

# **Kairiki Energy Limited**

ABN 34 002 527 906

**ANNUAL REPORT 2011**

## Corporate Directory

### Directors

Paul Damien John Fry  
Mark Walker Fenton  
Duncan Wilson Maclean

### Company Secretary

Neville John Bassett

### Registered and Principal Office

Suite 3, Churchill Court  
331-335 Hay Street  
Subiaco WA 6008

Telephone: (08) 9388 6711

Facsimile: (08) 9388 6744

Website: [www.kairikienergy.com](http://www.kairikienergy.com)

### Share Registry

Computershare Investor Services Pty Ltd  
Level 2, Reserve Bank Building  
45 St Georges Terrace  
Perth WA 6000

Investor enquiries:

Telephone: 1300 557 010

(08) 9323 2000

Facsimile: (08) 9323 2033

### Auditor

Rothsay  
Chartered Accountants  
96 Parry Street  
Perth WA 6000

### Securities Exchange Listing

ASX Limited  
(Home Branch - Perth)  
ASX Code: KIK

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## Company Highlights

### SC 54A – TINDALO PROJECT

- ❖ The Tindalo development commenced testing on 6 June 2010.
- ❖ A work-over of the well was conducted in September 2010 in an attempt to rectify water ingress issues in the original vertical well by drilling a sidetrack well. The well was brought back on stream with an initial test production rate of approximately 5,000 barrels of oil per day (bopd) before water ingress occurred. A workover of the sidetrack was then conducted involving the placement of a selective completion and the well re-tested.
- ❖ Production and other diagnostic data gathered during the testing period in the December 2010 half-year confirmed that the sidetrack and subsequent work-over were unsuccessful in preventing or slowing formation water influx to the extent required for commercial oil production. As a result, the Joint Venture Partners made a decision to abandon the Tindalo Well on 29 December 2010.
- ❖ Total production for the project was approximately 269k bbls (KIK share: 81k bbls), resulting in net revenue to Kairiki of approximately US\$6.5 million.

### SC 54A - OTHER

- ❖ 3D seismic data covering 140 sq km was reprocessed within the central portion of the contract area which includes the Nido 1X1 and Yakal discoveries. Ongoing technical work is focussed on mapping and volumetrics of prospects and development opportunities on the reprocessed 3D and also the various development options for the Nido 1X1 oil discovery which straddles the SC 54A and SC 14A permits.
- ❖ In July 2011 Kairiki announced it had selected its preferred farm-in partner in SC 54A to farm down a further 15.05% interest in SC 54A.

### SC 54B – GINDARA PROJECT

- ❖ Kairiki farmed down its interest in SC 54B by 18% interest to Shell resulting in Kairiki maintaining an interest of 22% in the permit. As consideration, Shell agreed to fund 75% of the Gindara-1 exploration well cost up to a maximum well cost of US\$24 million in return for 45% participating interest (18% provided by Kairiki).
- ❖ The Shell Deepwater Rig “Atwood Falcon” contracted to drill Gindara-1 spudded on 20 May 2011.
- ❖ The Gindara-1 well resulted in a 187 metre hydrocarbon column being discovered. However, the discovery was considered non-commercial due to the poor quality reservoir encountered.
- ❖ Seismic mapping of the central and southern parts of SC 54B highlighted the potential significance of the Pawikan lead. The Pawikan lead is larger and potentially more oil-prone than the Gindara prospect.

### PERMITTING

- ❖ A 12 month extension to the current SC 54A and SC 54B Service Contracts was approved by the Philippines Department of Energy in July 2011 resulting in the current work programme phase now expiring 4 August 2012.

**CORPORATE**

- ❖ Completion of Placement and Rights Issue in December 2010 raising \$8,519,280 (before issue costs).
- ❖ Completion of Placement and Rights Issue in February 2011 raising \$12,378,920 (before issue costs).
- ❖ Completion of Placement and Rights Issue in July 2011 raising \$6,000,000 (before issue costs).
- ❖ Mr Duncan Maclean joined the Board.

## Chairman's Letter

Dear Shareholder,

Kairiki's strategy over the past few years has been to commercialise the SC 54A portfolio to generate revenue as well as to realise the exploration upside potential of SC 54B, as quickly as possible.

During the past year, the Company's first investment in SC 54A, the Tindalo project, was unsuccessful. Despite undertaking a work-over and well intervention and remediation program which involved sidetracking the vertical Tindalo well, testing the open-hole sidetrack, recompleting the sidetrack with a selective completion and conducting an extensive testing programme from isolated zones within the sidetrack, excessive water production rendered the development uneconomic. In early 2011 the SC 54A Joint Venture decided to abandon and demobilise the Tindalo development equipment.

Whilst the results of the Tindalo development were very disappointing, the overall production characteristics of similar Nido pinnacle reefs in the area have historically been very good. Following the Tindalo result, there was strong interest by a number of oil companies to farm-in to Kairiki's SC 54A asset as there remains a substantial portfolio of discovered oil pools and exploration prospects yet to be developed in the area, no doubt each with their own production characteristics.

As a result, Kairiki announced in July 2011 that it had selected a preferred farminee to farm-out a 15.05% participating interest in return for a funded drilling programme. Currently, the farminee is completing due diligence and legal documentation is underway.

The other major area of focus during the year was the drilling of Gindara in SC 54B. In October 2010 Kairiki farmed-down its interest in SC 54B to Shell Philippines Exploration B.V. to take a 45% position in the Joint Venture (18% provided by Kairiki) in return for the drilling of a well on Gindara.

Gindara was subsequently drilled in May-June 2011 and logging data confirmed the discovery of a 187 metre hydrocarbon column consisting of a 144 metre gas column and a possible 43 metre oil column. Unfortunately, the thickness of poor quality reservoir in the upper part of the Nido Limestone reservoir section was substantially thicker than expected resulting in nearly all the hydrocarbon column occurring in poor quality reservoir and the discovery being non-commercial.

The results from Gindara highlighted the occurrence of strong hydrocarbon charge in the area and has now driven the exploration focus towards the south, where reprocessed vintage 2D seismic indicates the possible extension of the Malampaya source graben into the Pawikan area. Importantly, a very large lead – Pawikan – has been identified which is approximately 53 sq km in size, and hence larger than Gindara, with a vertical relief of approximately 300 metres. The acquisition of 2D seismic data in the period to December 2011 is under consideration and will focus on confirming this interpretation.

It has been an eventful year for Kairiki, with the Company delivering on its strategy to expose its shareholders to production and upside exploration activity. Whilst the results have been disappointing, the acreage Kairiki retains is still considered highly prospective. Kairiki's strategy of farming down further its interest in SC 54A for a carried drilling activity will allow the company to commercialise its interest in SC 54A. The drilling result at Gindara has highlighted the oil potential of Pawikan and therefore we believe that SC 54B remains highly prospective.

I would like to thank the efforts of our Board and staff who navigated the challenging technical, commercial and financial challenges that the company has faced in the last 12 months in a difficult market environment.

We look forward to the next 12-18 months with excitement as we recommence our exploitation efforts in SC 54A and continue to mature our exploration acreage in SC 54B.



Paul Fry  
Chairman

## Operations Review

### Development (Extended Well Test) - SC 54A Tindalo

#### SC 54A WORKING INTERESTS

Company	Working Interest
<b>Nido Petroleum Philippines Pty Ltd (Nido) Operator</b>	42.4%
<b>Yilgarn Petroleum Philippines Pty Ltd, (Kairiki)</b>	30.1%
<b>Trafigura Ventures III BV (Trafigura)</b>	15.0%
<b>TG World (BVI) Corporation (TG World)</b>	12.5%

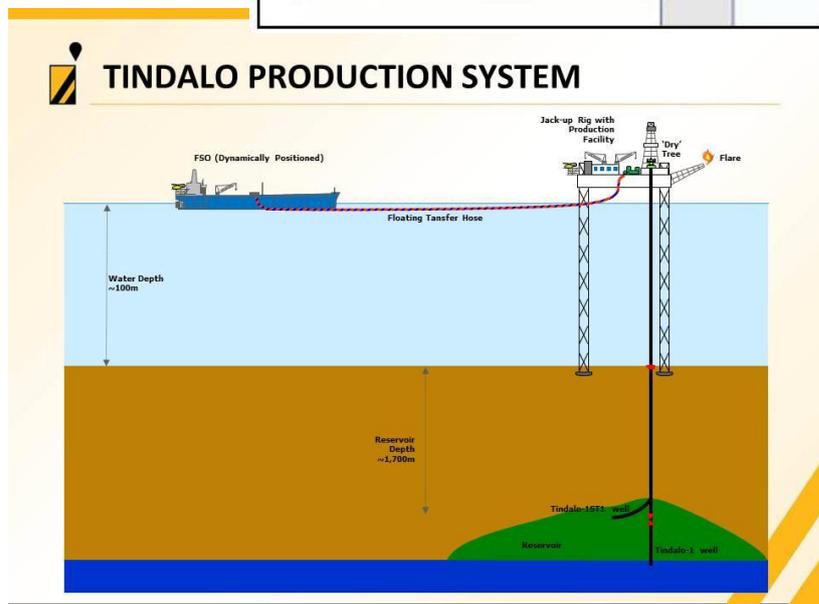
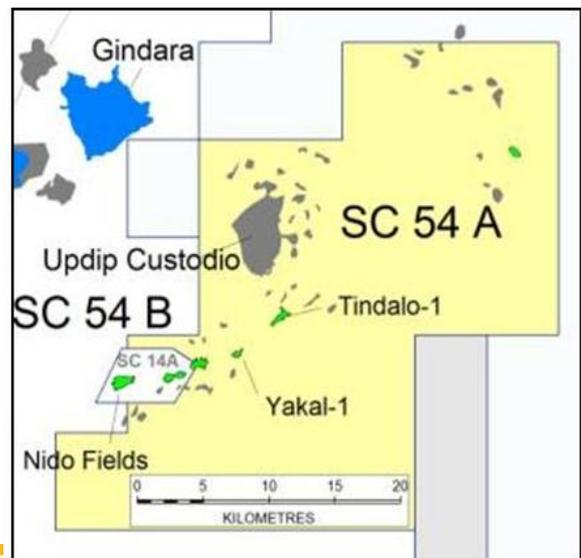
#### PRODUCTION AND CRUDE OIL LIFTING

During the period from 1 July 2010 to the end of the project in February 2011, oil production was 170,968 bbls (KIK share: 51,461 bbls). Total production for the project was approximately 269k bbls (KIK share: 81k bbls).

A lift of the first crude oil cargo from Tindalo of 194,336 barrels occurred on 20 September 2010 and resulted in Kairiki receiving US\$4,401,056 (A\$4,774,861) for its share of revenues from the 58,495 barrels of oil sold to a buyer in South Korea.

Having made the decision to abandon Tindalo at the end of December 2010 and demobilise all of the production equipment in early January 2011, a sale of the remaining oil inventory to a Singapore buyer occurred in early February 2011. The sale of the remaining 73,420 bbls crude at the end of the project generated a further US\$2,104,473 net to Kairiki.

The Extended Well Test (EWT) period expired on 2 November 2010 with all production post this date subject to normal production sharing contract terms applicable in the Philippines.



## TINDALO WELL TEST

The Extended Well Test (EWT) at Tindalo which formally commenced on 6 June 2010 was designed to evaluate well performance, thereby providing a long-term reservoir management plan for optimisation of Tindalo's resources and value during the normal production phase beyond the EWT term.

## WELL REMEDIATION

During the initial stages of the EWT, water was produced to surface which was later determined to be water from the formation. The formation water production was being produced from either a flow path to the aquifer behind the production casing and within the wellbore, or conversely was the result of a high permeability, high angle fracture(s) with direct access to the aquifer associated particularly with this well location.

As a result of the significant water cuts being experienced the Joint Venture decided to initiate a work-over which was anticipated to increase the amount of oil produced by a significant reduction or elimination of the watercut.

The SC 54A Joint Venture approved the Tindalo-1 well intervention and remediation programme, and decided after well re-entry to sidetrack within the Nido Limestone. The original Tindalo-1 vertical well bore was plugged back and the Aquamarine Driller drilled approximately 180 metres of reservoir in a new high-angle sidetrack hole to the south-southwest of the original Tindalo-1 well. This provided 120 metres of near horizontal producing section and the production completion, including the downhole electric submersible pump, was re-installed.

Testing and other diagnostic data gathered from the sidetrack and a subsequent work-over that involved the installation of a selective completion were unsuccessful in preventing or slowing formation water influx to the extent required for commercial oil production. As a result, the Joint Venture Partners made a decision to abandon the Tindalo Well on 29 December 2010.



## ABANDONMENT AND DEMOBILISATION

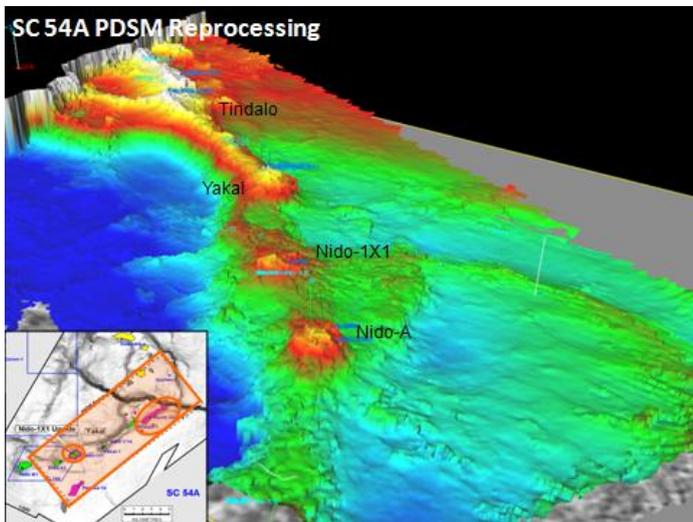
Having made the decision to abandon Tindalo the Joint Venture partners considered whether to demobilise the production equipment and hardware from SC 54A, or to retain the equipment for further work within the permit. A decision was made in early January 2011 not to pursue the Yakal development at that time. A review of the Tindalo Project results that incorporate the sub-surface, technical and operational aspects of the project was required prior to any further development activities in the shallow water.

