block 7, Yemen assets due to the inability to recommence production and activities in Yemen as a result of the ongoing conflict. This impairment provision may be reversed in the future once a successful resolution to the conflict is achieved and production at the An Nayah Oilfield has been restarted.

In the previous corresponding period, the consolidated entity recognised total dry hole and impairment expense of US\$1,203,000 mainly in relation to impairment recognised against the Adeline Sugar Factory No. 4 well due to well performance and an undrilled exploration prospect.

## 13. Deferred tax assets

### Deferred tax assets and liabilities

	Assets		Liabilities		Net	
	2017 US\$'000	2016 US\$'000	2017 US\$'000	2016 US\$'000	2017 US\$'000	2016 US\$'000
Exploration, evaluation and development expenditure	<b>3,232</b>	3,232	-	-	<b>3,232</b>	3,232
Other items	<b>60</b>	49	-	-	<b>60</b>	49
Deferred tax balances not brought to account	<b>(3,292)</b>	(3,281)	-	-	<b>(3,292)</b>	(3,281)
Deferred tax assets/(liabilities)	-	-	-	-	-	-

### Unrecognised deferred tax assets

Deferred tax assets have not been recognised in respect of the following items:

	2017 US\$'000	2016 US\$'000
Deductible temporary differences in USA	<b>3,292</b>	3,281
Tax operating loss carry-forwards in USA	<b>39,122</b>	33,859
Deductible temporary differences in Canada	<b>1,717</b>	1,717
Tax operating loss carry-forwards in Canada	<b>232</b>	231
Deductible temporary differences in Australia	-	15
Tax operating loss carry-forwards in Australia	<b>3,514</b>	2,730
	<b>47,877</b>	41,833

## Notes to the Financial Statements

### For the year ended 31 December 2017

#### 13. Deferred tax assets (continued)

Under Australian Accounting Standards, the consolidated entity is required to assess at each reporting period, the extent to which deferred tax assets in respect of the carry-forward of unused tax losses and temporary differences qualify for recognition on the balance sheet based on current facts and circumstances, including projected future taxable profits.

Historically, no deferred tax assets have been recognised in relation to the Australian operations as they do not qualify for recognition of deferred tax assets until such time that it is probable that future taxable profits will be available against which unused tax losses and temporary differences in the relevant tax jurisdictions can be utilised.

The deductible temporary differences and tax losses in Australia do not expire under current tax legislation though these losses are subject to testing under loss recoupment rules, in order for them to be utilised. USA and Canada loss carry forwards begin to expire in 2021 and later.

#### Movement in temporary differences during the year

	Balance 1 Jan 16 US\$'000	Recognised in income US\$'000	Recognised in equity US\$000	Balance 31 Dec 16 US\$'000
Exploration and evaluation expenditure	3,848	(616)	-	3,232
Other items	42	7	-	49
Deferred tax balances not brought to account	(3,890)	609	-	(3,281)
	-	-	-	-

	Balance 1 Jan 17 US\$'000	Recognised in income US\$'000	Recognised in equity US\$000	Balance 31 Dec 17 US\$'000
Exploration and evaluation expenditure	<b>3,232</b>	-	-	<b>3,232</b>
Other items	<b>49</b>	<b>11</b>	-	<b>60</b>
Deferred tax balances not brought to account	<b>(3,281)</b>	<b>(11)</b>	-	<b>(3,292)</b>
	-	-	-	-

#### 14. Trade and other payables

	2017 US\$'000	2016 US\$'000
<b>Current</b>		
<b>Trade and other payables, stated at cost</b>		
Trade payables	<b>264</b>	2,892
Exploration and evaluation accruals	-	200
Operational and administration accruals	<b>2,694</b>	9,054
Related party payables	<b>204</b>	83
	<b>3,162</b>	12,229
<b>Non-current</b>		
Operational and administration accruals	<b>3,699</b>	-
	<b>3,699</b>	-

#### 15. Interest bearing loans and borrowings

	2017 US\$'000	2016 US\$'000
<b>Non-current</b>		
Secured borrowings - convertible notes	<b>5,568</b>	3,299
	<b>5,568</b>	3,299

#### Secured borrowings - convertible notes

Secured borrowings represent the outstanding balance at 31 December 2017 under a convertible note facility with Republic Investment Management and associates in Singapore, managed through the registrar Sing Rim Pte Ltd of Singapore. The consolidated entity entered into a US\$15 million facility in August 2016.



The key terms and conditions of the convertible note facility as set out in the secured convertible notes Deed Poll dated 23 August 2016 (subsequently amended by a Deed of Variation dated 14 September 2016 and Letter of Variation dated 28 December 2016, Letter of Variation dated 30 March 2017, and Letter of Variation dated 17 August 2017) are as follows:

- (a) Facility amount – US\$15 million.
- (b) Facility drawdown – available in three tranches of US\$5 million each.
- (c) Facility term – the convertible note facility had an initial redemption date of 31 December 2017. The Letter of Variation dated 28 December 2016 resulted in the redemption date being amended from 31 December 2017 to 5 July 2018. The Letter of Variation dated 17 August 2017 extended the redemption date from 5 July 2018 to 23 January 2019.
- (d) Interest – interest accrues daily at 10% per annum for the period through 31 December 2017, compounded monthly on the drawn amount, with interest capitalising into the principal amount of the convertible notes. The Letter of Variation dated 28 December 2016 resulted in the interest rate increasing from 10% to 12.5% per annum for the period of the extension of the redemption date from 1 January 2018 to 5 July 2018. The Letter of Variation dated 17 August 2017 resulted in the interest rate of 12.5% per annum continue from 5 July 2018 to 23 January 2019.
- (e) Security – the convertible notes constitute unsubordinated and secured obligations of the Company. The Company and the registrar entered into a general security deed on 23 August 2016 under which the Company granted the registrar a general security interest over all of the Company's assets as security for the Company's obligations under the convertible notes. In addition, the Company granted the registrar mortgages over certain assets of its U.S. subsidiaries.
- (f) Conditions precedent to issue – the convertible notes are subject to a number of conditions precedent to issue, as follows:
  - (i) Tranche 1. US\$5 million may be issued no later than 31 December 2016. There are no outstanding conditions precedent for this Tranche. As at 31 December 2017, the consolidated entity had issued convertible notes for a face value of US\$5 million under this Tranche;
  - (ii) Tranche 2. US\$5 million may be issued no later than 5 January 2018, as follows:
    - (A) US\$2 million may be issued upon clear indication that oil has commenced to flow freely within the Republic of Yemen, shipped and sold, which will be prima facie evidenced by the Yemen companies, Safer and Jana Hunt having produced and transported through the Marib pipeline and shipped and sold no less than 500,000 barrels of oil per month over a two month period;
    - (B) US\$2 million may be issued in parcels of US\$500,000 for each 50,000 barrels of oil net to the Company which has been produced, transported, and stored at the shipping terminal, ready for sale; and
    - (C) US\$1 million may be issued in US\$500,000 parcels for each 50,000 barrels of oil net shipped and sold.

(iii) Tranche 3. US\$5 million may be issued no later than 5 January 2018, as follows:

- (A) US\$500,000 may be issued for each 50,000 barrels net to the Company, produced, transported, shipped and sold, in excess of the 100,000 barrels of crude per month anticipated in Tranche 2.
- (g) Conversion to Petsec Energy Ltd shares – the noteholder will be entitled to convert up to 50% of the outstanding amount of the convertible notes into shares, by delivering a conversion notice at any time prior to the maturity date. The maximum number of shares issued on conversion is restricted to 46 million shares provided that this number is less than 19.9% of the issued capital or potential issued capital of the Company.
- (h) Conversion price – each convertible note will convert into shares at conversion prices ranging from A\$0.15 to A\$0.30 per Share (as amended on 28 December 2016), as follows:
  - (A) Tranche 1: Interest – A\$0.15/share;
  - (B) Tranche 1: Principal (up to 50% may be converted) – A\$0.15/share;
  - (C) Tranche 2: Principal and interest (up to 50% may be converted) – A\$0.25/share; and
  - (D) Tranche 3: Principal and interest (up to 50% may be converted) – A\$0.30/share.

In accordance with the terms of the Deed Poll, the Company issued 5 million shares at A\$0.20/share on 17 October 2016, being the facility fee shares, to the Registrar of the secured convertible note facility. On 15 March 2017, the Company issued 5 million shares at A\$0.15/share to the Registrar under the Letter of Variation dated 28 December 2016 as a fee for extending the maturity date of the facility from 31 December 2017 to 5 July 2018. On 4 September 2017, the Company issued a further 5 million shares at A\$0.10/share to the Registrar under the Letter of Variation dated 17 August 2017 as a fee for extending the maturity date of the facility from 5 July 2018 to 23 January 2019.

The Deed of Variation dated 13 September 2016 amends terms to ensure compliance of the facility with ASX listing rules.

A waiver from ASX Listing Rule 7.3.2 was granted to the Company on 21 October 2016 to allow the Company to issue the convertible notes under the convertible note facility and for their conversion into ordinary shares, at any time up to 31 December 2017. Due to the variation of the terms of the convertible note facility since 28 December 2016, the Company can no longer rely upon the shareholder approval that was obtained at the Extraordinary General Meeting held on 1 December 2016 under ASX Listing Rule 7.1 for the issue and subsequent conversion of the convertible notes into fully paid ordinary shares, at any time up to 31 December 2017.