As a result of these decisions the Joint Venture decided to demobilise the project equipment (including the Aquamarine Driller and Tove Knutsen) from the Service Contract. The Tove Knutsen was demobilised to Singapore where it delivered the final cargo of Tindalo crude to buyers in Singapore. All contracts associated with the Tindalo Project were completed within the March 2011 quarter.

As a result of the abandonment of the Tindalo well, the net costs associated with Kairiki's share of the project from inception of approximately US\$30 million were written off at 31 December 2010.



SEISMIC REPROCESSING

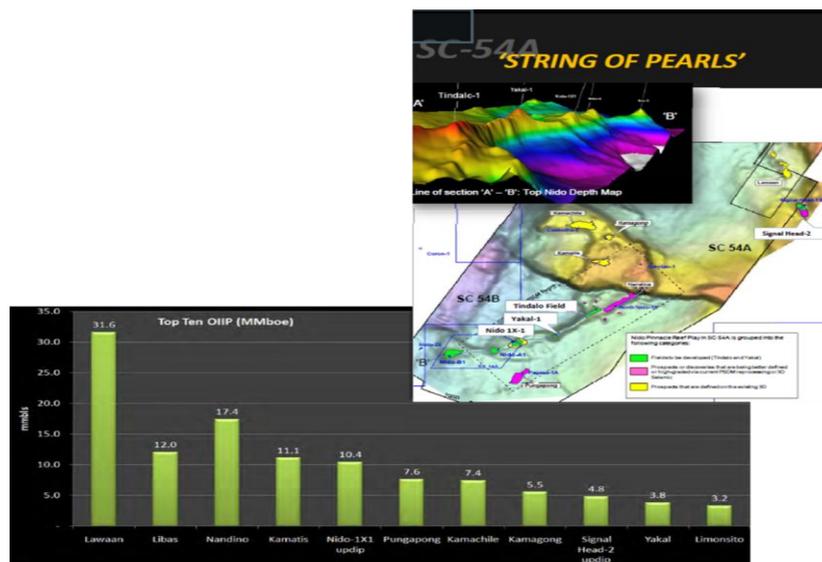


In addition to the activities being undertaken on Tindalo, the Joint Venture has been progressing the reprocessing of 3D seismic data covering an area of 140 sq km within the central portion of the contract area which includes the Tindalo, Nido 1X1 and Yakal discoveries, and the Pungapong and Nandino prospects along with numerous smaller leads.

Assessment of the results of Pre-stack Depth Migration seismic reprocessing of the area covering the Nido 1X1 oil discovery confirmed the robustness of the oil-bearing Nido Limestone pinnacle reef play. Work is currently ongoing to determine the potential oil volumes within the structure and commercialisation scenarios.

A substantial portfolio of potentially economic prospects and discoveries has been re-affirmed, with the highest graded opportunities identified to be the Nido 1X1

discovery and the Lawaan exploration prospect. Total oil in place resources are estimated by the Operator at 112 mmbbls in the top 10 prospects/discoveries (gross un-risked).



Location Map and Portfolio Inventory – SC 54A

FARMOUT

Subsequent to the end of the quarter, Kairiki announced that it had selected its preferred farminee party to farm-in to the SC 54A permit. The Party was granted an exclusive 60 day period to finalise its due diligence review and complete and execute farm-out and associated agreements. This exclusivity period was extended by an additional 30 days on 5 September 2011.

A condition of the farm-in negotiations requires the identity of the Party together with the terms of the farm-in agreement to remain confidential until the necessary farm-out documents have been executed.

The transaction contemplated will, if completed, result in Kairiki reducing its interest in SC 54A from 30.1% to 15.05% in return for a funded work programme involving drilling within the permit. Kairiki's expenditure commitments in SC 54A in the short to medium term are therefore expected to be minimal.

## Exploration – SC 54B Gindara

### SC 54B WORKING INTERESTS

Company	Working Interest
Nido Petroleum Philippines Pty Ltd (Nido) – Operator	33%
Yilgarn Petroleum Philippines Pty Ltd (Kairiki)	22%
Shell Philippines Exploration B.V. (Shell)	45%

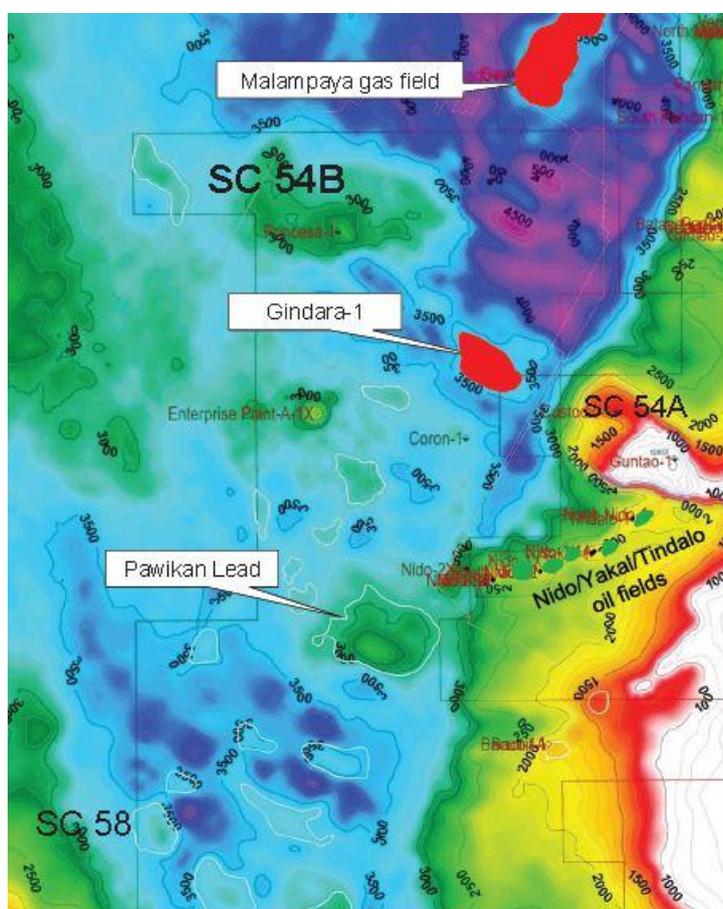
### GINDARA

In October 2010 Kairiki announced that it had successfully entered into an agreement with Shell Philippines Exploration B.V. (“Shell”), a subsidiary of the Royal Dutch Shell Group, to farm-out 18% out of its current 40% participating interest in SC 54B. As a result of this transaction, Shell acquired a 45% participating interest in SC 54B (Kairiki contributing 18% and SC 54B partner Nido Petroleum Limited (“Nido”) contributing 27%). To earn its participating interest, Shell would fund 75% of the Gindara-1 exploration well cost up to a maximum well cost of US\$24 million and pay US\$2.5 million towards past seismic costs. Final Government and other approvals were received by 28 January 2011.

This transaction enabled Kairiki and its partner to commence detailed drilling planning, including the ordering of long-lead items and materials with Gindara to be drilled in the first half of 2011.

The drilling of the Gindara-1 well commenced on 20 May 2011 using the semi-submersible drill rig “Atwood Falcon”. Gindara-1 was drilled to a depth of 3,660 metres MD. The well discovered a 187 metre hydrocarbon column (144 metres of gas and an additional 43 metres of oil). However, due to the hydrocarbon column being contained in poor quality reservoir, the discovery was considered non-commercial.

The Gindara result clearly demonstrates that there is an active hydrocarbon system in SC 54B. A thorough review of the Gindara results in combination with the seismic data in the area is in process. Should the results confirm the potential for substantial hydrocarbon charge from the Malampaya Trough this will have implications for leads such as Pawikan that would drain any possible extension of the Malampaya Trough in the central and southern areas of SC 54B.



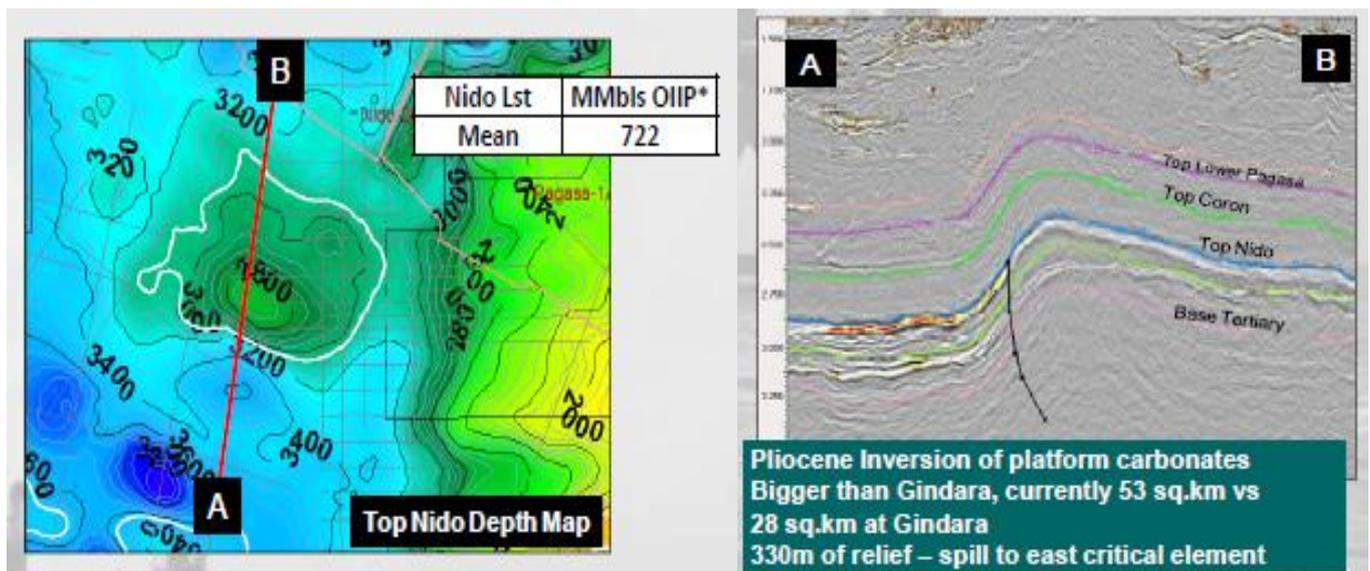
**EXPLORATION PROSPECTIVITY**

Interpretation of the 2D data in the southern portion of the permit was also continued during the early part of 2011. This work, which was based on vintage 2D seismic, identified a number of potential leads at top Nido limestone stratigraphic level, the largest of which is the Pawikan Lead.

**PAWIKAN**

During the period, seismic mapping of the central and southern parts of SC 54B has highlighted the potential significance of the Pawikan lead. The Pawikan lead is larger and potentially more oil-prone than Gindara, at 53 sq km in size with an approximately 300 metre relief. In-place oil is estimated at 2 bln bbls (unrisked estimate by Independent Review as reported by Operator). Further seismic will be required before firming the lead to prospect drilling status. In addition, seismic reprocessing of some 2D seismic lines within the southern portion of SC 54B has provided some preliminary evidence for the possible existence of the southern extension of the Malampaya Trough adjacent to the Pawikan lead. This could have implications for the prospectivity of the southern part of SC 54B as the Malampaya Trough is considered to have generated the hydrocarbons encountered in Gindara-1 approximately 30 km to the north of Pawikan.

In August 2011, the Operator advised Kairiki that it is reviewing the opportunity to acquire further 2D seismic in the following months over the Pawikan lead. This additional seismic is intended to mature the Pawikan lead for possible drilling in the future.



*Pawikan lead – Top Nido Depth Map*

*Pawikan Lead – Seismic Section*

**SC 54 - PERMITTING**

In July 2011, a 12 month extension to the current work period (Sub Phase 6) for Service Contract 54, which was to end on 4 August 2011, was granted by the Philippine Department of Energy (DOE). This extension of Sub Phase 6 until 4 August 2012 applies to both SC 54A and SC 54B blocks.

The well commitment associated with Sub Phase 6 has been met by the drilling of Gindara-1.

**RESOURCE ESTIMATES**

All potential hydrocarbon resource estimates in this annual report have been compiled by Dr M Fenton, the Company's Managing Director, in consultation with the respective Joint Venture Operator, where appropriate. Dr Fenton has a PhD in Geology and a Bachelor of Science (Honours) in Geology from the University of Melbourne and more than 25 years of relevant experience.

## Directors' Report

Your Directors present their report on Kairiki Energy Limited ("Kairiki" or "the Company") and its controlled entities ("the Group") for the year ended 30 June 2011.

### **DIRECTORS**

The names of the Directors of the Company in office during the financial year and up to the date of this report were as follows. Directors were in office for the entire year unless otherwise stated.

Paul Damien John Fry	
Mark Walker Fenton	
Duncan Wilson Maclean	– appointed 31 March 2011
Neville John Bassett	– appointed 28 September 2010, resigned 31 March 2011
Lawrence James Brown	– resigned 30 August 2010
John Trevor Nicholas Morton	– appointed 25 August 2010, resigned 28 September 2010
Jyn Sim Baker	– resigned 25 August 2010

### **INFORMATION ON DIRECTORS**

#### **Paul Damien John Fry**

CA  
Non-Executive Chairman

Mr Fry is a chartered accountant with over 20 years of experience in the oil and gas industry in Australia, UK and North America. He was formerly an oil and gas specialist partner with Ernst & Young and Pricewaterhouse Coopers in Australia and Canada.

During the past three years Mr Fry has held the following other listed company directorships:

- Segue Resource Limited (2 April 2008 to 15 June 2011)

Director since 4 April 2006.

#### **Mark Walker Fenton**

PhD (Geology)  
Managing Director

Dr Fenton has over 25 years of experience in operating oil and gas companies and has extensive experience in both offshore and onshore oil field developments, particularly in SE Asia and the Middle East. He has held a range of technical, management and executive positions with international and Australian oil and gas majors as well as smaller ASX-listed oil companies during his career.

Dr Fenton has a PhD in Geology from the University of Melbourne and is a member of the Society of Petroleum Engineers (SPE). He has significant international technical and operating skills in project development, exploration and project acquisition.

During the past three years Mr Fenton has held the following other listed company directorships:

- Baraka Petroleum Limited (10 August 2007 – 31 July 2008)

Director since 1 December 2009.

**DIRECTORS' REPORT**

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**Duncan Wilson Maclean**

LLM (Comm Law), LLB  
Non-executive Director

Mr Maclean, a partner at Minter Ellison, is a corporate lawyer with over 18 years corporate experience. He specialises in resources and energy related matters and advises on major acquisitions, divestments, joint venture arrangements and project structuring. Mr Maclean has a Masters of Commercial Law (Energy & Resources) and a Bachelor of Laws. He is a member of the Australian Institute of Company Directors (AICD), the Australian Mineral and Petroleum Lawyers Association (AMPLA) and the Association of International Petroleum Negotiators (AIPN).

Mr Maclean has held no other listed company directorships within the past three years.

Appointed 31 March 2011.

**Neville John Bassett**

B.Bus, FCA  
Non-Executive Director

Mr Bassett specialises in the area of corporate consulting, financial management and advisory services, consulting to a number of publicly listed and private companies in a diverse range of industry sectors. He has experience in company listings, capital raisings and mergers and acquisitions. Through his exposure to Australian financial markets, he has a wealth of understanding of matters pertaining to the Corporations Act, ASX listing requirements, corporate taxation and finance.

During the past three years Mr Bassett has held the following other listed company directorships:

- RAM Resources Limited (22 March 2004 to present)
- Vector Resources Limited (22 April 2010 to present)
- Neurodiscovery Limited (6 August 2010 to present)
- Mamba Resources Limited (13 August 2010 to present)
- Modena Resources Limited (14 September 2006 – 30 January 2009)

Appointed 28 September 2010, resigned 31 March 2011.

**Lawrence James Brown**

B.Sc (Hons) – Geology/Geophysics

Mr Brown has over 25 years international petroleum exploration industry experience as an exploration geoscientist. He joined BP in 1982 and after 17 years working predominantly on international assignments covering the Middle East, Asia, Africa, UK and Australia, he settled in Australia in 1999 where he took up a lead role in Woodside's International Team. He was appointed as a Shell Global Consultant and led Woodside's technical exploration effort in deepwater Mauritania, culminating in the landmark Chinguetti discovery.

During the past three years Mr Brown held the following other listed company directorships:

- Rialto Energy Limited (16 February 2006 to 15 May 2009)

Resigned 30 August 2010.

DIRECTORS' REPORT

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**John Trevor Nicholas Morton**

CA, M. Appl. Finance, BA, B. Comm

Mr Morton is Chief Portfolio Manager of IMC Resources (Australia) Pty Limited (IMC Australia). He has in excess of 15 years of experience in investments, strategy and corporate finance both in Australia and overseas, having worked with Ernst & Young Corporate Finance and Rio Tinto.

Mr Morton held no other listed company directorships within the past three years.

Appointed 25 August 2010, resigned 28 September 2010.

**Jyn Sim Baker**

LLB

Ms Baker held the role of Chief Executive Officer for IMC Resources Group, which spans Australia, China and Indonesia, until May 2010. She was responsible for investments in mining resources, oil and gas resources and the vertical integration process for the IMC's core businesses in shipping and logistics.

Ms Baker has over 20 years of management and legal advisory experience. Prior to joining IMC, Ms Baker was the Chief Executive Officer of Midwest Corporation Limited, a company listed on the Australian Securities Exchange. Formerly a practicing corporate lawyer, Ms Baker's expertise extends across energy industry projects, minerals exploration and mining, and infrastructure development

Ms Baker holds a Bachelor of Law and an ICSA (Institute of Chartered Secretary and Administration) qualification from the University of London and a Certificate in Legal Practice from the University of Malaysia. She is a member of the Australian Institute of Company Directors.

During the past three years Ms Baker held the following other listed company directorships:

- Atlas Iron Limited (13 November 2006 – 31 May 2010);
- Horizon Oil Limited (6 June 2007 – 22 June 2010);
- LinQ Capital Limited (27 November 2006 – 31 May 2010); and
- View Resources Limited (9 September 2007 – 30 October 2007).

Resigned 25 August 2010.

**COMPANY SECRETARY**

Neville John Bassett

**DIRECTORS' INTERESTS IN SHARES AND OPTIONS**

The relevant interest of each Director in the shares and options of the Company at the date of this Report is as follows:

Paul Fry

- 10,725,518 ordinary fully paid shares
- 12,500,000 unlisted options exercisable at 6.5 cents between 16 May 2012 and 16 May 2014

Mark Fenton

- 107,000 ordinary fully paid shares
- 20,000,000 unlisted options exercisable at 6.5 cents between 16 May 2012 and 16 May 2014

Duncan Maclean

- 7,995,000 ordinary fully paid shares
- 1,199,250 listed options exercisable at 0.4 cents between 1 June 2013 and 30 June 2013
- 7,500,000 unlisted options exercisable at 6.5 cents between 16 May 2012 and 16 May 2014

**DIRECTORS' REPORT**

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***MEETINGS OF THE COMPANY'S DIRECTORS***

The number of meetings of the Company's Directors held during the year ended 30 June 2011, and the number of meetings attended by each Director were:

	<b>Number Attended</b>	<b>Maximum Possible</b>
Paul Fry	4	4
Mark Fenton	4	4
Duncan Maclean	1	1
Neville Bassett	4	4
Lawrence Brown	1	1
Jyn Sim Baker	1	1
John Morton	0	0

***CORPORATE STRUCTURE***

Kairiki Energy Limited is a limited liability company that is incorporated and domiciled in Australia.

***NATURE OF OPERATIONS AND PRINCIPAL ACTIVITIES***

The principal activities of the Company and its controlled entities during the financial year were:

- Exploration for oil and gas
- Evaluation of oil and gas properties
- Development of oil and gas properties.

***OPERATING AND FINANCIAL REVIEW***

**Operating Activities**

A detailed review of the operations of the Group is contained in the Operations Review on p. 7 to 12.

**Summary of Comprehensive Income**

The Group's consolidated loss for the financial year after tax was \$43,006,000 (2010: \$2,945,000).

The loss for the year included:

- The write-down of the Tindalo project, following the Joint Venture Partners' decision to abandon the well in December 2010, of \$28,198,000 (2010: nil).
- The write-down of deferred exploration and evaluation costs associated with the Gindara-1 well of \$10,212,000 (2010: nil).
- Impairment of receivables for deferred consideration in respect of the sale of a 4.9% interest in SC 54A of \$1,045,000 (2010: nil).
- General administration expenses of \$1,974,000 (2010: \$1,751,000);
- Cash interest expenses on the Convertible Note of \$1,219,000 (2010: \$1,472,000); and
- Non-cash accretion and borrowing costs on the Convertible Note of \$647,000 (2010: \$683,000).

These expenses were partially offset by:

- Interest income of \$63,000 (2010: \$88,000); and
- Foreign exchange gains of \$227,000 (2010: \$600,000).

**Earnings per Share**

The basic and diluted loss per share was 5.22 cents (2010: loss of 0.57 cents).

### Financing Activities

The Company raised \$20,928,000 before issue costs via the issue of securities during the year. Refer to Note 14 in the financial statements for details.

US\$2,000,000 of the Convertible Note owing to IMC was repaid. The repayment reduced the amount owing on the Convertible Note at maturity to US\$7,529,981.

### Summary of Financial Position

At 30 June 2011 the Group's unrestricted cash reserves were \$1,802,000 (2010: \$9,028,000). The decrease in cash was due to:

- net cash used in operating activities of \$3,021,000;
- net cash used in investing activities of \$20,896,000, comprised primarily of expenditures on oil and gas properties for the development of Tindalo of \$26,090,000 and expenditures on exploration and evaluation of \$2,529,000, offset by the sale of oil produced during the extended well test of Tindalo of \$6,486,000 and deferred consideration received from the sale of interests in oil and gas permits of \$1,243,000;
- repayment of \$1,982,000 of the Convertible Note; and
- proceeds from capital raisings of \$19,356,000, net of costs.

### Dividends

No dividend was paid or declared by the Company in the period since the end of the previous financial year and up to the date of this report.

### *SIGNIFICANT EVENTS AFTER BALANCE DATE*

#### (i) Underwritten Rights Issue

On 26 August 2011 the Company completed a \$6,000,000 (before expenses of the issue) capital raising via a pro-rata renounceable rights issue that was underwritten by Patersons Securities Limited, the Company's Lead Manager. The Rights Issue was offered to eligible shareholders, on the basis of three (3) new share for every two (2) shares held at an issue price of 0.4 cents per share. For every four shares subscribed for in the Rights Issue, the applicant received 1 "piggy back" option. The primary option is exercisable at 0.4 cents during June 2013 and will expire on 30 June 2013. The primary option is exercisable into one share and a secondary option which is exercisable at 0.4 cents and expires on 30 June 2015.

Pursuant to the Rights Issue the Company allotted the following securities on 6 September 2011:

- 2,688,078,239 ordinary shares; and
- 750,133,177 Attaching Options expiring 30 June 2013 and exercisable at \$0.004 cents were issued.

The funds raised are being utilised towards the ongoing participation in the Company's interest in the Philippines Offshore Exploration Service Contract SC 54A and SC 54B, repayment of US\$1 million of the outstanding balance of the Convertible Note, costs of the offer and for additional working capital.

#### (ii) Convertible Note Amendments

On 24 August 2011 the Company negotiated the following amendments to the Convertible Note agreement:

- i) The repayment date of the Convertible Notes has been extended by two years from September/October 2011 to September/October 2013;
- ii) The interest rate paid on the outstanding balance of the Convertible Notes has been reduced from 12% to 4% with the remaining 8% capitalised to the balance of the Convertible Notes and payable on maturity; and
- iii) The conversion price of the Convertible Notes is now based on a 10% discount to the 20 day volume weighted average price with a minimum conversion price of 0.4 cents.

These amendments were approved at a shareholders meeting held on 25 August 2011.

**(iii) SC 54A Farmin**

On 11 July 2011 the Company announced that it has selected its preferred farminee party ("Party") for entry into SC 54A. The Party has completed technical due diligence and is in the process of working through its legal due diligence.

A condition of the farm-in negotiations requires the identity of the Party together with the terms of the farm-in agreement to remain confidential until the necessary documents have been executed.

The transaction contemplated will result in Kairiki reducing its interest in SC 54A from 30.1% to 15.05% in return for a funded work programme involving drilling within the permit.

No other matters or circumstances have arisen since the end of the financial year which significantly affected or may significantly affect the operations of the Group, the results of those operations, or the state of affairs of the Group in future financial years.

***FUTURE DEVELOPMENTS***

Kairiki intends to continue to explore its acreage in SC 54A and SC 54B. Any Final Investment Decision of future projects will consider the oil price forecasts and other economic and technical factors affecting the developments.

**REMUNERATION REPORT (AUDITED)**

This report details the nature and amount of remuneration for each Director and Executive of Kairiki Energy Limited. The information provided in the remuneration report includes remuneration disclosures that are audited as required by section 308(3C) of the Corporations Act 2001.

For the purposes of this report Key Management Personnel of the Group are defined as those persons having authority and responsibility for planning, directing and controlling the major activities of the group, directly or indirectly, including any director (whether executive or otherwise) of the parent company, and includes five executives in the Group receiving the highest remuneration.

For the purposes of this report the term "executive" includes those key management personnel who are not Directors of the parent company.

**Remuneration Committee**

The full Board carries out the role and responsibilities of the Remuneration Committee and is responsible for determining and reviewing the compensation arrangements for the Directors themselves, the Managing Director and any Executives.

Executive remuneration is reviewed annually having regard to individual and business performance, relevant comparative remuneration and internal and independent external advice.

**A. Remuneration policy**

The board policy is to remunerate Directors at market rates for time, commitment and responsibilities. The board determines payments to the Directors and reviews their remuneration annually, based on market practice, duties and accountability. Independent external advice is sought when required. The maximum aggregate amount of Directors' fees that can be paid is subject to approval by shareholders in general meeting, from time to time. Fees for Non-Executive Directors are not linked to the performance of the consolidated entity. However, to align Directors' interests with shareholders' interests, the Directors are encouraged to hold shares in the Company.

The Company's aim is to remunerate at a level that will attract and retain high-calibre Directors and employees. Company officers and directors are remunerated to a level consistent with the size of the company.

The Executive Directors and full time executives receive a superannuation guarantee contribution required by the government, which is currently 9%, and do not receive any other retirement benefits. Some individuals, however, may choose to sacrifice part of their salary to increase payments towards superannuation.

All remuneration paid to directors and executives is valued at the cost to the Company and expensed.

The Board believes that it has implemented suitable practices and procedures that are appropriate for an organisation of this size and maturity.

The Company did not pay any performance-based component of remuneration during the year.

**B. Remuneration structure**

In accordance with best practice corporate governance, the structure of Non-Executive Director and Executive compensation is separate and distinct.

**Non-Executive Director Compensation**

*Objective*

The Board seeks to set aggregate compensation at a level that provides the company with the ability to attract and retain Directors of the highest calibre, whilst incurring a cost that is acceptable to shareholders.

*Structure*

The Constitution and the ASX Listing Rules specify that the aggregate compensation of Non-Executive Directors shall be determined from time to time by a general meeting. An amount not exceeding the amount determined is then divided between the Directors as agreed. The latest determination was at the Annual General Meeting held in October 1996 when shareholders approved an aggregate compensation of \$150,000 per year.

DIRECTORS' REPORT

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The amount of aggregate compensation sought to be approved by shareholders and the manner in which it is apportioned amongst Directors is reviewed annually. The Board considers advice from external consultants as well as the fees paid to Non-Executive Directors of comparable companies when undertaking the annual review process. Non-Executive Directors' remuneration may include an incentive portion consisting of options, as considered appropriate by the Board, which may be subject to Shareholder approval in accordance with ASX listing rules. The Board is of the view that options are a cost effective benefit for small companies such as Kairiki that seek to conserve cash reserves. They also provide an incentive that ultimately benefits both shareholders and the option holder, as option holders will only benefit if the market value of the underlying shares exceeds the option strike price. Ultimately, shareholders will make that determination.