The Company is therefore required to seek shareholder approval under Listing Rule 7.1 for the conversion of the convertible notes, that have been issued under Tranche 1 of the facility, into ordinary shares, and intends to seek this approval at the May 2018 Annual General Meeting.

Tranches 2 and 3 of the facility which were not drawn down, were allowed to lapse at the expiry date of 5 January 2018, due to the delay in the restart of the An Nayah Oilfield in Yemen.

As discussed in note 32, the Company entered into an agreement with the Registrar subsequent to balance date to extend the redemption date of the facility and to reinstate Tranche 2 of the facility.

## Notes to the Financial Statements

For the year ended 31 December 2017

### 16. Fair value of financial derivative instruments

	2017 US\$'000	2016 US\$'000
<b>Non-current</b>		
Fair value of financial derivatives	178	764
	<b>178</b>	<b>764</b>

The fair value of the financial derivative instrument of US\$178,000 represents the embedded derivative component within the secured convertible note (refer note 15).

Embedded derivatives are separated from the host contract and accounted for separately if certain criteria are met.

Derivatives are initially valued at fair value; subsequent to initial recognition, derivatives are measured at fair value, and changes therein are recognised in profit and loss.

The fair value of the financial derivative was determined at initial recognition and subsequent reporting dates using a Monte Carlo model.

### 17. Employee benefits

#### (a) Superannuation/pension plans

The consolidated entity contributes to several defined contribution employee superannuation plans in Australia. Employer contributions are based on various percentages of their gross salaries. The consolidated entity is under no legal obligation to make contributions in excess of those specified in Superannuation Industry (Supervision) legislation. The amount recognised, as expense was, US\$38,000 for the year ended 31 December 2017 (2016: US\$36,000).

U.S. based employees are eligible to participate in a voluntary retirement savings plan under Section 401(k) of the US tax code ("401(k) plan"). Employer matching contributions under the 401(k) plan recognised as an expense was US\$31,000 for the year ended 31 December 2017 (2016: US\$48,000).

#### (b) Share-based payments

The Employee Share and Employee Option Plans, established by shareholder resolutions on 29 November 1994, provide for employees, executives and directors to be granted ordinary shares or options over ordinary shares at the discretion of the Nomination and Remuneration Committee.

##### Employee Share Plan

The following sets forth the share-based compensation transactions under the Company's Employee Share Plan ("ESP").

The number and weighted average share price, is as follows:

	Weighted average exercise price 2017	Number of shares 2017	Weighted average exercise price 2016	Number of shares 2016
Outstanding at the beginning of the period	A\$0.20	6,700,000	A\$0.20	5,900,000
Granted during the period <sup>1</sup>	-	-	A\$0.20	800,000
Forfeited during the period	A\$0.20	(3,000,000)	-	-
Outstanding at the end of the period	A\$0.20	3,700,000	A\$0.20	6,700,000

<sup>1</sup> Shares vest between 24 February 2017 - 24 February 2020 at a minimum share price of between A\$0.25-A\$0.40.

During the current year, no shares were granted under the Company ESP to employees as long term incentive compensation (2016: 800,000).

### Employee Option Plan

The following sets forth the share-based compensation transactions under the Company's Employee Option Plan ("EOP"). The number and weighted average exercise prices of options over ordinary shares, is as follows:

	Weighted average exercise price 2017	Number of options 2017	Weighted average exercise price 2016	Number of options 2016
Outstanding at the beginning of the period	-	-	-	-
Granted during the period	<b>A\$0.20</b>	<b>1,000,000</b>	-	-
Exercised during the period	-	-	-	-
Forfeited during the period	-	-	-	-
Outstanding at the end of the period	<b>A\$0.20</b>	<b>1,000,000</b>	-	-
Exercisable at the end of the period	-	-	-	-

At 31 December 2017, there were 1,000,000 options over ordinary shares outstanding (2016: Nil). During the year, 1,000,000 options were granted (2016: nil). No options were exercised or forfeited (2016: nil).

### Share and option grants to key management personnel

Grants of 1,000,000 options over ordinary shares were made to key management personnel during the year ended 31 December 2017 (2016: 800,000).

The following table summarises the fair value assumptions of options and shares granted to key management personnel during the years ended 31 December 2017 and 2016, respectively.

	Key management personnel 2017	Key management personnel 2016
Weighted average fair value at measurement date	<b>A\$0.005</b>	A\$0.005
Weighted average share price	<b>A\$0.097</b>	A\$0.09
Weighted average exercise price	<b>A\$0.20</b>	A\$0.20
Expected volatility (expressed as weighted average used in the modelling under Black-Scholes model)	<b>76.32%</b>	58.1%
Expected option life (expressed as weighted average used in the modelling under Black-Scholes model)	<b>1.72 years</b>	4.5 years
Expected dividends	-	-
Risk-free interest rate (based on national government bonds)	<b>2.01%</b>	1.75%

The expected volatility is based on historic volatility (calculated based on the weighted average remaining life of the shares and options), adjusted for any expected changes to future volatility due to publicly available information.

## 18. Rehabilitation provisions

	2017 US\$'000	2016 US\$'000
<b>Current</b>		
Balance at 1 January	<b>546</b>	2,573
Provisions used during the year	-	(2,125)
Change in provision estimate	<b>(546)</b>	-
Unwind of discount	-	98
Balance at 31 December	-	546
<b>Non-current</b>		
Balance at 1 January	<b>68</b>	61
Provisions made during the year	<b>99</b>	-
Unwind of discount	<b>12</b>	7
Balance at 31 December	<b>179</b>	68
	<b>179</b>	614

# Notes to the Financial Statements

## For the year ended 31 December 2017

### 19. Capital and reserves

#### Share capital

In thousands of shares	Ordinary Shares	
	2017	2016
On issue at 1 January	287,382	234,662
Shares issued	37,906	56,720
Shares cancelled	(3,000)	(4,000)
On issue at 31 December – fully paid <sup>1</sup>	322,288	287,382

<sup>1</sup> Shares on issue amount at 31 December 2017 includes 3,700,000 share options held by the trustee under the Employee Share Plan (2016: 6,700,000).

The Company does not have authorised capital or par value in respect of its issued shares.

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Company.

#### Translation reserve

The translation reserve comprises all foreign currency differences arising from the translation of the financial statements of operations where their functional currency is different to the presentation currency of the reporting entity.

#### Option reserve

The option reserve comprises the fair value of options to be issued as an underwriting fee in relation to the fully underwritten rights issue.

#### Share-based compensation

The share-based compensation represents the value of unvested options issued under the Company's Employee Option Plan. The value of vested options are transferred to share capital on vesting.

#### Capital management

The Board's policy is to maintain an appropriate capital base to sustain future development of the consolidated entity. This capital base may comprise equity and borrowings.

Neither the Company nor any of its subsidiaries are subject to externally imposed capital requirements.

## 20. Risk management framework and additional financial instruments disclosures

#### Risk Management Framework

The Board of Directors has overall responsibility for the establishment and oversight of the risk management framework. There is no separate risk management committee.

Risk management policies are established to identify and analyse the risks faced by the consolidated entity, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the consolidated entity's activities. The consolidated entity, through their training and management standards and procedures, aim to develop a disciplined and constructive control environment in which all employees understand their roles and obligations.

The forecast financial position of the consolidated entity is continually monitored and derivative financial instruments can be used to hedge exposure to fluctuations in commodity prices (refer to *Commodity Price Risk* below for further details).

The Board oversees how management monitors compliance with the consolidated entity's risk management policies and procedures and reviews the adequacy of the risk management framework in relation to the risks faced by the consolidated entity.

#### Additional financial instruments disclosures

##### Overview

The consolidated entity has exposure to the following risks from its use of financial instruments:

- Credit risk
- Liquidity risk
- Market risk

This note presents information about the consolidated entity's exposure to each of the above risks, their objectives, policies and processes for measuring and managing risk, and the management of capital. Further quantitative disclosures are included throughout this financial report.

##### Credit risk

Credit risk represents the loss that would be recognised if counterparties failed to perform as contracted. The credit risk on financial assets of the consolidated entity that have been recognised is the carrying amount, net of any provision for doubtful debts. The consolidated entity has assessed that the counterparty's credit ratings determined by a recognised ratings agency remains acceptable.



### Exposure to credit risk

The carrying amount of the consolidated entity's financial assets represents the maximum credit exposure. The consolidated entity's maximum exposure to credit risk at the reporting date was:

	Consolidated	
	2017 US\$'000	2016 US\$'000
Cash and restricted cash deposits	3,486	13,077
Trade and other receivables	524	4,566
	<b>4,010</b>	17,643

As at 31 December 2017, exposure to credit risk in relation to cash held by banks was managed with the equivalent of US\$2.5 million being held with Australian financial institutions rated AA and the remaining balances held in the USA with institutions rated A or higher.

Where possible, the consolidated entity manages its credit risk on trade receivables by dealing with only large reputable customers for its oil and gas sales. At balance date, 100% of trade receivable were due from three such customers. The consolidated entity does not consider there to be any impairment indicators associated with these debtors. The consolidated entity's credit risk is limited to the carrying value of its financial assets. None of the consolidated entity's receivables are materially past due (2016: is consistent with 2017).

### Liquidity risk

Liquidity risk is the risk that the consolidated entity will not be able to meet its financial obligations as they fall due. The consolidated entity's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the consolidated entity's reputation.

Ultimate responsibility for liquidity risk management rests with the Board of Directors. The consolidated entity manages liquidity risk by monitoring of future rolling cash flow forecasts. These reflect management's expectations of the settlement of financial assets and liabilities.

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

#### 31 December 2017

	Carrying amount US\$000	Contractual cashflows				
		6 mths or less US\$000	6 - 12 mths US\$000	1 - 2 years US\$000	2 - 5 years US\$000	5 years or more US\$000
Trade and other payables	6,861	3,162	-	3,699	-	-
Secured borrowings	5,568	-	-	6,394	-	-
Total	12,429	3,162	-	10,093	-	-

#### 31 December 2016

	Carrying amount US\$000	Contractual cashflows				
		6 mths or less US\$000	6 - 12 mths US\$000	1 - 2 years US\$000	2 - 5 years US\$000	5 years or more US\$000
Trade and other payables	12,229	12,229	-	-	-	-
Secured borrowings	3,299	-	-	5,434	-	-
Total	15,528	12,229	-	5,434	-	-

### Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, commodity prices, interest rates will affect the consolidated entity's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return.

# Notes to the Financial Statements

For the year ended 31 December 2017

## 20. Risk management framework and additional financial instruments disclosures (continued)

### Foreign exchange risk

During 2016 and 2017, operating costs were incurred in US, Australian and Canadian dollars, Arab Emirates Dirham and Yemeni Rials.

Throughout 2016 and 2017, the consolidated entity held the majority of its liquid funds in US dollars.

Fluctuations in the Australian dollar/US dollar exchange rate have impacted the underlying performance of the consolidated entity. The consolidated entity's policy is not to hedge the Australian dollar/US dollar exchange rate risk as income (cash inflows) and expenses (cash outflows), are predominantly denominated in US dollars, with the exception of Australian dollar denominated equity funding, consequently surplus funds are primarily held in US dollars. The impact of Arab Emirates Dirham, Canadian dollars and Yemeni Rials was not material.

### Commodity price risk

The revenue and income of the consolidated entity are affected by changes in natural gas and crude oil prices, and from time to time various financial transactions (swap contracts and collar contracts involving NYMEX commodity prices for natural gas and crude oil) may be undertaken to reduce the effect of these changes. The consolidated entity ensures that it has sufficient proved reserves of these commodities to cover all these transactions and it only enters into such derivatives to match its anticipated underlying physical production and reserves. The consolidated entity also limits the term of the transactions and the percentage of the Company's expected aggregate oil and natural gas production that may be hedged at any time.

### Swaps

In a natural gas swap agreement the consolidated entity receives from the counterparty the difference between the agreed contracted fixed price and the quoted or published reference settlement price if the latter is lower than the fixed price. If the reference settlement price is higher than the agreed fixed price, the consolidated entity will pay the difference to the counterparty.

### Collars

In a collar agreement, a floor price and a ceiling price are established. If there is no cash outlay upon entering a collar arrangement, it is called a "costless" or "cashless" collar. If quoted reference prices at the specified date (expiration date) are lower than the floor price, then the counterparty pays the price difference multiplied by the notional quantity to the consolidated entity. If the quoted reference prices at the specified date are higher than the ceiling price, then the consolidated entity pays the price difference multiplied by the notional quantity to the counterparty.

At 31 December 2017, the consolidated entity had no outstanding oil or natural gas hedges in place (previous corresponding period: Nil).

### Interest rate risk

The consolidated entity's exposure to market interest rates primarily relates to the consolidated entity's cash holdings (2016: cash holdings).

The financial instruments exposed to interest rate risk are as follows:

	2017 US\$'000	2016 US\$'000
<b>Financial assets</b>		
Cash and restricted cash deposits	<b>3,486</b>	13,077
	<b>3,486</b>	13,077

### Sensitivity analysis

In managing commodity price and interest rate risks the consolidated entity aims to reduce the impact of short-term fluctuations on the consolidated entity's earnings. However, credit considerations limit the amount of hedging with derivative instruments that the consolidated entity can enter into. The consolidated entity and the Company do not use derivative instruments to manage foreign exchange rate risk. Over the longer-term, permanent changes in commodity prices, interest rates and exchange rates will have an impact on profit.

The estimated impact of a 10 per cent change in the average commodity price for the year ended 31 December 2017 would have increased or decreased the consolidated entity's profit or loss by US\$132,000 (2016: US\$109,000) excluding potential impact of impairments. The estimated impact of a change of 100 basis points in interest rates would have increased or decreased the consolidated entity's profit or loss by US\$5,000 (2016: US\$14,000). The estimated impact of a 10 per cent change in the USD/AUD and USD/CAD exchange rates would have increased or decreased the consolidated entity's profit or loss by a total of US\$183,000 (2016: US\$170,000).

### Fair values of financial assets and liabilities

The carrying values of financial assets and liabilities of the Group approximate their fair values.

The Group measures and recognises in the statement of financial position on a recurring basis certain assets and liabilities at fair value in accordance with AASB13 Fair value measurement. The fair value must be estimated for recognition and measurement or for disclosure purposes in accordance with the following hierarchy:

Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities;

Level 2: Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (as priced) or indirectly (derived from prices); and

Level 3: Inputs for the asset or liability which are not based on observable market data (unobservable inputs).

The fair values of financial assets and liabilities, together with the carrying amounts shown in the balance sheet, are as follows:

	2017		2016	
	Carrying amount US\$'000	Fair value US\$'000	Carrying amount US\$'000	Fair value US\$'000
Trade and other receivables	524	524	4,566	4,566
Cash and restricted cash deposits	3,486	3,486	13,077	13,077
Trade and other payables	(6,861)	(6,861)	(12,229)	(12,229)
Secured borrowings	(5,568)	(5,568)	(3,299)	(3,299)
Financial derivative instruments	(178)	(178)	(764)	(764)
	<b>(8,597)</b>	<b>(8,597)</b>	1,351	1,351

The financial derivative instrument of US\$178,000 (2016: US\$764,000) is a level 2 instrument.

Refer to note 4 for the determination of fair values.

## 21. Operating leases

### Leases as lessee

Non-cancellable operating lease rentals are payable as follows:

	2017 US\$'000	2016 US\$'000
Less than 1 year	306	441
Between 1 and 2 years	249	207
Between 2 and 3 years	256	201
Between 3 and 4 years	206	210
Between 4 and 5 years	-	200
	<b>1,017</b>	1,259

The consolidated entity leases office space in Australia and the USA under operating leases. The leases typically run for a period between 1 and 5 years. None of the leases includes contingent rentals.

During the year ended 31 December 2017, US\$511,000 was recognised as an expense in the statement of comprehensive income in respect of operating leases including month-to-month leases (2016: US\$528,000).

## 22. Capital and other commitments

	2017 US\$'000	2016 US\$'000
<b>Capital expenditure commitments</b>		
<b>Exploration, evaluation and development expenditure</b>		
<i>Contracted but not provided for and payable:</i>		
Within one year	-	2,909
One year or later and no later than five years	-	-
	-	2,909

## Notes to the Financial Statements

For the year ended 31 December 2017

### 23. Contingencies and legal matters

The consolidated entity is a defendant from time to time in legal proceedings. Where appropriate the consolidated entity takes legal advice. The consolidated entity does not consider that the outcome of any current proceedings is likely to have a material effect on its operations or financial position.

The production, handling, storage, transportation and disposal of oil and natural gas, by-products thereof and other substances and materials produced or used in connection with oil and natural gas operations were subject to regulation under U.S. federal, state and local laws and regulations primarily relating to protection of human health and environment. To date, expenditure related to complying with these laws and for remediation of existing environmental contamination has not been significant in relation to the results of operations of the Company.

From time to time, the Company's U.S. subsidiary, Petsec Energy Inc. ("PEI"), is required to provide bonding or security for the benefit of U.S. regulatory authorities and certain lease operators in relation to its obligations to pay lease rentals and royalties, the plugging and abandonment of oil and natural gas wells, and the removal of related facilities. The consolidated entity had no bonding or security obligation requirements as at 31 December 2017 (2016: US\$3,300,000 secured by cash collateral of US\$3,303,000).

### 24. Deed of cross guarantee

Pursuant to ASIC Corporations Instrument 2016/785, relief is granted to certain wholly owned Australian subsidiaries of the Company from the Corporations Act requirements for preparation, audit, and publication of Financial Reports and Directors' Reports.

It is a condition of the Class Order that the Company and each of its subsidiaries enter into a Deed of Cross Guarantee Indemnity. The effect of the deed is that the Company guarantees to each creditor payment in full of any debt in the event of winding up of any of the subsidiaries under certain provisions of the Corporations Act. If a winding-up occurs under other provisions of the Act, the Company will only be liable in the event that after six months any creditor has not been paid in full. The subsidiaries have also given similar guarantees in the event that the Company is wound up.