Separate from their duties as Directors, the Non-Executive Directors undertake work for the Company directly related to the evaluation and implementation of various business opportunities, including oil and gas exploration and new business ventures, for which they receive a daily rate. These payments are made pursuant to consultancy agreements entered into by the Non-Executive Directors with the Company and are not taken into account when determining their aggregate remuneration levels.

### **Executive Compensation**

#### *Objective*

The entity aims to reward Executives with a level and mix of compensation commensurate with their position and responsibilities within the entity so as to:

- reward Executives for company and individual performance against targets set by appropriate benchmarks;
- align the interests of Executives with those of shareholders;
- link rewards with the strategic goals and performance of the Company; and
- ensure total compensation is competitive by market standards.

#### *Structure*

In determining the level and make-up of Executive remuneration, the Board negotiates a remuneration to reflect the market salary for a position and individual of comparable responsibility and experience. Due to the limited size of the Company and of its operations and financial affairs, the use of a separate remuneration committee is not considered appropriate. Remuneration is regularly compared with the external market by participation in industry salary surveys and during recruitment activities generally. If required, the Board may engage an external consultant to provide independent advice in the form of a written report detailing market levels of remuneration for comparable Executive roles.

Remuneration consists of a fixed remuneration and a long term incentive portion as considered appropriate.

Compensation may consist of the following key elements:

- Fixed Compensation;
- Variable Compensation;
- Short Term Incentive (STI); and
- Long Term Incentive (LTI).

#### *Fixed Remuneration*

The level of fixed remuneration is set so as to provide a base level of remuneration which is both appropriate to the position and is competitive in the market. Fixed remuneration is reviewed annually by the Board having regard to the Company and individual performance, relevant comparable remuneration in the oil and gas industry and external advice.

The fixed remuneration is a base salary or monthly consulting fee.

#### *Variable Pay — Long Term Incentives*

The objective of long term incentives is to reward Directors/Executives in a manner which aligns this element of remuneration with the creation of shareholder wealth. The incentive portion is payable based upon attainment of objectives related to the Director's/Executive's job responsibilities. The objectives vary, but all are targeted to relate directly to the Company's business and financial performance and thus to shareholder value.

DIRECTORS' REPORT

Long term incentives (LTIs) granted to Directors/Executives are delivered in the form of options.

LTI grants to Executives are delivered in the form of share options. These options are issued at an exercise price and with vesting conditions determined by the Board at the time of issue.

The objective of the granting options is to reward Executives in a manner which aligns the element of remuneration with the creation of shareholder wealth. As such LTIs are made to Executives who are able to influence the generation of shareholder wealth and thus have an impact on the Company's performance.

The level of LTI granted is, in turn, dependent on the Company's recent share price performance, the seniority of the Executive and the responsibilities the Executive assumes in the Company.

Typically, the grant of LTIs occurs at the commencement of employment or in the event that the individual receives a promotion and, as such, is not subsequently affected by the individual's performance over time.

**C. Service agreements**

The following Key Management Personnel are employed under rolling contracts:

	<b>Notice Period</b>
<b>Directors</b>	
Paul Fry	1 month
Mark Fenton	3 months

The terms of service with Neville Bassett and Duncan Maclean are not formalised in a contract.

On resignation, any LTI options that have vested or that will vest during the notice period will be released. LTI options that have not yet vested will be forfeited.

**D. Details of remuneration for year**

Details of key management personnel are set out below.

**Directors**

Paul Fry	Chairman (Non-Executive)
Mark Fenton	Managing Director
Duncan Maclean	Director (Non-Executive) – appointed 31 March 2011
Neville Bassett	Director (Non-Executive) – appointed 28 September 2010, resigned 31 March 2011
John Morton	Director (Non-Executive) – appointed 25 August 2010, resigned 28 September 2010
Lawrence Brown	Director (Executive) – resigned 30 August 2010
Jyn Sim Baker	Director (Non-Executive) – resigned 25 August 2010

**Executives**

Neville Bassett	Company Secretary
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No other persons fulfilled the role of key management personnel.

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**DIRECTORS' REPORT**

**Remuneration**

Details of the remuneration of each Director and named executive officer of the Company, including their related entities, during the year was as follows:

	Year	Short Term Benefits		Post Employment	Share-based Payments	Total	Remuneration consisting of options during the year %
		Salary and consulting fees \$	Director fees \$	Superannuation \$	Options \$		
<b>Directors</b>							
P Fry	2011	146,789	-	13,211	36,406	196,406	18.5%
	2010	275,282	-	24,775	-	300,057	-
M Fenton Appointed 1/12/2009	2011	323,760	-	3,240	58,250	385,250	15.1%
	2010	290,110	-	1,890	-	292,000	-
D Maclean Appointed 31/3/2011	2011	-	12,000	-	21,844	33,844	64.5%
	2010	-	-	-	-	-	-
J Morton Appointed 25/8/2010 Resigned 28/9/2010	2011	-	-	-	-	-	-
	2010	-	-	-	-	-	-
L Brown Resigned 30/8/2010	2011	22,309	-	2,008	-	24,317	-
	2010	194,760	-	7,703	-	202,463	-
J Baker <sup>(i)</sup> Resigned 25/8/2010	2011	-	8,332	-	-	8,332	-
	2010	-	86,132	-	87,696	173,828	50.4%
R Jefferies Resigned 18/8/2009	2011	-	-	-	-	-	-
	2010	-	4,500	-	-	4,500	-
<b>Executives</b>							
N Bassett <sup>(ii)</sup>	2011	42,028	-	2,972	21,844	66,844	32.7%
	2010	36,000	-	-	-	36,000	-

- (i) Ms Baker's director's fees were paid to IMC Australia Pty Ltd. Her director's fees for 2010 included an amount of \$36,132 relating to the previous financial year.
- (ii) Mr Bassett was appointed as a Director on 28 September 2010 and resigned as a Director on 31 March 2011. He continued as Company Secretary during this period.

There were no performance related payments made during the year. Performance hurdles are not attached to remuneration options, however, the Board determines appropriate vesting periods to provide rewards over a period of time to key management personnel.

DIRECTORS' REPORT

**E. Compensation Options to Key Management Personnel**

The following options were granted as equity compensation benefits to Key Management Personnel. The options were issued free of charge. Each option entitles the holder to subscribe for one fully paid ordinary share in the Company.

**Terms and Conditions of Each Grant**

2011	<i>Number Vested During Year</i>	<b>Terms and Conditions of Each Grant</b>					
		<i>Granted Number</i>	<i>Grant Date</i>	<i>Value per Option at Grant Date \$</i>	<i>Exercise Price \$</i>	<i>First Exercise Date</i>	<i>Last Exercise Date</i>
<b>Directors</b>							
	-	12,500,000	16/5/2011	0.023	0.065	16/5/2012	16/5/2014
	-	20,000,000	16/5/2011	0.023	0.065	16/5/2012	16/5/2014
	-	7,500,000	16/5/2011	0.023	0.065	16/5/2012	16/5/2014
<b>Executives</b>							
	-	7,500,000	16/5/2011	0.023	0.065	16/5/2012	16/5/2014
	-	47,500,000					

**Terms and Conditions of Each Grant**

2010	<i>Number Vested During Year</i>	<b>Terms and Conditions of Each Grant</b>					
		<i>Granted Number</i>	<i>Grant Date</i>	<i>Value per Option at Grant Date \$</i>	<i>Exercise Price \$</i>	<i>First Exercise Date</i>	<i>Last Exercise Date</i>
<b>Directors</b>							
	-	2,000,000	14/12/2009	0.081	0.15	14/12/2010	14/12/2012
	-	2,000,000					

(i) These options were forfeited on 25 August 2010 upon Ms Baker's resignation.

The Binomial Option Pricing Model was used to value the options issued as share-based payments. Refer to Note 20 'Share-based payments' in the Notes to the financial statements for variables used in the models.

DIRECTORS' REPORT

**F. Shares Issued to Key Management Personnel on Exercise of Compensation Options**

No key management personnel exercised options during the years ended 30 June 2011 or 30 June 2010.

**SHARES UNDER OPTION**

Unissued ordinary shares of the Company under option at the date of this report are as follows:

	<i>Number</i>	<i>Exercise Price</i>	<i>Exercise Date</i>
Listed Options	750,133,177	0.4 cents	Between 1/6/2013 and 30/6/2013
Unlisted Options	49,000,000	6.5 cents	Between 16/5/2012 and 16/5/2014

In addition, under the Convertible Notes the note holder, IMC, has the option to convert the Notes into ordinary fully paid shares of the Company at a conversion price based on a 10% discount to the 20 day volume weighted average price with a minimum conversion price of 0.4 cents. The Convertible Notes mature in September and October 2013.

The maximum number of ordinary fully paid shares that IMC may receive on converting the Notes as at the date of this report is 1,604,486,448 shares.

**ENVIRONMENTAL REGULATIONS**

The Group's environmental obligations are regulated under both State and Federal law. All environmental performance obligations are monitored by the Board and subjected from time to time to Government agency audits and site inspections. The Company has a policy of at least complying with, but in most cases exceeding, its statutory environmental performance obligations. No environmental breaches have occurred or have been notified by any Government agencies during the year ended 30 June 2011 or subsequent to year end.

**CORPORATE GOVERNANCE**

In recognising the need for the highest standards of corporate behaviour and accountability, the Directors of Kairiki Energy Limited support and have adhered to the principles of corporate governance and have established a set of policies and manuals for the purpose of managing corporate governance. The Company's detailed corporate governance policy statement is contained in the section headed 'Corporate Governance Statement' of the annual report.

**INSURANCE OF OFFICERS**

The Company has in place an insurance policy insuring Directors and Officers of the Company against any liability arising from a claim brought by a third party against its Directors and Officers, and against liabilities for costs and expenses incurred by them in defending any legal proceedings arising out of their conduct while acting in their capacity as a Director or Officer of the Company, other than conduct involving a wilful breach of duty in relation to the Company.

In accordance with a confidentiality clause under the insurance policy, the amount of the premium paid to the insurers or the limit of liability covered by the policy has not been disclosed. This is permitted under Section 300(9) of the Corporations Act 2001.

**ROUNDING**

The amounts contained in this report and in the financial statements have been rounded to the nearest \$1,000 (where rounding is applicable) under the option available to the Company under ASIC Class Order 98/0100. The Company is an entity to which the Class Order applies.

DIRECTORS' REPORT

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**AUDITOR INDEPENDENCE AND NON-AUDIT SERVICES**

No non-audit services were provided by the Company's auditors.

**Auditors' independence – Section 307C**

The following is a copy of a letter received from the Company's auditors:



Level 18, Central Park Building, 152-158 St Georges Terrace, Perth WA 6000  
P.O. Box 8716, Perth Business Centre WA 6849  
Phone (08) 6364 5076 www.rothsay.com.au

The Directors  
Kairiki Energy Limited  
331-335 Hay Street  
Subiaco WA 6008

Dear Sirs

In accordance with Section 307C of the Corporations Act 2001 (the "Act") I hereby declare that to the best of my knowledge and belief there have been:

- i) no contraventions of the auditor independence requirements of the Act in relation to the audit of the 30 June 2011 financial statements; and
- ii) no contraventions of any applicable code of professional conduct in relation to the audit.

A handwritten signature in blue ink, appearing to read 'G Swan'.

Graham Swan (Lead auditor)

Rothsay Chartered Accountants

Dated 29 September 2011



Chartered Accountants

Liability limited by the Accountants Scheme, approved  
under the Professional Standards Act 1994 (NSW).

This report is made in accordance with a resolution of the Directors.

For and on behalf of the Board.

A handwritten signature in black ink, appearing to read 'Mark Fenton'.

**Dr Mark Fenton**  
Managing Director  
Perth Western Australia  
29 September 2011

# KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES

## CORPORATE GOVERNANCE STATEMENT

The Board of Directors of Kairiki Energy Limited is responsible for the corporate governance of the Company. The Board guides and monitors the business and affairs of Kairiki Energy Limited on behalf of the shareholders by whom they are elected and to whom they are accountable. This statement reports on Kairiki Energy Limited's key governance principles and practices.

### 1. COMPLIANCE WITH BEST PRACTICE RECOMMENDATIONS

The Company, as a listed entity, must comply with the Corporations Act 2001 and the ASX Limited (ASX) Listing Rules. The ASX Listing Rules require the Company to report on the extent to which it has followed the Corporate Governance Recommendations published by the ASX Corporate Governance Council (ASXCGC). Where a recommendation has not been followed, that fact is disclosed, together with the reasons for the departure.