The subsidiaries subject to the Deed are:

- Petsec Investments Pty. Limited
- Petroleum Securities Pty. Limited
- Najedo Pty. Ltd
- Petroleum Securities Share Plan Pty Limited
- Laurel Bay Petroleum Limited
- Ginida Pty. Limited
- Western Medical Products Pty. Limited

A consolidated statement of comprehensive income and consolidated balance sheet, comprising the Company and subsidiaries which are a party to the Deed, after eliminating all transactions between parties to the Deed of Cross Guarantee, as at 31 December 2017 and 2016, is set out as follows:

### Summarised consolidated statement of profit or loss and other comprehensive income and retained earnings/(accumulated losses)

	2017 US\$000	2016 US\$000
Other income and expenses	2,246	6,168
Operating expenses	(1,841)	(1,704)
Finance income/(expense)	(268)	(653)
Net movement in provisions against loans and investments in controlled entities	(593)	-
<b>Profit/(loss) before tax</b>	<b>(456)</b>	3,811
Income tax benefit/(expense)	-	-
<b>Profit/(loss) after tax</b>	<b>(456)</b>	3,811
Other comprehensive income	-	-
<b>Total comprehensive income for the period</b>	<b>(456)</b>	3,811
Retained earnings/(accumulated losses) at beginning of year	(164,211)	(168,022)
<b>Retained earnings/(accumulated losses) at end of year</b>	<b>(164,667)</b>	(164,211)

## Balance sheet

	2017 US\$000	2016 US\$000
<b>Assets</b>		
Cash and cash equivalents	2,261	8,745
Restricted deposits	-	269
Loans receivable from related parties	-	-
Other receivables	35	2,529
Prepayments	207	54
<b>Total current assets</b>	<b>2,503</b>	11,597
Restricted deposits	222	-
Loans receivable from controlled entities	22,714	12,041
Loans receivable from related parties	-	-
Other financial assets	36,503	32,013
Other investments	-	896
Property, plant and equipment	119	122
<b>Total non-current assets</b>	<b>59,558</b>	45,072
<b>Total assets</b>	<b>62,061</b>	56,669
<b>Liabilities</b>		
Trade and other payables	377	523
Employee benefits provision	49	40
<b>Total current liabilities</b>	<b>426</b>	563
Secured borrowings	5,568	3,299
Fair value of derivative instruments	178	764
Loans payable to controlled entities	-	341
Employee benefits provision	202	184
<b>Total non-current liabilities</b>	<b>5,948</b>	4,588
<b>Total liabilities</b>	<b>6,374</b>	5,151
<b>Net assets</b>	<b>55,687</b>	51,518
<b>Equity</b>		
Issued capital	193,991	193,733
Reserves	26,363	21,996
Retained earnings/(accumulated losses)	(164,667)	(164,211)
<b>Total equity</b>	<b>55,687</b>	51,518



# Notes to the Financial Statements

For the year ended 31 December 2017

## 25. Consolidated entities

	Country of Incorporation	Ownership interest	
		2017 %	2016 %
<b>Parent entity</b>			
Petsec Energy Ltd			
<b>Significant subsidiaries</b>			
Petsec Investments Pty. Limited	Australia	<b>100</b>	100
Petroleum Securities Pty. Limited	Australia	<b>100</b>	100
Najedo Pty. Limited	Australia	<b>100</b>	100
Petroleum Securities Share Plan Pty. Limited	Australia	<b>100</b>	100
Petsec America Pty. Limited	Australia	<b>100</b>	100
Petsec (U.S.A.) Inc.	USA	<b>100</b>	100
Petsec Energy Inc.	USA	<b>100</b>	100
Petsec Exploration and Production LLC	USA	<b>100</b>	100
Petsec Energy Resources Inc.	USA	<b>100</b>	100
Petsec Energy Canada Ltd	Canada	<b>100</b>	100
Laurel Bay Petroleum Limited	Australia	<b>100</b>	100
Ginida Pty. Limited	Australia	<b>100</b>	100
Western Medical Products Pty. Limited	Australia	<b>100</b>	100
Petsec Energy Yemen Ltd	British Virgin Islands	<b>100</b>	100
Petsec Energy (Middle Eastern) Limited	British Virgin Islands	<b>100</b>	100
West Yemen Oil (Block S-1), Inc.	Turks and Caicos Islands	<b>100</b>	100
Yemen (Block S-1), Inc.	Cayman Islands	<b>100</b>	100

With the exception of Petsec Energy (Middle Eastern) Limited, Petsec Energy Yemen Ltd, West Yemen Oil (Block S-1), Inc., and Yemen (Block S-1), Inc., all entities carry on business in the country where they were incorporated.

## 26. Segment reporting

The consolidated entity operates in the oil and gas industry.

Segment information is presented in the consolidated financial statements in respect of the consolidated entity's geographic segments, which reflects the presentation of information to the chief operating decision maker.

Segment results include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Segment acquisition of property, plant and equipment, intangibles and exploration, evaluation and development assets is the total cost incurred during the period to acquire segment assets that are expected to be utilised for more than one period.

In presenting information on the basis of geographical segments, segment assets and liabilities, segment revenue and net profit/(loss) after tax are based on the geographical location of operations.

	Australia		USA		Canada		MENA		Consolidated	
	2017 US\$'000	2016 US\$'000	2017 US\$'000	2016 US\$'000	2017 US\$'000	2016 US\$'000	2017 US\$'000	2016 US\$'000	2017 US\$'000	2016 US\$'000
Oil and gas sales	-	-	<b>1,316</b>	1,116	-	-	-	-	<b>1,316</b>	1,116
Royalties paid	-	-	-	(25)	-	-	-	-	-	(25)
<b>Net revenues after royalties *</b>	-	-	<b>1,316</b>	1,091	-	-	-	-	<b>1,316</b>	1,091
Segment net profit/(loss) before tax	<b>(2,103)</b>	(2,236)	<b>(2,171)</b>	(4,535)	<b>(2)</b>	(4)	<b>(7,688)</b>	(6,249)	<b>(11,964)</b>	(13,024)
Income tax expense	-	-	-	-	-	-	-	-	-	-
<b>Profit/(loss) after tax</b>	<b>(2,103)</b>	(2,236)	<b>(2,171)</b>	(4,535)	<b>(2)</b>	(4)	<b>(7,688)</b>	(6,249)	<b>(11,964)</b>	(13,024)
Depreciation, depletion, amortisation & reclamation	<b>16</b>	11	<b>903</b>	778	-	-	<b>6</b>	2	<b>925</b>	791
Dry hole, impairment and abandonment expense	-	-	-	1,203	<b>1</b>	-	<b>3,987</b>	-	<b>3,988</b>	1,203
Exploration and work-over expense	-	-	-	936	-	-	-	-	-	936
Segment assets	<b>2,844</b>	11,719	<b>16,934</b>	16,345	-	-	<b>387</b>	7,308	<b>20,165</b>	35,372
Acquisition of property, plant and equipment and exploration, evaluation and development assets	<b>46</b>	105	<b>3,846</b>	2,533	-	-	<b>361</b>	227	<b>4,253</b>	2,865

\* There are no inter-segment sales.

\*\* 100% of the Group's oil and gas sales and royalties are derived from one customer.

	Australia		USA		Canada		MENA		Consolidated	
	2017 US\$'000	2016 US\$'000	2017 US\$'000	2016 US\$'000	2017 US\$'000	2016 US\$'000	2017 US\$'000	2016 US\$'000	2017 US\$'000	2016 US\$'000
Segment liabilities	<b>6,373</b>	4,811	<b>1,120</b>	3,688	-	-	<b>5,687</b>	8,772	<b>13,180</b>	17,271
Cash flows from operating activities	<b>(1,593)</b>	(1,975)	<b>326</b>	(1,593)	<b>(2)</b>	(4)	<b>(3,640)</b>	(3,227)	<b>(4,909)</b>	(6,799)
Cash flows from investing activities	<b>(46)</b>	(105)	<b>(3,846)</b>	(2,533)	-	-	<b>(361)</b>	(227)	<b>(4,253)</b>	(2,865)
Cash flows from financing activities	<b>2,449</b>	10,029	-	-	-	-	-	-	<b>2,449</b>	10,029

## Notes to the Financial Statements

For the year ended 31 December 2017

### 27. Interests in unincorporated joint operating arrangements

Included in the assets of the consolidated entity are the following items which represent the consolidated entity's interest in the assets and liabilities in joint operating arrangements:

	2017 US\$'000	2016 US\$'000
<b>Assets</b>		
<b>Oil and gas properties:</b>		
Producing leases – at cost	19,362	14,363
Less: accumulated amortisation and impairment	(3,798)	(2,436)
	<b>15,564</b>	11,927
Represented by the following lease carrying values:		
– Offshore Gulf of Mexico	13,259	8,391
– Onshore Louisiana	2,305	3,536
– MENA	-	-
Total oil and gas properties	<b>15,564</b>	11,927
<b>Exploration and evaluation properties:</b>		
– MENA	-	358
Total exploration and evaluation properties	-	358

	2017 US\$'000	2016 US\$'000
<b>Liabilities</b>		
<b>Rehabilitation provision:</b>		
– Offshore Gulf of Mexico	90	-
– Onshore Louisiana	89	68
	<b>179</b>	68

The contribution of the consolidated entity's joint operating arrangements to EBIT (including exploration write-offs and impairments; and excluding the effects of hedging and any gain on sale of interests):

	2017 US\$'000	2016 US\$'000
– Offshore Gulf of Mexico	110	(468)
– Onshore Louisiana	(472)	(1,534)
– Onshore Canada	(2)	(4)
– MENA	(1,326)	(1,323)
	<b>(1,690)</b>	(3,329)

The principal activity of all the joint operating arrangements is oil & gas exploration. Listed below is the geographic location of each of the joint operating arrangements and the percentage working interest held in the joint operating arrangement by the consolidated entity as at and during the year ended 31 December:

	Interest held 2017	Interest held 2016
– Offshore Gulf of Mexico	12.50%	12.50%
– Onshore Louisiana	12.50% to 25.00%	12.50% to 25.00%
– MENA	35.00% to 100.00%	35.00% to 100.00%

In respect of the joint operating arrangements listed above, the voting powers of the consolidated entity align with its ownership percentages listed in all cases. Management has determined that the consolidated entity has joint control of these arrangements by virtue of the agreements it has with its other partners. The consolidated entity accounts for its share of the individual assets and liabilities of the joint operating arrangements in light of the fact that all of these arrangements lack legal form as separate vehicles.

## 28. Wholly owned areas of interest

Included in the assets and liabilities of the consolidated entity are the following items which represent the consolidated entity's wholly owned areas of interest:

	2017 US\$'000	2016 US\$'000
<b>Assets</b>		
<b>Oil and gas properties:</b>		
Producing leases – at cost	3,554	4,883
Less: accumulated amortisation and impairments	(3,439)	–
	115	4,883
Represented by the following lease carrying values:		
– MENA	115	4,883
	115	4,883

	2017 US\$'000	2016 US\$'000
<b>Liabilities</b>		
<b>Rehabilitation provision:</b>		
– MENA	–	–
	–	–

The contribution of the consolidated entity's areas of interest to EBIT (including exploration write-offs and impairments; and excluding the effects of hedging):

	2017 US\$'000	2016 US\$'000
– Offshore Gulf of Mexico	–	(107)
– MENA	(5,013)	(4,001)
	(5,013)	(4,108)

## 29. Reconciliation of cash flows from operating activities

	2017 US\$'000	2016 US\$'000
<b>Cash flows from operating activities</b>		
Loss for the period	(11,964)	(13,024)
<i>Adjustments for:</i>		
Depreciation, depletion and amortisation	925	791
Dry-hole and impairment expense	3,988	1,203
Exploration and work-over expense	–	936
Net foreign exchange gains	(6)	(133)
Net loss on property, plant and equipment	–	7
Share-based payment expenses	22	23
<b>Operating loss before changes in working capital and provisions</b>	<b>(7,035)</b>	<b>(10,197)</b>
Decrease in restricted cash deposits	3,373	93
Decrease in receivables and prepayments	4,095	308
(Decrease)/Increase in payables and provisions	(5,342)	2,997
<b>Net cash used in operating activities</b>	<b>(4,909)</b>	<b>(6,799)</b>

# Notes to the Financial Statements

## For the year ended 31 December 2017

### 30. Related parties

The following were key management personnel of the consolidated entity at any time during the reporting period and unless otherwise indicated were key management personnel for the entire period:

Non-executive director	Executive director
D A Mortimer A P Baden	T N Fern (Chairman and Managing Director)

Executives
M Petkovski (Chief Executive Officer, Petsec Energy (Middle Eastern) Limited)
R J Smith (Chief Executive Officer, Petsec Energy Inc.) <sup>1</sup>
R A Keogh (Group Chief Financial Officer and President, Petsec Energy Inc.)
R A Krenzke (Executive Vice President Exploration, Petsec Energy Inc.) <sup>2</sup>
P Gahdmar (Company Secretary and Group Financial Controller, Petsec Energy Ltd)

1 Mr. Smith retired from the Company, effective as of 31 May 2017.

2 Mr. Krenzke transitioned from full-time employment to a consultancy with the Company, effective as of 1 June 2017.

### Key management personnel compensation

The key management personnel compensation included in personnel expenses (see note 6) is as follows:

	2017 US\$	2016 US\$
Wages and salaries	804,065	1,163,706
Service agreements	819,085	793,940
Termination benefits	600,000	-
Post-employment benefits	44,010	57,207
Short-term incentives/retention cash bonus	-	23,014
Share-based payment compensation	15,888	19,642
Other benefits <sup>1</sup>	161,401	180,387
	<b>2,444,449</b>	<b>2,237,896</b>

1 Other benefits represent amounts paid on behalf of the Managing Director and Executive Officers in respect of insurance, car parking, fringe benefits and sign-on bonuses.

### Individual directors and executives compensation disclosures

Information regarding individual directors' and executives' compensation and some equity instruments disclosures as required by Corporations Act s300A and Corporations Regulations 2M.3.03 are provided in the Remuneration Report section of the Directors' Report on pages 25 to 31.

Apart from the details disclosed in this note, no director has entered into a material contract with the Company or consolidated entity since the end of the previous financial year and there were no material contracts involving directors' interests existing at year-end.

Non-executive directors appointed prior to 2003 are entitled to receive a retirement benefit that is equivalent to the remuneration received in the three years prior to retirement. Incoming non-executive directors appointed thereafter are not entitled to receive retirement benefits in accordance with the recommendations made by the ASX Corporate Governance Council. Directors' retirement obligations are presently US\$152,000 in total (2016: US\$140,000).



### Transactions with key management personnel

Key management personnel of the Company and their immediate relatives control approximately 17.6 percent of the voting shares of the Company.

1,000,000 options were issued by the Company under its shareholder approved Employee Option Plan ("EOP") to key management personnel as long term incentive compensation during the year (2016: nil).

No shares were issued by the Company under its shareholder approved Employee Share Plan ("ESP") during the year (2016: 800,000). Refer to note 17(b) for details.

The aggregate amounts recognised in service agreements during the year relating to key management personnel and their personally related entities, were a total expense of US\$819,000 (2016: US\$794,000). Refer to Remuneration Report for further details.

### Assets and liabilities arising from the above related party transactions

	2017 US\$'000	2016 US\$'000
<b>Current assets</b>		
Related party receivables	6	-
<b>Current liabilities</b>		
Related party payables	204	83

### Other related party disclosures

Information relating to subsidiaries is set out in note 25.

## 31. Parent entity disclosures

As at, and throughout, the financial year ending 31 December 2017 the parent entity of the consolidated group was Petsec Energy Ltd.

	2017 US\$'000	2016 US\$'000
<b>Result of parent entity</b>		
Profit/(loss) for the period	(11,946)	3,708
Other comprehensive income	4,094	(732)
Total comprehensive income/(loss) for the period	(7,852)	2,976
<b>Financial position of parent entity at year end</b>		
Current assets	13,560	11,597
Total assets	54,610	59,806
Current liabilities	425	563
Total liabilities	10,802	8,889
<b>Total equity of the parent entity comprising of:</b>		
Share capital	193,991	193,193
Share-based payment compensation reserve	39	31
Foreign currency translation reserve	25,707	21,648
Option reserve	451	416
Accumulated losses	(176,380)	(164,371)
<b>Total equity</b>	43,808	50,917

### Parent entity guarantees in respect of the debts of its subsidiaries

The parent entity has entered into a Deed of Cross Guarantee with the effect that the Company guarantees debts in respect of its subsidiaries. Further details of the Deed of Cross Guarantee and the subsidiaries subject to the deed are disclosed in note 24.

### Parent entity contingencies and capital commitments

The parent entity had no contingent liabilities and capital commitments outstanding at 31 December 2017.

# Notes to the Financial Statements

## For the year ended 31 December 2017

### 32. Events subsequent to balance date

Subsequent to balance date, the Company entered into an agreement with the Registrar of the secured convertible note facility to extend the redemption date of the facility and to reinstate Tranche 2 of the facility which was not drawn down and allowed to lapse at the expiry date of 5 January 2018. The key terms of the variation agreement include:

#### Extension of redemption date of the facility

1. Redemption date amended from 23 January 2019 to 23 July 2019.
2. Interest rate of 12.5% per annum monthly compounding for the period 1 January 2018 to 23 January 2019 will increase to 15% per annum monthly compounding from 23 January 2019 to 23 July 2019.
3. Conversion price to be reduced from 15 cents per share to 12.5 cents per share.
4. A note extension facility fee of 5 million fully paid shares in Petsec Energy Ltd at a value of 10 cents per share.
5. The expiry date of the unlisted options previously issued to Sing Rim Pte Ltd, for underwriting the Petsec Energy Ltd rights issue in November 2016, to be extended from 23 January 2019 to 23 July 2020, and the exercise price reduced from 15 cents per share to 12.5 cents per share.

#### Reinstatement of Tranche 2 - US\$5 million

Tranche 2 of the convertible note facility which provides access to a further US\$5 million is subject to the following conditions precedent to issue, and is at the discretion of the Registrar:

- (a) 40% of Tranche 2 on clear indication based upon publicly available information that crude oil has commenced to flow freely within the Republic of Yemen and crude oil has been shipped and sold in material amounts from that Country.
- (b) 10% for each 100,000 barrels of crude oil net to the Group which has been produced in Yemen and transported and stored at the shipping terminal ready for sale, up to a total of 40% of Tranche 2.
- (c) 10% for every 100,000 barrels of crude oil shipped and sold by the Group from Yemen, up to a total of 20% of Tranche 2.
- (d) Conversion: Maximum of 100% of the interest owing on the notes from Tranche 2 and 50% of the advance made under Tranche 2.
- (e) Conversion price: 12.5 cents per share.
- (f) Interest rate: 12.5% per annum compounded monthly.
- (g) Facility fee: 5 million fully paid shares in Petsec Energy Ltd at such times as the facility is drawn.
- (h) Drawdown: Expires on 23 January 2019.
- (i) Redemption date: 23 July 2019.

## Directors' Declaration

- 1 In the opinion of the directors of Petsec Energy Ltd ("the Company"):
  - (a) the financial statements and notes and the Remuneration report in the Directors' Report, set out on pages 25 to 64, are in accordance with the *Corporations Act 2001* including:
    - (i) giving a true and fair view of the financial position of the Company and the consolidated entity as at 31 December 2017 and of their performance, as represented by the results of their operations and their cash flows, for the year ended on that date; and
    - (ii) complying with Australian Accounting Standards and the Corporations Regulation 2001; and
  - (b) the financial report also complies with International Financial Reporting Standards as disclosed in note 2; and
  - (c) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.
- 2 There are reasonable grounds to believe that the Company and the controlled entities identified in note 25 will be able to meet any obligations or liabilities to which they are or may become subject to by virtue of the Deed of Cross Guarantee between the Company and those controlled entities pursuant to ASIC Corporations Instrument 2016/785.
- 3 The directors have been given the declarations required by Section 295A of the *Corporations Act 2001* from the Chief Executive Officer and Chief Financial Officer for the financial year ended 31 December 2017.