The table below summaries the Company's compliance with the Corporate Governance Council's Recommendations:

Principle #	ASX Corporate Governance Council Recommendations	Reference	Comply
<b>Principle 1</b>	<b>Lay solid foundations for management and oversight</b>		
1.1	Establish the functions reserved to the board and those delegated to senior executives and disclose those functions.	2(a)	Yes
1.2	Disclose the process for evaluating the performance of senior executives.	2(h), 3(b), Remuneration Report	Yes
1.3	Provide the information indicated in the Guide to reporting on principle 1.	2(a), 2(h), 3(b), Remuneration Report	Yes
<b>Principle 2</b>	<b>Structure the board to add value</b>		
2.1	A majority of the board should be independent directors.	2(b), 2(e)	No
2.2	The chair should be an independent director.	2(c), 2(e)	No
2.3	The roles of chair and chief executive officer should not be exercised by the same individual.	2(b), 2(c)	Yes
2.4	The Board should establish a nomination committee.	2(d)	No
2.5	Disclose the process for evaluating the performance of the Board, its committees and individual directors.	2(h)	Yes
2.6	Provide the information indicated in the Guide to reporting on principle 2.	2(b), 2(c), 2(d), 2(e), 2(h)	Yes
<b>Principle 3</b>	<b>Promote ethical and responsible decision-making</b>		
3.1	Establish a code of conduct and disclose the code or a summary as to:	4(a)	Yes
	<ul style="list-style-type: none"> <li>• the practices necessary to maintain confidence in the company's integrity;</li> <li>• the practices necessary to take into account the company's legal obligations and the reasonable expectations of its stakeholders; and</li> <li>• the responsibility and accountability of individuals for reporting and investigating reports of unethical practices.</li> </ul>		
3.2	Establish a policy concerning trading in company securities by directors, senior executives and employees and disclose the policy or a summary of that policy.	4(b)	Yes
3.3	Provide the information indicated in the Guide to reporting on principle 3.	4(a), 4(b)	Yes
<b>Principle 4</b>	<b>Safeguard integrity in financial reporting</b>		
4.1	The Board should establish an audit committee.	3(a)	Yes
4.2	The audit committee should be structured so that it:	3(a)	No
	<ul style="list-style-type: none"> <li>• consists only of non-executive directors;</li> <li>• consists of a majority of independent directors;</li> <li>• is chaired by an independent chair, who is not chair of the Board; and</li> <li>• has at least three members.</li> </ul>		

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**CORPORATE GOVERNANCE STATEMENT**

<b>Principle #</b>	<b>ASX Corporate Governance Council Recommendations</b>	<b>Reference</b>	<b>Comply</b>
4.3	The audit committee should have a formal charter.	3(a)	Yes
4.4	Provide the information indicated in the Guide to reporting on principle 4.	3(a)	Yes
<b>Principle 5</b>			
<b>Make timely and balanced disclosure</b>			
5.1	Establish written policies designed to ensure compliance with ASX Listing Rule disclosure requirements and to ensure accountability at senior executive level for that compliance and disclose those policies or a summary of those policies.	5(a), 5(b)	Yes
5.2	Provide the information indicated in the Guide to reporting on principle 5.	5(a), 5(b)	Yes
<b>Principle 6</b>			
<b>Respect the rights of shareholders</b>			
6.1	Design a communications policy for promoting effective communication with shareholders and encouraging their participation at general meetings and disclose the policy or a summary of that policy.	5(a), 5(b)	Yes
6.2	Provide the information indicated in the Guide to reporting on principle 6.	5(a), 5(b)	Yes
<b>Principle 7</b>			
<b>Recognise and manage risk</b>			
7.1	Establish policies for the oversight and management of material business risks and disclose a summary of those policies.	6(a)	Yes
7.2	The Board should require management to design and implement the risk management and internal control system to manage the company's material business risks and report to it on whether those risks are being managed effectively. The Board should disclose that management has reported to it as to the effectiveness of the company's management of its material business risks.	6(a), 6(b), 6(d)	Yes
7.3	The Board should disclose whether it had received assurance from the chief executive officer and the chief financial officer that the declaration provided in accordance with section 295A of the Corporations Act is founded on a sound system of risk management and internal control and that the system is operating effectively in all material respects in relation to financial reporting risks.	6(c)	Yes
7.4	Provide the information indicated in the Guide to reporting on principle 7.	6(a), 6(b), 6(c), 6(d)	Yes
<b>Principle 8</b>			
<b>Remunerate fairly and responsibly</b>			
8.1	The Board should establish a remuneration committee.	3(b)	No
8.2	Clearly distinguish the structure of non-executive directors' remuneration from that of executive directors and senior executives.	3(b), Remuneration Report	Yes
8.3	Provide the information indicated in the Guide to reporting on principle 8.	3(b),	Yes

**2. THE BOARD OF DIRECTORS**

**2(a) Roles and Responsibilities of the Board**

The Board is accountable to the shareholders and investors for the overall performance of the Company and takes responsibility for monitoring the Company's business and affairs and setting its strategic direction, establishing and overseeing the Company's financial position.

The Board is responsible for:

- ensuring the Company's conduct and activities are ethical and carried out for the benefit of all its stakeholders;
- development of corporate strategy, implementation of business plans and performance objectives;
- reviewing, ratifying and monitoring systems of risk management, codes of conduct and legal and regulatory compliance;
- the appointment of the Company's Managing Director, Chief Executive Officer (or equivalent), Chief Financial Officer, Company Secretary and other senior executives;

- monitoring senior executives' performance and implementation of strategy;
- determining appropriate remuneration policies;
- allocating resources and ensuring appropriate resources are available to management;
- approving and monitoring the annual budget, progress of major capital expenditure, capital management, and acquisitions and divestitures; and
- approving and monitoring financial and other reporting.

Other than as specifically reserved to the Board, responsibility for the day-to-day management of the Company's business activities is delegated to the Managing Director and Executive Management.

## **2(b) Board Composition**

The Directors determine the composition of the Board employing the following principles:

- the Board, in accordance with the Company's constitution, must comprise a minimum of three Directors;
- the roles of the Chairman of the Board and of the Managing Director should be exercised by different individuals;
- the majority of the Board should comprise Directors who are non-executive;
- the Board should represent a broad range of qualifications, experience and expertise considered of benefit to the Company; and
- the Board must be structured in such a way that it has a proper understanding of, and competency in, the current and emerging issues facing the Company, and can effectively review management's decisions.

The Board is currently comprised of two Non-Executive Directors and one Executive Director.

The skills, experience, expertise, qualifications and terms of office of each Director in office at the date of the annual report are included in the Directors' Report.

The Company's constitution requires one-third of the Directors (or the next lowest whole number) to retire by rotation at each Annual General Meeting (AGM). The Directors to retire at each AGM are those who have been longest in office since their last election. Where Directors have served for equal periods, they may agree amongst themselves or determine by lot who will retire. A Director must retire in any event at the third AGM since he or she was last elected or re-elected. Retiring Directors may offer themselves for re-election.

A Director appointed as an additional or casual Director by the Board will hold office until the next AGM when they may be re-elected.

The Managing Director is not subject to retirement by rotation and, along with any Director appointed as an additional or casual Director, is not to be taken into account in determining the number of Directors required to retire by rotation.

## **2(c) Chairman and Managing Director**

The Chairman is responsible for:

- leadership of the Board;
- the efficient organisation and conduct of the Board's functions;
- the promotion of constructive and respectful relations between Board members and between the Board and management;
- contributing to the briefing of Directors in relation to issues arising at Board meetings;
- facilitating the effective contribution of all Board members; and
- committing the time necessary to effectively discharge the role of the Chairman.

The Managing Director is responsible for:

- implementing the Company's strategies and policies; and
- the day-to-day management of the Company's business activities.

The Board specifies that the roles of the Chairman and the Managing Director are separate roles to be undertaken by separate people.

**2(d) Nomination Committee**

The Company does not comply with ASX Recommendation 2.4. The Company is not of a relevant size to consider formation of a nomination committee to deal with the selection and appointment of new Directors and as such a nomination committee has not been formed.

Nominations of new Directors are considered by the full Board. If any vacancies arise on the Board, all Directors are involved in the search and recruitment of a replacement. The Board has taken a view that the full Board will hold special meetings or sessions as required. The Board is confident that this process for selection and review is stringent and full details of all Directors are provided to shareholders in the annual report and on the Company's website.

**2(e) Independent Directors**

The Company recognises that independent Directors are important in assuring shareholders that the Board is properly fulfilling its role and is diligent in holding senior management accountable for its performance. The Board assesses each of the Directors against specific criteria to decide whether they are in a position to exercise independent judgment.

Directors of Kairiki Energy Limited are considered to be independent when they are independent of management and free from any business or other relationship that could materially interfere with, or could reasonably be perceived to materially interfere with, the exercise of their unfettered and independent judgement.

In making this assessment, the Board considers all relevant facts and circumstances. Relationships that the Board will take into consideration when assessing independence are whether a Director:

- is a substantial shareholder of the Company or an officer of, or otherwise associated directly with, a substantial shareholder of the Company;
- is employed, or has previously been employed in an executive capacity by the Company or another Company member, and there has not been a period of at least three years between ceasing such employment and serving on the Board;
- has within the last three years been a principal of a material professional advisor or a material consultant to the Company or another Company member, or an employee materially associated with the service provided;
- is a material supplier or customer of the Company or other Company member, or an officer of or otherwise associated directly or indirectly with a material supplier or customer; or
- has a material contractual relationship with the Company or another Company member other than as a Director.

The Board currently includes two Non-Executive Directors, however, Mr Fry is not considered independent under the guidelines in Recommendation 2.1 Box 2.1 'Relationships affecting independent status', as he has previously been employed in an executive capacity by the Company in the last three years.

The following persons were directors of Kairiki Energy Limited during and subsequent to the end of the financial year:

Paul Fry	Chairman (Non-Executive)
Mark Fenton	Managing Director
Duncan Maclean	Director (Non-Executive) – appointed 31 March 2011
Neville Bassett	Director (Non-Executive) – appointed 28 September 2010, resigned 31 March 2011
John Morton	Director (Non-Executive) – appointed 25 August 2010, resigned 28 September 2010
Lawrence Brown	Director (Executive) – resigned 30 August 2010
Jyn Sim Baker	Director (Non-Executive) – resigned 25 August 2010

The Board does not currently comprise, and has not at any point during the year been comprised, of a majority of independent Non-Executive Directors. Given the size and scale of the Company's current operations, the Board does not consider it essential to appoint further independent Directors at this time. The Board will continue to monitor the need to appoint additional Non-Executive Directors, as considered appropriate.

The Board recognises the importance of independent views and, given the Board's role in supervising the activities of management, that the Chairman should be an independent, Non-Executive Director. The Board considers that at this stage of the Company's development, the non-executive role carried out by the Chairman, although not considered independent, is in the best interests of the Company.

**2(f) Avoidance of conflicts of interest by a Director**

In order to ensure that any interests of a Director in a particular matter to be considered by the Board are known by each Director, each Director is required by the Company to disclose any relationships, duties or interests held that may give rise to a potential conflict. Directors are required to adhere strictly to constraints on their participation and voting in relation to any matters in which they may have an interest.

**2(g) Board access to information and independent advice**

Directors are able to access members of the management team at any time to request relevant information.

There are procedures in place, agreed by the Board, to enable Directors, in furtherance of their duties, to seek independent professional advice at the company's expense.

**2(h) Review of Board performance**

The performance of the Board is reviewed regularly by the Chairman. The Chairman conducts performance evaluations which involve an assessment of each Board member's performance against specific and measurable qualitative and quantitative performance criteria. The Board member assessment measures are the responsibility of the Chairman. The performance criteria against which directors and executives are assessed is aligned with the financial and non-financial objectives of Kairiki Energy Limited. Primarily, the review will be carried out through consultation by the Chairman and with individual Directors. Directors whose performance is consistently unsatisfactory may be asked to retire.

**3. BOARD COMMITTEES**

**3(a) Audit Committee**

Given the size and scale of the Company's operations the full Board undertakes the role of the Audit Committee. The Audit Committee does not comply with ASX Recommendation 4.2 as the Chair of the Board is Chair of the Audit Committee and the Audit Committee does not comprise only Non-Executive Directors. The role and responsibilities of the Audit Committee are summarised below.

The Audit Committee is responsible for reviewing the integrity of the Company's financial reporting and overseeing the independence of the external auditors. The Board sets aside time to deal with issues and responsibilities usually delegated to the Audit Committee to ensure the integrity of the financial statements of the Company and the independence of the auditor.

The Board reviews the audited annual and half-year financial statements and any reports which accompany published financial statements and recommends their approval to the members. The Board also reviews annually the appointment of the external auditor, their independence and their fees.

The Board is also responsible for establishing policies on risk oversight and management. The Company has not formed a separate Risk Management Committee due to the size and scale of its operations.

*External Auditors*

The Company's policy is to appoint external auditors who clearly demonstrate quality and independence. The performance of the external auditor is reviewed annually and applications for tender of external audit services are requested as deemed appropriate, taking into consideration assessment of performance, existing value and tender costs. It is Rothsay's policy to rotate engagement directors on listed companies at least every five years.

An analysis of fees paid to the external auditors, including a breakdown of fees for non-audit services, is provided in the notes to the financial statements in the Annual Report.

There is no indemnity provided by the company to the auditor in respect of any potential liability to third parties.

The external auditor is requested to attend the annual general meeting and be available to answer shareholder questions about the conduct of the audit and preparation and content of the audit report.

There were no non-audit services provided by the auditors during the year.

**3(b) Remuneration Committee**

The role of a Remuneration Committee is to assist the Board in fulfilling its responsibilities in respect of establishing appropriate remuneration levels and incentive policies for employees.

The Board has not established a separate Remuneration Committee due to the size and scale of its operations. This does not comply with Recommendation 8.1, however the Board as a whole takes responsibility for such issues.

The responsibilities include setting policies for senior officers remuneration, setting the terms and conditions for the CEO, if any, reviewing and making recommendations to the Board on the Company's incentive schemes and superannuation arrangements, reviewing the remuneration of both Executive and Non-Executive Directors and undertaking reviews of the key management personnel performance.

The Company has structured the remuneration of its senior executive, where applicable, such that it comprises a fixed salary, statutory superannuation and, where applicable, participation in the Company's employee share option plan.

The Company believes that by remunerating senior executives in this manner it rewards them for performance and aligns their interests with those of shareholders and increases the Company's performance.

Non-Executive Directors are paid their fees out of the maximum aggregate amount approved by shareholders for Non-Executive Director remuneration. The Company does not adhere to Recommendation 8.2 Box 8.2 'Non-executive directors should not receive options or bonus payments'. The Company may, in the future, grant options to Non-Executive Directors. The Board is of the view that options (for both Executive and Non-Executive Directors) are a cost effective benefit for small companies such as Kairiki Energy Limited that seek to conserve cash reserves. They also provide an incentive that ultimately benefits both shareholders and the option holders, as option holders will only benefit if the market value of the underlying shares exceeds the option strike price. Ultimately, shareholders will make that determination.

The board policy is to remunerate Directors at market rates for time, commitment and responsibilities. The Board determines payments to the Directors and reviews their remuneration annually, based on market practice, duties and accountability. Independent external advice is sought when required. Fees for Non-Executive Directors are not linked to the performance of the consolidated entity. However, to align Directors' interests with shareholders' interests, the Directors are encouraged to hold shares in the Company.

The Company's aim is to remunerate at a level that will attract and retain high-calibre directors and employees. Company officers and Directors are remunerated to a level consistent with the size of the Company.