Signed in accordance with a resolution of the directors:



Terrence N. Fern  
Director

Sydney, 27 February 2018

# Auditor's Report

## To the shareholders of Petsec Energy Ltd



## Independent Auditor's Report

To the shareholders of Petsec Energy Ltd

### Report on the audit of the Financial Report

#### Opinion

We have audited the **Financial Report** of Petsec Energy Ltd (the Company).

In our opinion, the accompanying Financial Report of the Company is in accordance with the *Corporations Act 2001*, including:

- giving a true and fair view of the **Group** and Company's financial position as at 31 December 2017 and of its financial performance for the year ended on that date; and
- complying with *Australian Accounting Standards* and the *Corporations Regulations 2001*.

The **Financial Report** comprises:

- Consolidated statement of financial position as at 31 December 2017.
- Consolidated statement of profit or loss and other comprehensive income, Consolidated statement of changes in equity, and Consolidated statement of cash flows for the year then ended
- Notes including a summary of significant accounting policies
- Directors' Declaration.

The **Group** consists of the Company and the entities it controlled at the year end or from time to time during the financial year.

#### Basis for opinion

We conducted our audit in accordance with *Australian Auditing Standards*. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the Financial Report* section of our report.

We are independent of the Company and Group in accordance with the *Corporations Act 2001* and the ethical requirements of the *Accounting Professional and Ethical Standards Board's APES 110 Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the Financial Report in Australia. We have fulfilled our other ethical responsibilities in accordance with the Code.



## Key Audit Matters

The **Key Audit Matters** we identified are:

- Going concern basis of preparation; and
- Oil and Gas Properties.

**Key Audit Matters** are those matters that, in our professional judgment, were of most significance in our audit of the Financial Report of the current period.

These matters were addressed in the context of our audit of the Financial Report as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

## Going Concern Basis for Preparation

Refer to Note 2d "Going Concern basis of preparation".

### The key audit matter

The Group's use of the going concern basis of accounting and the associated extent of uncertainty is a key audit matter due to the high level of judgment required by us in evaluating the Group's assessment of going concern.

The Directors have determined that the use of the going concern basis of accounting is appropriate in preparing the financial report. Their assessment of going concern was based on cash flow projections. The preparation of these projections incorporated a number of assumptions and judgments, and the Directors have concluded that the range of possible outcomes considered in arriving at this judgment does not give rise to a material uncertainty casting significant doubt on the Group's ability to continue as a going concern.

We critically assessed the levels of uncertainty, as it related to the Group's ability to continue as a going concern, within these assumptions and judgments, focusing on the following:

- Impact of future commodity prices to cash inflows projected.
- The Group's planned levels of operational and capital expenditures, and the ability of the Group to manage cash outflows within available funding.

### How the matter was addressed in our audit

Our audit procedures included, amongst others:

We analysed the cash flow projections by:

- Evaluating the underlying data used to generate the projections. We specifically looked for their consistency including commodity prices with those used by management, and tested by us, as set out in the oil and gas properties key audit matter, their consistency with the Group's intentions, as outlined in Directors minutes and strategy documents, and their comparability to past practices;
- Analysing the impact of reasonably possible changes in projected cash flows and their timing, to the projected periodic cash positions. Assessing the resulting impact on the ability of the Group to pay debts as and when they fall due and continue as a going concern. The specific areas we focused on were informed from the results of our tests of the accuracy of previous Group cash flow projections and sensitivity analysis on key cash flow projection assumptions.
- Assessing the planned levels of operating and capital expenditures for consistency of relationships and trends to the Group's historical results, results since year end, and our understanding of the business, industry and economic conditions of the Group;



## Auditor's Report Continued



<ul style="list-style-type: none"> <li>The nature and feasibility of planned methods the Group has to meet its financing commitments.</li> </ul> <p>In assessing this key audit matter, we involved senior audit team members who understand the Group's business, industry and the economic environment it operates in.</p>	<ul style="list-style-type: none"> <li>We assessed significant non-routine forecast cash inflows and outflows for feasibility, quantum and timing, and their impact to going concern and funding conditions. We used our knowledge of the client, its industry and status to assess the level of associated uncertainty.</li> <li>We read correspondence with existing financiers to understand and assess the options available to the Group including renegotiation of existing debt facilities;</li> <li>We evaluated the Group's going concern disclosures in the financial report by comparing them to our understanding of the matter, the events or conditions incorporated into the cash flow projection assessment, the Group's plans, and accounting standard requirements</li> </ul>
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Oil and Gas properties \$15.7m	
Refer to Note 12(a) to the financial report.	
The key audit matter	How the matter was addressed in our audit
<p>The Group's Oil and Gas properties were a significant portion (77.8%) of the Group's total assets, and their carrying value was a key audit matter due to the high level of judgement required by us to assess the carrying value.</p> <p>The key judgements involved in the carrying value assessment are forward looking assumptions, as used in the Group's value in use models. The key assumptions are forecast production, oil and gas prices, discount rates and reserve estimates. Management obtain a reserve report from a third party expert to assist in their carrying value assessment.</p> <p>Our assessment is made more challenging given certain recent operating conditions, intermittent production issues, political instability in Middle Eastern located wells and the oil and gas price volatility, each of which are uncertain as to their future improvement.</p>	<p>Our audit procedures included, amongst others:</p> <ul style="list-style-type: none"> <li>We held discussions with management and read the minutes of directors meetings and ASX announcements to understand if the Group had decided to discontinue production at any well. We used this knowledge when assessing forecast production assumptions and the recoverability of the oil and gas properties;</li> <li>We compared historical production profiles for consistency with forecast production trends. We analysed the impact of the political instability in the Middle East to forecast production. We compare forecast production to third party expert reserve reports and investigated inconsistencies.</li> <li>We used our valuation specialists to compare management's discount rates to equivalent industry participants.</li> </ul>



	<ul style="list-style-type: none"> <li>• For all oil and gas properties we performed sensitivity analysis on key assumptions in the value in use models such as production forecasts, discount rates and oil and gas prices to identify areas of increased audit focus.</li> <li>• We compared management's oil and gas price assumptions against published forecasts such as the (WTI oil price) and investigated inconsistencies.</li> <li>• We obtained the Group's value in use models and agreed amounts to FY18 Board approved production plans, FY18 budgets and the third party reserve report.</li> <li>• We assessed the competence and the independence of the third party experts who prepare the third party reserve report used by management to assist in their carrying value assessment of oil and gas properties</li> </ul>
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### Other Information

Other Information is financial and non-financial information in Petsec's annual reporting which is provided in addition to the Financial Report and the Auditor's Report. The Directors are responsible for the Other Information.

Our opinion on the Financial Report does not cover the Other Information and, accordingly, we do not express any form of assurance conclusion thereon.

In connection with our audit of the Financial Report, our responsibility is to read the Other Information. In doing so, we consider whether the Other Information is materially inconsistent with the Financial Report or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

We are required to report if we conclude that there is a material misstatement of this Other Information, and based on the work we have performed on the Other Information that we obtained prior to the date of this Auditor's Report we have nothing to report.

## Auditor's Report Continued



### Responsibilities of the Directors for the Financial Report

The Directors are responsible for:

- preparing the Financial Report that gives a true and fair view in accordance with *Australian Accounting Standards* and the *Corporations Act 2001*.
- implementing necessary internal control to enable the preparation of a Financial Report that gives a true and fair view and is free from material misstatement, whether due to fraud or error.
- assessing the Company and Group's ability to continue as a going concern and whether the use of the going concern basis of accounting is appropriate. This includes disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless they either intend to liquidate the Company and Group or to cease operations, or have no realistic alternative but to do so.

### Auditor's responsibilities for the audit of the Financial Report

Our objective is:

- to obtain reasonable assurance about whether the Financial Report as a whole is free from material misstatement, whether due to fraud or error; and
- to issue an Auditor's Report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Australian Auditing Standards will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error. They are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of this Financial Report.

A further description of our responsibilities for the Audit of the Financial Report is located at the Auditing and Assurance Standards Board website at:

[http://www.auasb.gov.au/auditors\\_responsibilities/ar1.pdf](http://www.auasb.gov.au/auditors_responsibilities/ar1.pdf) This description forms part of our Auditor's Report.



## Report on the Remuneration Report

### Opinion

In our opinion, the Remuneration Report of Petsec Energy Ltd for the year ended 31 December 2017, complies with *Section 300A* of the *Corporations Act 2001*.

### Director's responsibilities

The Directors of the Company are responsible for the preparation and presentation of the Remuneration Report in accordance with *Section 300A* of the *Corporations Act 2001*.

### Our responsibilities

We have audited the Remuneration Report included in pages 25 to 31 of the Director's report for the year ended 31 December 2017.

Our responsibility is to express an opinion on the Remuneration Report, based on our Audit conducted in accordance with *Australian Auditing Standards*.

A handwritten signature in blue ink that reads 'KPMG'.

KPMG

A handwritten signature in blue ink, appearing to be 'D. Camilleri'.