The Board believes that it has implemented suitable practices and procedures that are appropriate for an organisation of this size and maturity.

In accordance with best practice corporate governance, the structure of Non-Executive Director and Executive compensation is separate and distinct.

In determining remuneration, the Board has taken a view that the full Board will hold special meetings or sessions as required. No Director participated in any deliberation regarding his or her own remuneration or related issues. The Board is confident that this process for determining remuneration is stringent and full details of remuneration policies and remuneration received by Directors and executives in the current period is contained in the "Remuneration Report" within the Directors' Report of the Annual Report.

#### **4. ETHICAL AND RESPONSIBLE DECISION MAKING**

##### **4(a) Code of Ethics and Conduct**

The Board endeavours to ensure that the Directors, officers and employees of the Company act with integrity and observe the highest standards of behaviour and business ethics in relation to their corporate activities. The "Code of Conduct" sets out the principles, practices, and standards of personal behaviour the Company expects people to adopt in their daily business activities.

All Directors, officers and employees are required to comply with the Code of Conduct. Senior managers are expected to ensure that employees, contractors, consultants, agents and partners under their supervision are aware of the Company's expectations as set out in the Code of Conduct.

All Directors, officers and employees are expected to:

- comply with the law;
- act in the best interests of the Company;
- be responsible and accountable for their actions; and
- observe the ethical principles of fairness, honesty and truthfulness, including prompt disclosure of potential conflicts.

**4(b) Trading in Company Securities by Directors and Employees**

The Board has adopted a Securities Trading Policy which complies with the requirements of Listing Rule 12.12 which regulates dealings by Directors, officers and employees in securities issued by the Company.

The policy, which is available on the Company's website, includes the Company's closed periods, restrictions on trading that apply to the Company's key management personal, trading that is not subject to the policy, exceptional circumstances in which key management personnel may be permitted to trade during a prohibited period with prior written clearance and the procedure for obtaining written clearance. The policy provides that employees, directors and officers must not enter into transactions or arrangements which operate to limit the economic risk of their security holding in the Company without first seeking and obtaining written acknowledgement from the Board

**5. TIMELY AND BALANCED DISCLOSURE**

**5(a) Shareholder communication**

The Company believes that all shareholders should have equal and timely access to material information about the Company including its financial situation, performance, ownership and governance. The Company's "ASX Disclosure Policy" encourages effective communication with its shareholders by requiring that Company announcements:

- be factual and subject to internal vetting and authorisation before issue;
- be made in a timely manner;
- not omit material information;
- be expressed in a clear and objective manner to allow investors to assess the impact of the information when making investment decisions;
- be in compliance with ASX Listing Rules continuous disclosure requirements; and
- be placed on the Company's website promptly following release.

Shareholders are encouraged to participate in general meetings. Copies of addresses by the Chairman or Managing Director are disclosed to the market and posted on the Company's website. The Company's external auditor attends the Company's annual general meeting to answer shareholder questions about the conduct of the audit, the preparation and content of the audit report, the accounting policies adopted by the Company and the independence of the auditor in relation to the conduct of the audit.

**5(b) Continuous disclosure policy**

The Company is committed to ensuring that shareholders and the market are provided with full and timely information and that all stakeholders have equal opportunities to receive externally available information issued by the Company. The Company's "ASX Disclosure Policy" described in 5(a) reinforces the Company's commitment to continuous disclosure and outline management's accountabilities and the processes to be followed for ensuring compliance.

The policy also contains guidelines on information that may be price sensitive. The Company Secretary has been nominated as the person responsible for communications with the ASX. This role includes responsibility for ensuring compliance with the continuous disclosure requirements with the ASX Listing Rules and overseeing and coordinating information disclosure to the ASX.

**6. RECOGNISING AND MANAGING RISK**

The Board is responsible for ensuring there are adequate policies in relation to risk management, compliance and internal control systems. The Company's policies are designed to ensure strategic, operational, legal, reputation and financial risks are identified, assessed, effectively and efficiently managed and monitored to enable achievement of the Company's business objectives. A written policy in relation to risk oversight and management has been established ("Audit and Risk Management Charter"). Considerable importance is placed on maintaining a strong control environment. There is an organisation structure with clearly drawn responsibilities.

**6(a) Board oversight of the risk management system**

The Board is responsible for approving and overseeing the risk management system. The Board reviews, at least annually, the effectiveness of the implementation of the risk management controls and procedures.

The principal aim of the system of internal control is the management of business risks, with a view to enhancing the value of shareholders' investments and safeguarding assets. Although no system of internal control can provide absolute assurance that the business risks will be fully mitigated, the internal control systems have been designed to meet the Company's specific needs and the risks to which it is exposed.

Annually, the Board is responsible for identifying the risks facing the Company, assessing the risks and ensuring that there are controls for these risks, which are to be designed to ensure that any identified risk is reduced to an acceptable level.

The Board is also responsible for identifying and monitoring areas of significant business risk. Internal control measures currently adopted by the Board include:

- at least quarterly reporting to the Board in respect of operations and the Company's financial position, with a comparison of actual results against budget; and
- regular reports to the Board by appropriate members of the management team and/or independent advisers, outlining the nature of particular risks and highlighting measures which are either in place or can be adopted to manage or mitigate those risks.

**6(b) Risk management roles and responsibilities**

The Board is responsible for approving and reviewing the Company's risk management strategy and policy. Executive management is responsible for implementing the Board approved risk management strategy and developing policies, controls, processes and procedures to identify and manage risks in all of the Company's activities.

The Board is responsible for satisfying itself that management has developed and implemented a sound system of risk management and internal control.

**6(c) Chief Executive Officer and Chief Financial Officer Certification**

The Chief Executive Officer and Chief Financial Officer, or equivalent, provide to the Board written certification that in all material respects:

- The Company's financial statements present a true and fair view of the Company's financial condition and operational results and are in accordance with relevant accounting standards;
- The statement given to the Board on the integrity of the Company's financial statements is founded on a sound system of risk management and internal compliance and controls which implements the policies adopted by the Board; and
- The Company's risk management and internal compliance and control system is operating efficiently and effectively in all material respects.

**6(d) Internal review and risk evaluation**

Assurance is provided to the Board by executive management on the adequacy and effectiveness of management controls for risk on a regular basis.

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME  
FOR THE YEAR ENDED 30 JUNE 2011**

		Consolidated	
	Note	2011 \$'000	2010 \$'000
Revenue	2(a)	63	88
Other income	2(a)	227	922
		290	1,010
Administrative expenses	2(b)	1,974	1,751
Exploration expenses		1	49
Impairment of oil and gas properties		28,198	-
Impairment of deferred exploration and evaluation expenditure		10,212	-
Impairment of receivables for deferred consideration for the sale of interest in oil and gas permits		1,045	-
Finance costs	2(b)	1,866	2,155
		43,296	3,955
<b>Loss before income tax expense</b>		<b>(43,006)</b>	<b>(2,945)</b>
Income tax expense	3	-	-
<b>Loss after tax for the period</b>		<b>(43,006)</b>	<b>(2,945)</b>
<b>Other comprehensive income/(loss)</b>			
Foreign currency translation		(6,509)	(2,187)
<b>Total comprehensive loss attributable to members of Kairiki Energy Limited</b>		<b>(49,515)</b>	<b>(5,132)</b>
Basic and diluted loss per share (cents per share)	4	(5.22) cents	(0.57) cents

The above consolidated statement of comprehensive income should be read in conjunction with the accompanying notes.

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**CONSOLIDATED STATEMENT OF FINANCIAL POSITION**

AS AT 30 JUNE 2011

		<b>Consolidated</b>	
	Note	<b>2011</b>	<b>2010</b>
		<b>\$'000</b>	<b>\$'000</b>
<b>ASSETS</b>			
<b>Current Assets</b>			
Cash and cash equivalents	5	1,802	9,028
Trade and other receivables	6	54	2,786
Inventories	7	-	2,407
<b>Total Current Assets</b>		<b>1,856</b>	<b>14,221</b>
<b>Non-Current Assets</b>			
Plant and equipment	8	7	13
Oil and gas properties	9	-	13,787
Deferred exploration and evaluation expenditure	10	14,343	24,254
<b>Total Non-Current Assets</b>		<b>14,350</b>	<b>38,054</b>
<b>Total Assets</b>		<b>16,206</b>	<b>52,275</b>
<b>LIABILITIES</b>			
<b>Current Liabilities</b>			
Trade and other payables	11	2,897	4,312
Provisions	12	5	1,291
Convertible notes	13	6,967	-
<b>Total Current Liabilities</b>		<b>9,869</b>	<b>5,603</b>
<b>Non-Current Liabilities</b>			
Convertible notes	13	-	10,271
<b>Total Non-Current Liabilities</b>		<b>-</b>	<b>10,271</b>
<b>Total Liabilities</b>		<b>9,869</b>	<b>15,874</b>
<b>Net Assets</b>		<b>6,337</b>	<b>36,401</b>
<b>EQUITY</b>			
Issued capital	14	70,234	50,926
Reserves	15	(3,905)	2,461
Accumulated losses		(59,992)	(16,986)
<b>Total Equity</b>		<b>6,337</b>	<b>36,401</b>

The above consolidated statement of financial position should be read in conjunction with the accompanying notes.

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**CONSOLIDATED STATEMENT OF CHANGES IN EQUITY  
FOR THE YEAR ENDED 30 JUNE 2011**

<b>Consolidated</b>	<b>Issued Capital \$'000</b>	<b>Share- based Payments Reserve \$'000</b>	<b>Foreign Currency Translation Reserve \$'000</b>	<b>Accumulated Losses \$'000</b>	<b>Total \$'000</b>
<b>Balance at 30 June 2009</b>	44,844	2,888	1,811	(14,041)	35,502
Loss for the period	-	-	-	(2,945)	(2,945)
Other comprehensive loss	-	-	(2,187)	-	(2,187)
<b>Total comprehensive loss for the period</b>	-	-	(2,187)	(2,945)	(5,132)
Shares issued	6,669	-	-	-	6,669
Share issue transaction costs	(474)	-	-	-	(474)
Share-based payments	-	(51)	-	-	(51)
Repayment of convertible notes	(113)	-	-	-	(113)
<b>Balance at 30 June 2010</b>	<b>50,926</b>	<b>2,837</b>	<b>(376)</b>	<b>(16,986)</b>	<b>36,401</b>
Loss for the period	-	-	-	(43,006)	(43,006)
Other comprehensive loss	-	-	-	-	-
<b>Total comprehensive loss for the period</b>	-	-	<b>(6,509)</b>	<b>(43,006)</b>	<b>(49,515)</b>
Shares issued	20,928	-	-	-	20,928
Share issue transaction costs	(1,559)	-	-	-	(1,559)
Share-based payments	-	143	-	-	143
Repayment of convertible notes	(61)	-	-	-	(61)
<b>Balance at 30 June 2011</b>	<b>70,234</b>	<b>2,980</b>	<b>(6,885)</b>	<b>(59,992)</b>	<b>6,337</b>

The above consolidated statement of changes in equity should be read in conjunction with the accompanying notes.

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**CONSOLIDATED STATEMENT OF CASH FLOWS  
FOR THE YEAR ENDED 30 JUNE 2011**

	Note	<b>Consolidated</b>	
		<b>2011</b>	<b>2010</b>
		<b>\$'000</b>	<b>\$'000</b>
<b>Cash flows from operating activities</b>			
Payments to suppliers and employees		(1,930)	(1,615)
Exploration costs expensed		(1)	(49)
Interest received		63	88
Interest and other costs of finance paid		(1,153)	(1,475)
<b>Net cash used in operating activities</b>	5(i)	<b>(3,021)</b>	<b>(3,051)</b>
<b>Cash flows from investing activities</b>			
Expenditure on oil and gas properties		(26,090)	(9,409)
Receipts from sales of oil produced during extended well test		6,486	-
Expenditure on exploration and evaluation		(2,529)	(734)
Proceeds from the sale of interests in oil and gas permits		1,243	6,281
Payments for plant and equipment		(6)	(5)
<b>Net cash used in investing activities</b>		<b>(20,896)</b>	<b>(3,867)</b>
<b>Cash flows from financing activities</b>			
Proceeds from issues of shares		20,928	6,669
Payments for share issue transaction costs		(1,572)	(866)
Repayment of convertible notes		(1,982)	(1,023)
Restricted cash released		-	1,022
<b>Net cash provided by financing activities</b>		<b>17,374</b>	<b>5,802</b>
<b>Net increase / (decrease) in cash held</b>		<b>(6,543)</b>	<b>(1,116)</b>
Cash at the beginning of the financial year		9,028	10,087
Effect of exchange rate changes		(683)	57
<b>Cash and cash equivalents at end of year</b>	5	<b>1,802</b>	<b>9,028</b>

The above consolidated statement of cash flows should be read in conjunction with the accompanying notes.

**1. Summary of Significant Accounting Policies**

**(a) Corporate information**

The financial report of Kairiki Energy Limited (“Kairiki” or “the Company”) and its subsidiaries (“the Group”) for the year ended 30 June 2011 was authorised for issue in accordance with a resolution of the Directors on 29 September 2011.

Kairiki is a company limited by shares incorporated in Australia whose shares are publicly traded on the Australian Securities Exchange. The nature of the operations and principal activities of the Group are described in the Directors’ Report.

**(b) Basis of Presentation**

The financial report is a general purpose financial report, which has been prepared in accordance with the requirements of the Corporations Act 2001, Australian Accounting Standards and authoritative pronouncements of the Australian Accounting Standards Board. The financial report has been prepared on a historical cost basis, with the exception of derivative financial instruments, which are measured at fair value.

The financial report is presented in Australian dollars and all values are rounded to the nearest thousand dollars (\$’000) unless otherwise stated.

The Group experienced losses after income tax for the year of \$43,006,000, had net cash outflows from operating activities for the year of \$3,021,000 and had a working capital deficiency of \$8,013,000 including amounts due on the convertible note of \$6,967,000.