Daniel Camilleri

Partner

Sydney

27 February 2018

## Exploration and Production Interests

### USA

Geographical Location	Field/Prospect	Status	Working Interest	Revenue Interest
<b>USA</b>				
Onshore Louisiana	Jeanerette	Shut-in	12.5%	9.22%
	Mystic Bayou	Producing	25.0%	18.50%
	Ouiski Bayou	Evaluation	12.5%	9.22%
Gulf of Mexico	Main Pass 270 B-1 well <sup>1</sup>	Producing	12.5%	10.26354%
	Main Pass 273 <sup>1</sup>	Evaluation	12.5%	10.26354%
	Main Pass 274	Evaluation	12.5%	10.24%

### MENA Region

Geographical Location	Licence	Status	Working Interest	Participating Interest
<b>Yemen</b>				
Shabwa Basin	Block 7, Al Barqa Permit	Evaluation	35.0%	29.75%
	Block 7, Al Barqa Permit <sup>2</sup>	Evaluation	40.0%	34.00%
	Block 7, Al Barqa Permit <sup>2</sup>	Evaluation	25.0%	21.25%
	Block S-1, Damis Production Licence	Shut-in	100.0%	82.50%

<sup>1</sup> The company holds an overriding royalty interest of 0.00441% in addition to the staked working interest.

<sup>2</sup> The Company has agreements with Oil Search Limited (40% W.I.) and KUFPEC (25% W.I.) to acquire their respective interests in the Block 7, Al Barqa Permit, in the Republic of Yemen, and assume operatorship of the block. The agreements were not completed as of 31 December 2017 and are subject to customary approvals from the Government of Yemen and the Ministry of Oil and Minerals.



## Shareholder Information

### Number of Shareholders

Issued capital was 322,287,924 ordinary shares held by 1,927 shareholders.

All issued shares carry equal voting rights on a one for one basis.

Size of Holding	No. of Holders
1 - 1,000	174
1,001 - 5,000	266
5,001 - 10,000	433
10,001 - 100,000	791
100,001 and over	263
<b>Total number of shareholders</b>	<b>1,927</b>
Number holding less than a marketable parcel	100

### Largest Twenty Shareholders

The largest twenty shareholders held 195,651,256 ordinary shares being 60.707% of the issued ordinary capital.

Name of Shareholder	Number of Shares Held	% of Issued Capital
Martin Place Securities Nominees Pty Ltd	67,034,028	20.799
Canning Oil Pty Ltd	25,709,116	7.977
HSBC Custody Nominees (Australia) Limited	22,335,520	6.930
Mr David A Mortimer & Mrs Barbara L Mortimer	11,335,339	3.517
Lippo Securities Ltd	11,332,500	3.516
Geofin Consulting Services Pty Limited	8,989,610	2.789
Mr Edward Gacka & Mrs Beryl Gacka	5,623,364	1.745
Martin Place Securities Nominees Pty Ltd <Gulf Stream A/c>	5,280,549	1.638
BNP Paribas Nominees Pty Ltd <IB AU Noms Retail Client DRP>	4,888,011	1.517
Citicorp Nominees Pty Limited	4,653,802	1.444
Mr Peter Gacka & Mrs Jenny Gacka	3,730,000	1.157
Petroleum Securities Share Plan Pty Limited	3,700,000	1.148
Hestian Pty Ltd	3,127,843	0.971
Den Duyts Corporation Pty Ltd	3,057,635	0.949
Mr David Lindsay Elsworth	2,800,000	0.869
Ms Dan Luo	2,649,943	0.822
Calveston Worldwide Ltd	2,460,000	0.763
Sino Champion Development Limited	2,459,579	0.763
Asian Corporate Advisers (BVI) Limited	2,250,000	0.698
Mr Nigel Pilcher & Mrs Frances Pilcher <Pilcher Super Fund A/c>	2,234,417	0.693

**Substantial shareholders disclosed in substantial shareholder notices given to the Company are as follows:**

Canning Oil Pty Ltd including its associates	37,876,361	11.752
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## 5 Year Comparative Data Summary

		2013	2014	2015	2016	2017	% change
<b>Financial Performance</b>							
Net Production (MMcfe) <sup>1</sup>		3,645	1,612	511	313	<b>347</b>	11%
Average Gas Equiv. Price Received	(US\$/Mcf)	\$4.50	\$5.08	\$3.07	\$3.48	<b>\$3.79</b>	9%
<b>US\$ million</b>							
Net Revenue	(US\$m)	\$16.4	\$8.2	\$1.6	\$1.1	<b>\$1.3</b>	18%
Net Profit/(Loss) after Tax	(US\$m)	(\$15.2)	(\$1.1)	(\$10.6)	(\$13.0)	<b>(\$12.0)</b>	n/a
Depreciation, depletion & amortisation	(US\$m)	\$7.0	\$1.8	\$0.5	\$0.8	<b>\$1.4</b>	13%
Exploration write-offs, impairments, abandonment and work-over expenses	(US\$m)	\$14.4	\$3.0	\$6.4	\$2.1	<b>\$4.0</b>	90%
Derivative (gains)/losses	(US\$m)	\$1.3	\$0.1	-	-	<b>-</b>	-
Net financial expense	(US\$m)	\$0.2	\$0.2	\$0.2	\$0.8	<b>\$0.3</b>	(63%)
Change in rehabilitation provision	(US\$m)	-	-	-	-	<b>(\$0.5)</b>	n/a
Income tax (benefit)/expense	(US\$m)	-	(\$0.6)	-	-	<b>-</b>	-
EBITDAX <sup>2</sup>	(US\$m)	\$7.7	\$3.4	(\$3.5)	(\$9.3)	<b>(\$6.8)</b>	n/a
EBITDAX Margin/Mcfe	(US\$/Mcf)	\$2.09	\$2.10	(\$6.81)	(\$29.84)	<b>(\$19.53)</b>	n/a
<b>Balance Sheet</b>							
Total Assets	(US\$m)	\$44.6	\$40.1	\$32.5	\$35.4	<b>\$20.2</b>	(43%)
Cash <sup>3</sup>	(US\$m)	\$25.4	\$32.6	\$12.8	\$13.1	<b>\$3.5</b>	(73%)
Debt	(US\$m)	-	-	-	\$3.3	<b>\$5.6</b>	70%
Shareholders' Equity	(US\$m)	\$35.4	\$34.2	\$23.8	\$18.1	<b>\$7.0</b>	(61%)
<b>Cashflow and Capital Expenditures</b>							
<b>Net cashflow from:</b>							
Operations	(US\$m)	\$8.1	\$1.1	(\$5.8)	(\$6.8)	<b>(\$4.9)</b>	n/a
Investing	(US\$m)	(\$10.1)	\$6.1	(\$12.3)	(\$2.8)	<b>(\$4.3)</b>	n/a
Financing	(US\$m)	(\$0.6)	-	-	\$10.0	<b>\$2.5</b>	(75%)
		(\$2.6)	\$7.2	(\$18.1)	\$0.4		
<b>Capital Expenditures<sup>4</sup></b>							
Exploration	(US\$m)	\$2.8	\$3.2	\$12.2	\$1.3	<b>-</b>	(100%)
Development	(US\$m)	\$2.9	\$1.3	\$0.5	\$1.2	<b>\$5.0</b>	317%
Acquisition	(US\$m)	-	\$1.2	\$3.4	\$3.0	<b>\$0.1</b>	(97%)
		\$5.7	\$5.7	\$16.1	\$5.5	<b>\$5.1</b>	(7%)
<b>A\$ million</b>							
EBITDAX <sup>2</sup>	(A\$m)	\$8.0	\$3.8	(\$4.7)	(\$12.5)	<b>(\$8.9)</b>	n/a
Net Profit/(Loss) after Tax	(A\$m)	(\$15.8)	(\$1.2)	(\$14.1)	(\$17.5)	<b>(\$15.7)</b>	n/a
USD/AUD exchange rate		0.9639	0.8981	0.7517	0.7420	<b>0.7655</b>	3%
<b>Operating Margins &amp; Costs</b>							
Average Gas Price Received	(US\$/Mcf)	\$4.50	\$5.08	\$3.07	\$3.48	<b>\$3.79</b>	9%
+ Other Income	(US\$/Mcf)	(\$0.01)	\$1.25	\$1.50	\$0.63	<b>\$0.07</b>	(89%)
- Operating Costs (GG&A + LOE)	(US\$/Mcf)	\$2.40	\$4.23	\$11.38	\$33.95	<b>\$23.39</b>	(31%)
= EBITDAX <sup>2</sup> Margin	(US\$/Mcf)	\$2.09	\$2.10	(\$6.81)	(\$29.84)	<b>(\$19.53)</b>	n/a
Depreciation, Depletion & Amortisation	(US\$/Mcf)	\$1.93	\$1.13	\$1.05	\$2.53	<b>\$4.08</b>	61%
<b>Proved and Probable Reserves (2P)<sup>5</sup></b>							
USA	(MMboe)	1.2	0.3	3.7	3.9	<b>3.8</b>	(3%)
Yemen <sup>6</sup>	(MMboe)	-	-	5.6	5.6	<b>5.6</b>	-
		1.2	0.3	9.3	9.5	<b>9.4</b>	(1%)

1 MMcfe = million cubic feet of gas equivalent. Mcfe = thousand cubic feet of gas equivalent. Conversion ratio: 1 barrel of oil = 6 Mcf of gas.