The ability of the Group to continue as a going concern is principally dependent upon the following:

- The successful commercial exploitation of the Group’s oil and gas resources;
- A farm-down or sale of its interest in SC 54A and SC 54B;
- Raising additional capital to fund the Group’s ongoing exploration and development program and working capital requirements, as and when required; and
- Meeting the terms of its convertible note agreement as outlined in note 13 and as amended subsequent to the end of the reporting period (refer to Note 26).

Subsequent to 30 June 2011 the following events occurred (refer to Note 26):

- An underwritten pro-rata renounceable rights issue raised equity proceeds of \$6,000,000 before issue costs;
- A number of amendments to the Convertible Note agreement were agreed with the Noteholder, including an extension of the repayment date by two years from September/October 2011 to September/October 2013; and
- The Company announced that it has selected its preferred farminee party for entry into SC 54A. The transaction contemplated will result in Kairiki reducing its interest in SC 54A from 30.1% to 15.05% in return for a funded work programme involving drilling within the permit.

As a result of the success of the above measures subsequent to year end, the financial report has been prepared on a going concern basis.

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**

**1. Summary of Significant Accounting Policies (continued)**

**(c) Statement of compliance**

The financial report complies with Australian Accounting Standards and International Financial Reporting Standards (IFRS).

**(d) Adoption of new and revised standards**

The Group has adopted the following new and amended Australian Accounting Standards and AASB Interpretations as of 1 July 2010.

- AASB 2009-5 Further Amendments to Australian Accounting Standards arising from the Annual Improvements Project
- AASB 2009-8 Amendments to Australian Accounting Standard – Group Cash-Settled Share-based Payment Transactions
- AASB 2009-10 Amendments to Australian Accounting Standard – Classification of Rights Issues
- AASB 2010-3 Amendments to Australian Accounting Standards arising from the Annual Improvements Project
- Interpretation 19 Extinguishing Financial Liabilities with Equity Instruments

The adoption of the above Standards and Interpretations did not have an impact on the financial statements or performance of the Group.

The Group has reviewed all of the Australian Accounting Standards and Interpretations that have recently been issued or amended but are not yet effective and have not been adopted by the Group for the annual reporting period ending 30 June 2010. These include the following:

Reference	Title	Summary	Application date of standard	Application date for Group
AASB 124 (Revised)	Related Party Disclosures (December 2009)	The revised AASB 124 simplifies the definition of a related party, clarifying its intended meaning and eliminating inconsistencies from the definition, including: <ul style="list-style-type: none"> <li>(a) the definition now identifies a subsidiary and an associate with the same investor as related parties of each other;</li> <li>(b) entities significantly influenced by one person and entities significantly influenced by a close member of the family of that person are no longer related parties of each other; and</li> <li>(c) the definition now identifies that, whenever a person or entity has both joint control over a second entity and joint control or significant influence over a third party, the second and third entities are related to each other.</li> </ul>	1 January 2011	1 July 2011
AASB 10	Consolidated Financial Statements	IRFS 10 establishes a new control model that applies to all entities. It replaces parts of IAS 27 Consolidated and Separate Financial Statements dealing with the accounting for consolidated financial statements and SIC-12 Consolidation – Special Purpose Entities.  The new control model broadens the situations when an entity is considered to be controlled by another entity and includes new guidance for applying the model to specific situations, including when acting as a manager may give control, the impact of potential voting rights and when holding less than a majority of voting rights may give control.	1 January 2013	1 July 2013

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**

**1. Summary of Significant Accounting Policies (continued)**

**(d) Adoption of new and revised standards (continued)**

Reference	Title	Summary	Application date of standard	Application date for Group
AASB 9 Financial Instruments	Amendments to Australian Accounting Standard – Financial Instruments and its associated amending standards	<p>AASB 9 includes requirements for the classification and measurement of financial assets resulting from the first part of Phase 1 of the IASB’s project to replace IAS 39 Financial Instruments: Recognition and Measurement (AASB 139: Financial Instruments: Recognition and Measurement).</p> <p>These requirements improve and simplify the approach for classification and measurement of financial assets compared with the requirements of AASB 139. The main changes from AASB 139 are described below.</p> <p>(a) Financial assets are classified based on:</p> <p style="margin-left: 20px;">(1) The objective of the entity’s business model for managing the financial assets;</p> <p style="margin-left: 20px;">(2) The characteristics of the contractual cash flows.</p> <p>(b) AASB 9 allows an irrevocable election on initial recognition to present gains and losses on investments in equity instruments that are not held for trading in other comprehensive income. Dividends in respect of these investments that are a return on investment can be recognised in profit or loss and there is no impairment or recycling on disposal of the instrument.</p> <p>(c) Financial assets can be designated and measured at fair value through profit or loss at initial recognition if doing so eliminates or significantly reduces a measurement or recognition inconsistency that would arise from measuring assets or liabilities, or recognising the gains and losses on them, on different bases.</p>	1 January 2013	1 July 2013
AASB 2009-11	Amendments to Australian Accounting Standards arising from AASB 9 [AASB 1, 3, 4, 5, 7, 101, 102, 108, 112, 118, 121, 127, 131, 132, 136, 139, 1023 & 1038 and Interpretations 10 & 12	These amendments arise from the issuance of AASB 9 <i>Financial Instruments</i> that sets out requirements for the classification and measurement of financial assets. The requirements in AASB 9 form part of the first phase of the International Accounting Standards Board’s project to replace IAS 39 <i>Financial Instruments: Recognition and Measurement</i> .	1 January 2013	1 July 2013
AASB 2009-12	Amendments to Australian Accounting Standards [AASB 5, 8, 108, 110, 112, 119, 133, 137, 139, 1023 & 1031 and Interpretations 2, 4, 16, 1039 & 1052]	<p>This amendment makes editorial changes to a range of Australian Accounting Standards and Interpretations.</p> <p>In particular, it amends AASB 8 <i>Operating Segments</i> to require an entity to exercise judgement in assessing whether a government and entities known to be under the control of that government are considered to be a single customer for the purposes of certain operating segment disclosures.</p>	1 January 2011	1 July 2011

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**

**1. Summary of Significant Accounting Policies (continued)**

**(d) Adoption of new and revised standards (continued)**

Reference	Title	Summary	Application date of standard	Application date for Group
AASB 2009-14	Amendments to Australian Interpretation – Prepayments of a Minimum Funding Requirement	<p>These amendments arise from the issuance of Prepayments of a Minimum Funding Requirement (Amendments to IFRIC 14). The requirements of IFRIC 14 meant that some entities that were subject to minimum funding requirements could not treat any surplus in a defined benefit pension plan as an economic benefit.</p> <p>The amendment requires entities to treat the benefit of such an early payment as a pension asset. Subsequently, the remaining surplus in the plan, if any, is subject to the same analysis as if no prepayment had been made.</p>	1 January 2011	1 July 2011
AASB 1053	Application of Tiers of Australian Accounting Standards	<p>This Standard establishes a differential financial reporting framework consisting of two Tiers of reporting requirements for preparing general purpose financial statements:</p> <ul style="list-style-type: none"> <li>• Tier 1: Australian Accounting Standards</li> <li>• Tier 2: Australian Accounting Standards – Reduced Disclosure Requirements</li> </ul> <p>Tier 2 comprises the recognition, measurement and presentation requirements of Tier 1 and substantially reduced disclosures corresponding to those requirements.</p> <p>The following entities apply Tier 1 requirements in preparing general purpose financial statements:</p> <ul style="list-style-type: none"> <li>(a) For-profit entities in the private sector that have public accountability (as defined in this Standard)</li> <li>(b) The Australian Government and State, Territory and Local Governments</li> </ul> <p>The following entities apply either Tier 2 or Tier 1 requirements in preparing general purpose financial statements:</p> <ul style="list-style-type: none"> <li>(a) For-profit private sector entities that do not have public accountability</li> <li>(b) All not-for-profit private sector entities</li> <li>(c) Public sector entities other than the Australian Government and State, Territory and Local Governments.</li> </ul>	1 July 2013	1 July 2013

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**

**1. Summary of Significant Accounting Policies (continued)**

**(d) Adoption of new and revised standards (continued)**

AASB 1054	Australian Additional Disclosures	<p>This Standard is as a consequence of phase 1 of the joint Trans-Tasman Convergence project of the AASB and FRSB.</p> <p>This Standard relocates all Australian specific disclosures from other standards to one place and revises disclosures in the following areas:</p> <ul style="list-style-type: none"> <li>(a) Compliance with Australian Accounting Standards</li> <li>(b) The statutory basis or reporting framework for financial statements</li> <li>(c) Whether the financial statements are general purpose or special purpose</li> <li>(d) Audit fees</li> <li>(e) Imputation credits</li> </ul>	1 July 2011	1 July 2011
AASB 2010-2	Amendments to Australian Accounting Standards arising from reduced disclosure requirements	This Standard gives effect to Australian Accounting Standards – Reduced Disclosure Requirements. AASB 1053 provides further information regarding the differential reporting framework and the two tiers of reporting requirements for preparing general purpose financial statements.	1 July 2013	1 July 2013
AASB 2010-4	Further Amendments to Australian Accounting Standards arising from the Annual Improvements Project [AASB 1, 7, 101 & 134 and Interpretation 13]	<p>Emphasises the interaction between quantitative and qualitative AASB 7 disclosures and the nature and extent of risks associated with financial instruments.</p> <p>Clarifies that an entity will present an analysis of other comprehensive income for each component of equity, either in the statement of changes in equity or in the notes to the financial statements.</p> <p>Provides guidance to illustrate how to apply disclosure principles in AASB 134 for significant events and transactions.</p>	1 January 2011	1 July 2011
AASB 2010-5	Amendments to Australian Accounting Standards [AASB 1, 3, 4, 5, 101, 107, 112, 118, 119, 121, 132, 133, 134, 137, 139, 140, 1023 & 1038 and Interpretations 112, 115, 127, 132 & 1042]	<p>This Standard makes numerous editorial amendments to a range of Australian Accounting Standards and Interpretations, including amendments to reflect changes made to the text of IFRS by the IASB.</p> <p>These amendments have no major impact on the requirements of the amended pronouncements.</p>	1 January 2011	1 July 2011
AASB 2010-6	Amendments to Australian Accounting Standards – Disclosures on Transfer of Financial Assets [AASB 1 & 7]	The amendments increase the disclosure requirements for transactions involving transfers of financial assets. They require enhancements to the existing disclosures in IFRS 7 where and asset is transferred but is not derecognised and introduce new disclosures for assets that are derecognised but the entity continues to have a continuing exposure to the asset after the sale.	1 July 2011	1 July 2011

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**

**1. Summary of Significant Accounting Policies (continued)**

**(d) Adoption of new and revised standards (continued)**

Reference	Title	Summary	Application date of standard	Application date for Group
AASB 2010-7	Amendments to Australian Accounting Standards arising from AASB 9 (December 2010) [AASB 1, 3, 4, 5, 101, 102, 108, 112, 118, 120, 121, 127, 128, 131, 132, 136, 137, 139, 1023 & 1038 and Interpretations 2, 5, 10, 12, 19 & 127]	<p>The requirements for classifying and measuring financial liabilities were added to AASB 9. The existing requirements for the classification of financial liabilities and the ability to use the fair value option have been retained. However, where the fair value option is used for financial liabilities, the change in fair value is accounted for as follows:</p> <ul style="list-style-type: none"> <li>• The change attributable to changes in credit risk are presented in other comprehensive income (OCI)</li> <li>• The remaining change is presented in profit or loss.</li> </ul> <p>If this approach creates or enlarges an accounting mismatch in the profit or loss, the effect of the changes in credit risk are also presented in profit or loss.</p>	1 January 2013	1 July 2013
AASB 2010-8	Amendments to Australian Accounting Standards – Deferred Tax: Recovery of Underlying Assets [AASB 12]	These amendments address the determination of deferred tax on investment property measured at fair value and introduce a rebuttable presumption that deferred tax on investment property measured at fair value should be determined on the basis that the carrying amount will be recoverable through sale. The amendments also incorporate <i>SIC-21 Income Taxes – Recovery of Revalued Non-Depreciable Assets</i> into AASB 112.	1 January 2012	1 July 2012
AASB 2011-1	Amendments to Australian Accounting Standards arising from the Trans-Tasman Convergence project [AASB 1, 5, 101, 107, 108, 121, 128, 132 & 134 and Interpretations 2, 112 & 113]	This Standard amends many Australian Accounting Standards, removing the disclosures which have been relocated to AASB 1054.	1 January 2011	1 July 2011
AASB 2011-2	Amendments to Australian Accounting Standards arising from the Trans-Tasman Convergence project – Reduced Disclosure Regime [AASB 101 & 1054]	This Standard makes amendments to the application of revised disclosures to Tier 2 entities that are applying AASB 1053.	1 January 2013	1 July 2013

The impact of the adoption of these new and revised standards and interpretations has not been determined by the Group.

**1. Summary of Significant Accounting Policies (continued)**

**(e) Basis of consolidation**

The consolidated financial statements comprise the financial statements of Kairiki Energy Limited (the “Company” or “parent entity”) and its subsidiaries as at 30 June each year (“the Group”).

Subsidiaries are fully consolidated from the date the Group obtains control until such time as control ceases. Control exists where the Group has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

The financial statements of the subsidiaries are prepared for the same period as the parent entity, using consistent accounting policies. In preparing the consolidated financial statements, all intercompany balances and transactions, income and expenses and profit and losses resulting from intra-group transactions are eliminated in full.

Investments in subsidiaries held by Kairiki Energy Limited are accounted for at cost in the separate financial statements of the parent entity, less any impairment charges.

The acquisition of subsidiaries is accounted for using the acquisition method of accounting. The acquisition method involves recognising at acquisition date, separately from goodwill, the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree. The identifiable assets acquired and the liabilities assumed are measured at their acquisition date fair values. The difference between the above items and the fair value of the consideration (including the fair value of any pre-existing investment in the acquiree) is goodwill or a discount on acquisition.

A change in the ownership interest of a subsidiary that does not result in a loss of control is accounted for as an equity transaction.

**(f) Foreign currency translation**

The financial statements are measured using the currency of the primary economic environment in which the entity operates (the ‘functional currency’). The functional currency of the parent entity Kairiki Energy Limited is United States Dollars, due to the Company’s US Dollar convertible note funding. As the Company is listed on the Australian Securities Exchange, its presentation currency is Australian Dollars.