2 EBITDAX = earnings before interest (financial income and expense), income tax, depreciation, depletion and amortisation, and exploration (including dry hole and impairment expense, exploration and work-over expense). EBITDAX is a non-IFRS number and is unaudited.

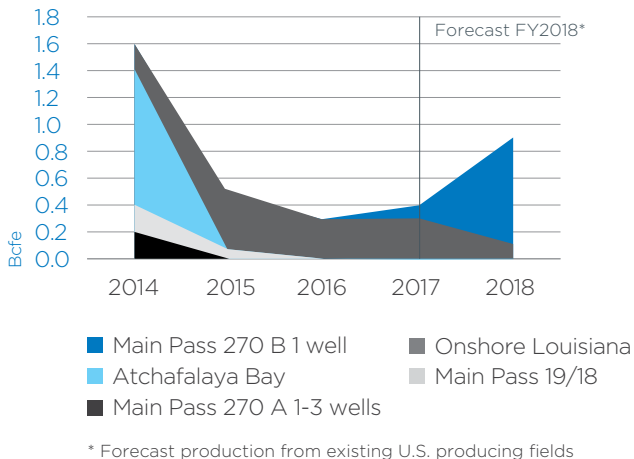
3 FY2017 includes US\$0.2 million of cash deposits.

4 Excludes minor (non-oil & gas) property, plant & equipment expenditure and investments.

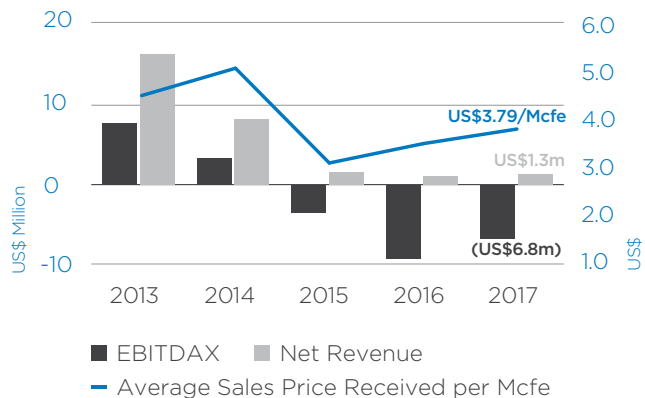
5 2P reserve estimates are based on independent reserve assessments.

6 An Ngyah Oilfield reserves as attributed by DeGolyer and McNaughton Canada Limited as of 1 January 2016. This is unchanged from the initial reserves assessment prepared by DeGolyer and McNaughton Canada, and announced to the ASX on 15 March 2016.

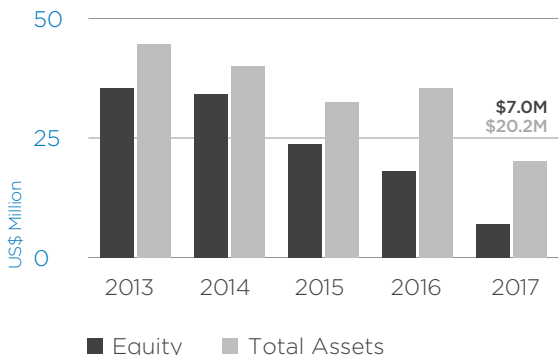
### Production history by Field (USA)



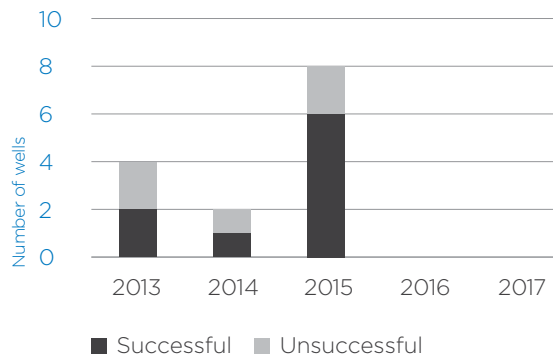
### EBITDAX, Net Revenue & Average Sales Price Received/Mcfe



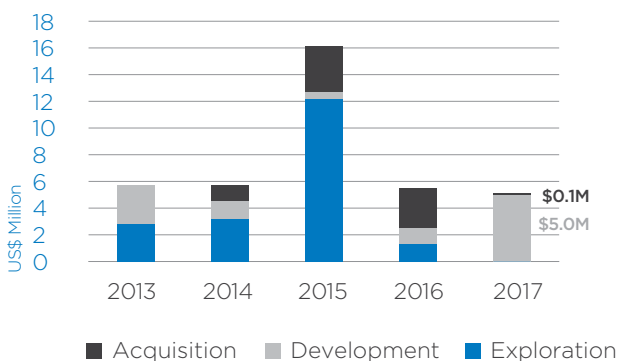
### Balance Sheet Equity and Total Assets



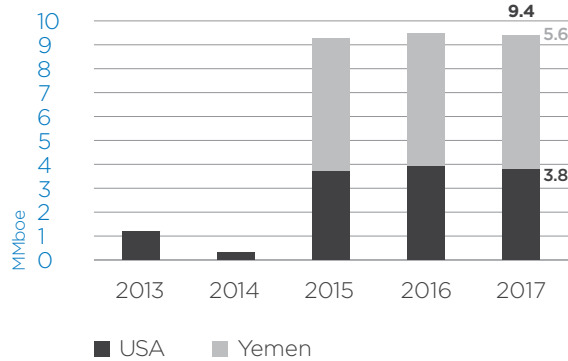
### Wells Drilled/Successful 36% success rate - 5 years to 2017



### Exploration, Development and Acquisition Expenditure



### Year End Independently Assessed Proved and Probable Reserves



## Glossary

<b>1P</b>	Proved reserves
<b>2P</b>	Proved and probable reserves
<b>AMI</b>	Area of mutual interest
<b>Bcf</b>	Billion cubic feet of gas
<b>Bcfe</b>	Billion cubic feet of gas equivalent
<b>Bopd</b>	Barrels of oil per day
<b>Capex</b>	Capital expenditure
<b>cps</b>	Cents per share
<b>DD&amp;A</b>	Depreciation, depletion and amortisation
<b>EBITDAX</b>	Earnings before Interest, taxation, depreciation, amortisation and exploration expense. EBITDAX is a non-IFRS number
<b>Field</b>	An area consisting of a single reservoir or multiple reservoirs all grouped on or related to the same individual geological structural feature and/or stratigraphic condition
<b>JV</b>	Joint venture
<b>Mbbls</b>	Thousand barrels of crude oil or other liquid hydrocarbons
<b>Mbo</b>	Thousand barrels of oil
<b>Mboe</b>	Thousand barrels of oil equivalent
<b>MMbbls</b>	Million barrels of crude oil or other liquid hydrocarbons
<b>MMbo</b>	Million barrels of oil
<b>MMboe</b>	Million barrels of oil equivalent
<b>Mcfe</b>	Thousand cubic feet of gas equivalent
<b>MMcf</b>	Million cubic feet of gas
<b>MMcfe</b>	Million cubic feet of gas equivalent
<b>MMcfpd</b>	Million cubic feet of gas per day
<b>NRI</b>	Net revenue interest
<b>Oil</b>	Crude oil and condensate
<b>Proved reserves</b>	The estimated quantities of crude oil, natural gas and natural gas liquids that geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic and operating conditions
<b>Proved undeveloped reserves</b>	Proved reserves that are expected to be recovered from new wells on undrilled acreage or from existing wells where a relatively major expenditure is required for recompletion
<b>Working Interest or W.I.</b>	The operating interest which gives the owner the right to drill, produce and conduct operating activities on the property and a share of production

# Corporate Directory

## Board of Directors

Terrence N Fern – Chairman and Managing Director

David A Mortimer – Non-executive Director

Alan P Baden – Non-executive Director

## Company Secretary

Paul Gahdmar

## Australian Management

Terrence N Fern – Chairman and Managing Director

Paul Gahdmar – Company Secretary and  
Group Financial Controller

Manny Anton – Head of Investor Relations &  
Corporate Development

## MENA Management

Maki M Petkovski – Chief Executive Officer of  
Petsec Energy (Middle Eastern) Limited (“PEMEL”)

Murray R Hawkes – Chief Operating Officer &  
Yemen General Manager of PEMEL

John L Rees – Vice President Technical of PEMEL

## USA Management

Ross A Keogh – President of PEI and  
Group Chief Financial Officer

## Registered Office and Principal Business Office

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One Farrer Place

Telephone: + 61 2 9247 4605

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## MENA Offices

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Algeria (ST)

Sana'a, Yemen

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Facsimile: + 967 1 448368

## USA Offices

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Houston, TX 77002

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Suite 300, Lafayette

LA 70508 USA

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Facsimile: +1 337 989 7271

## Share Register

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Telephone: 1300 737 760

International: + 61 2 9290 9600

Facsimile: 1300 653 459

International: + 61 2 9279 0664

Email: [enquiries@boardroomlimited.com.au](mailto:enquiries@boardroomlimited.com.au)

## Depository Receipts Register

The Bank of New York

6th Floor, 620 Avenue of the Americas

New York NY 10011 USA

Telephone: + 1 646 885 3300

Facsimile: + 1 646 885 3043

## Auditors

KPMG Australia

Level 38, Tower Three

International Towers Sydney

300 Barangaroo Avenue

Sydney NSW 2000 Australia

## Stock Exchange

Listed on the Australian Stock Exchange, Symbol: PSA

Traded in USA on ADRs, Symbol: PSJEY

## For further information

Web: [www.petsec.com.au](http://www.petsec.com.au)