The functional currency of subsidiary Yilgarn Petroleum Philippines Pty Ltd is also US Dollars. The functional currency of the other Australian subsidiaries is Australian Dollars.

Transactions in foreign currencies are initially recorded in the functional currency at the exchange rates ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are converted at the rate of exchange ruling at the reporting date.

As at the reporting date the assets and liabilities of the parent entity and the subsidiary with US dollar functional currency are translated into the presentation currency of Kairiki Energy Limited at the rate of exchange at the reporting date and the statements of comprehensive income are translated at the spot rate of the transactions or average exchange rates for the period.

The exchange differences arising on translation are recognised in the foreign currency translation reserve in equity. On disposal of a foreign entity, the deferred cumulative amount recognised in equity relating to that particular foreign operation is recognised in the statement of comprehensive income.

**(g) Significant Accounting Estimates and Judgments**

***Significant accounting judgments***

In the process of applying the Group’s accounting policies, management has made the following judgments, apart from those involving estimations, which have a significant effect on the amounts recognised in the financial statements.

***Exploration and evaluation assets***

The Group’s accounting policy for exploration and evaluation expenditure is set out at Note 1(1). The application of this policy necessarily requires management to make certain assumptions as to future events and circumstances. Any such assumptions may change as new information becomes available. If, after having capitalised expenditure under the policy, it is concluded that the expenditures are unlikely to be recovered by future exploitation or sale, then the relevant capitalised amount is written off to the statement of comprehensive income.

**1. Summary of Significant Accounting Policies (continued)****(g) Significant Accounting Estimates and Judgments (continued)*****Significant accounting estimates and assumptions***

The carrying amounts of certain assets and liabilities are often determined based on estimates and assumptions of future events. The key estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of certain assets and liabilities within the next annual reporting period are:

***(i) Impairment of assets***

In determining the recoverable amount of assets, in the absence of quoted market prices, estimations are made regarding the present value of future cash flows using asset-specific discount rates and a “value in use” discounted cash flow methodology. Additional disclosures are provided about the discount rate and any other significant assumptions. For oil and gas properties, expected future cash flow estimation is based on reserves, future production profiles, commodity prices and costs.

***(ii) Share-based payment transactions***

The Group measures the cost of equity-settled transactions with employees by reference to the fair value of the equity instruments at the date at which they are granted. The fair value is determined using a binomial model using the assumptions detailed in Note 20.

***(iii) Restoration obligations***

Where a restoration obligation exists, the Group estimates the future removal costs of offshore oil and gas platforms, production facilities, wells and pipelines at the time of installation of the assets. In most instances, removal of assets occurs many years into the future. This requires judgmental assumptions regarding removal date, future environmental legislation, the extent of reclamation activities required, the engineering methodology for estimating cost, future removal technologies in determining the removal cost and liability specific discount rates to determine the present value of these cash flows. For more detail regarding the policy in respect of the provision for restoration refer to Note 1(q).

***(iv) Valuation of convertible notes***

The Group issued convertible notes in September and October 2008, which contains a holder call option embedded derivative. The carrying value of the call option component was based on the residual value of the debt after subtracting the debt value from the face value of the debt.

**(h) Cash and cash equivalents**

Cash comprises cash at bank and in hand. Cash equivalents are short term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

For the purposes of the statement of cash flows, cash and cash equivalents consist of cash and cash equivalents as described above, net of outstanding bank overdrafts.

**(i) Trade and other receivables**

Trade receivables are recognised initially at fair value (generally the original invoice amount) and subsequently measured at amortised cost using the effective interest method, less an allowance for impairment.

Collectability of receivables is reviewed on an ongoing basis. Debts that are known to be uncollectable are written off when identified. An impairment provision is recognised when there is objective evidence that the Group will not be able to collect the receivable. Financial difficulties of the debtor, default payment or debts more than 60 days overdue are considered objective evidence of impairment. The amount of the impairment loss is the receivable carrying amount compared to the present value of estimated future cash flows, discounted at the effective interest rate.

Restricted cash is not due for settlement until rights of tenure are forfeited or performance obligations are met.

**1. Summary of Significant Accounting Policies (continued)**

**(j) Inventories**

Inventories are valued at the lower of cost and net realisable value.

Cost is determined as follows:

- (i) Materials, which include drilling and maintenance stocks, are valued at cost.
- (ii) Petroleum products, comprising extracted crude oil stored in FSO tanks, are valued using the full absorption cost method.

Inventories and material stocks are accounted for on a first in, first out (FIFO) basis.

Net realisable value is the estimated selling price in the ordinary course of business, less estimated costs of completion and the estimated costs necessary to make the sale.

**(k) Plant and equipment**

Plant and equipment is stated at cost less accumulated depreciation and any accumulated impairment losses.

Depreciation is calculated on a straight-line basis over the estimated useful life of the assets as follows:

Plant and equipment – 2 to 5 years

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

*Disposal*

An item of property, plant and equipment is derecognised upon disposal or when no further future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the statement of comprehensive income in the year the asset is derecognised.

**(l) Exploration and evaluation expenditure**

Costs related to the acquisition of properties that contain resources are allocated separately to specific areas of interest. These costs are capitalised until the viability of the area of interest is determined.

Exploration and evaluation expenditure is stated at cost and is accumulated in respect of each identifiable area of interest.

Such costs are only carried forward to the extent that they are expected to be recouped through the successful development of the area of interest (or alternatively by its sale), or where activities in the area have not yet reached a stage which permits a reasonable assessment of the existence or otherwise of economically recoverable reserves, and active operations are continuing. Accumulated costs in relation to an abandoned area are written off to the statement of comprehensive income in the period in which the decision to abandon the area is made.

The Directors review the carrying value of each area of interest as at the balance date and any exploration expenditure which no longer satisfies the above policy is written off.

Once an area of interest enters the development phase, all capitalised acquisition, exploration and evaluation expenditures are transferred to oil and gas properties.

**(m) Oil and Gas Properties**

*Assets in development*

When the technical and commercial feasibility of an undeveloped oil or gas field has been demonstrated the field enters its development phase. The costs of oil and gas assets are transferred from exploration and evaluation expenditure and reclassified into development phase and include past exploration and evaluation costs, development drilling and other subsurface expenditures, surface plant and equipment, and any associated land and buildings.

**1. Summary of Significant Accounting Policies (continued)****(m) Oil and Gas Properties (continued)***Producing assets*

The costs of oil and gas assets in production are separately accounted for as tangible assets, and include past exploration and evaluation costs, pre-production development costs and the ongoing costs of continuing to develop reserves for production and to expand or replace plant and equipment and any associated land and buildings. Depletion charges are calculated using a unit of production method which will amortise the cost of carried forward exploration, evaluation and development expenditure over the life of the estimated Proved plus Probable Reserves (2P), in a cash generating unit.

Provisions for future restoration are made where there is a present obligation as a result of development or production activity, and is capitalised as a component of the cost of those activities. The provision for restoration policy is discussed in full at Note 1(q).

**(n) Impairment of non-financial assets**

The Group assesses at each reporting date whether there is an indication that an asset may be impaired. Where an indicator of impairment exists, the Group makes a formal estimate of recoverable amount. Where the carrying amount of an asset exceeds its recoverable amount the asset is considered impaired and is written down to its recoverable amount.

Recoverable amount is the greater of fair value less costs to sell and value in use. It is determined for an individual asset, unless the asset's value in use cannot be estimated to be close to its fair value less costs to sell and it does not generate cash inflows that are largely independent of those from other assets or groups of assets, in which case, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

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 assessments of the time value of money and the risks specific to the asset.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but only to the extent that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years.

**(o) Investments and other financial assets**

Financial assets in the scope of AASB 139 *Financial Instruments: Recognition and Measurement* are classified as either financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, or available-for-sale investments, as appropriate. The classification depends on the purpose for which the investments were acquired or originated. Designation is re-evaluated at each reporting date, but there are restrictions on reclassifying to other categories.

When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transactions costs.

All regular way purchases and sales of financial assets are recognised on the trade date i.e. the date that the Group commits to purchase the asset. Regular way purchases or sales are purchases or sales of financial assets under contracts that require delivery of the assets within the period established generally by regulation or convention in the marketplace.

**(i) Financial assets at fair value through profit or loss**

Financial assets classified as held for trading are included in the category 'financial assets at fair value through profit or loss'. Financial assets are classified as held for trading if they are acquired for the purpose of selling in the near term. Derivatives are also classified as held for trading unless they are designated as effective hedging instruments. Gains or losses on investments held for trading are recognised in profit or loss.

**(ii) Loans and receivables**

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are carried at amortised cost using the effective interest method. Gains and losses are recognised in profit or loss when the loans and receivables are derecognised or impaired.

**I. Summary of Significant Accounting Policies (continued)**

**(o) Investments and other financial assets (continued)**

*(iii) Available-for-sale investments*

Available-for-sale investments are those non-derivative financial assets that are designated as available-for-sale or are not classified as any of the three preceding categories. After initial recognition available-for sale investments are measured at fair value with gains or losses being recognised as a separate component of equity until the investment is derecognised or until the investment is determined to be impaired, at which time the cumulative gain or loss previously reported in equity is recognised in profit or loss.

The fair value of investments that are actively traded in organised financial markets is determined by reference to quoted market bid prices at the close of business on the reporting date. For investments with no active market, fair value is determined using valuation techniques. Such techniques include using recent arm's length market transactions; reference to the current market value of another instrument that is substantially the same; discounted cash flow analysis and option pricing models, making as much use of available and supportable market data as possible and keeping judgmental inputs to a minimum.

**(p) Trade and other payables**

Trade payables and other payables are carried at amortised cost and represent liabilities for goods and services provided to the Group prior to the end of the financial year that are unpaid and arise when the Group becomes obliged to make future payments in respect of the purchase of these goods and services.

**(q) Provisions**

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

When the Group expects some or all of a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate assets but only when the reimbursement is virtually certain. The expense relating to any provision is presented in the statement of comprehensive income net of any reimbursement.

Provisions are measured at management's best estimate of the expenditure required to settle the present obligation at reporting date. If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects the risks specific to the liability.

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

*Restoration Provisions*

The Group recognises any legal or constructive restoration obligation as a liability at its present value at the time a legal liability or constructive obligation exists and when a reliable estimate of the amount of the obligation can be made. The carrying amount of the long-lived assets to which the obligation relates is increased by the asset retirement obligation costs and amortised over the producing life of the asset.

Restoration provisions are based on the estimated cost of restoration work required at the end of the useful life of the producing fields, including removal of facilities and equipment required or intended to be removed, together with abandonment of producing wells. These estimates of the asset retirement obligations are based on current technology, legal requirements and future costs, which have been discounted to their present value. In determining the asset retirement obligations, the Company has assumed no significant changes will occur in the relevant legislation in relation to restoration of sites in the future.

Where a restoration obligation is assumed as part of the acquisition of an asset or obligation, the liability is initially measured at the present value of the future cash flows to settle the present obligation as at the acquisition date. Over time, the liability is accreted to its present value each period based on a risk adjusted pre-tax discount rate appropriate to the risks inherent in the liability. The unwinding of the discount is recorded within finance costs. Upon settlement of the liability, the Company either settles the obligation for its recorded amount or incurs a gain or loss upon settlement.

**1. Summary of Significant Accounting Policies (continued)**

**(r) Interests in Joint Ventures**

Interests in jointly controlled assets are reported in the financial statements by including the Group's share of assets employed in the Joint Ventures, the share of liabilities incurred in relation to the Joint Ventures and the share of any expenses and revenues in relation to the Joint Ventures in their respective categories.

**(s) Employee benefits**

Liabilities for wages and salaries, including non-monetary benefits and annual leave, expected to be settled within 12 months of the reporting date are recognised in other payables in respect of employees' services up to the reporting date. They are measured at the amounts expected to be paid when the liabilities are settled.

**(t) Leases**

The determination of whether an arrangement is or contains a lease is based on the substance of the arrangement and requires an assessment of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

Finance leases, which transfer to the Group substantially all the risks and benefits incidental to ownership of the leased item, are capitalised at the inception of the lease at the fair value of the leased asset or, if lower, the present value of the minimum lease payments.

Operating lease payments are recognised as an expense in the statement of comprehensive income on a straight-line basis over the lease term.

**(u) Issued capital**

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

**(v) Revenue recognition**

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured.

Interest revenue is recognised as it accrues, taking into account the effective yield on the financial asset.

**(w) Borrowing Costs**

Borrowing costs are expensed in the period in which they are incurred except for borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset that necessarily takes a substantial period to get ready for its intended use or sale. In this case, borrowing costs are capitalised as part of the cost of the qualifying asset.

**(x) Share-based payment transactions**

*Equity settled transactions:*

The Group provides benefits to employees (including Directors) and consultants of the Group in the form of share-based payments, whereby those individuals render services in exchange for shares or rights over shares (equity-settled transactions).

When provided, the cost of these equity-settled transactions with these individuals is measured by reference to the fair value of the equity instruments at the date at which they are granted. The fair value is determined using a binomial model. In valuing equity-settled transactions, no account is taken of any performance conditions, other than conditions linked to the price of the shares of Kairiki Energy Limited (market conditions) if applicable.

The cost of equity-settled transactions is recognised, together with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled, ending on the date on which the relevant individuals become fully entitled to the award (the vesting period).

The cumulative expense recognised for equity-settled transactions at each reporting date until vesting date reflects (i) the extent to which the vesting period has expired and (ii) the Group's best estimate of the number of equity instruments that will ultimately vest. No adjustment is made for the likelihood of market performance conditions being met as the effect of these conditions is included in the determination of fair value at grant date. The amount charged or credited to the statement of comprehensive income for a period represents the movement in cumulative expense recognised as at the beginning and end of that period.

NOTES TO THE FINANCIAL STATEMENTS

1. *Summary of Significant Accounting Policies (continued)*

(x) **Share-based payment transactions (continued)**

No expense is recognised for awards that do not ultimately vest, except for awards where vesting is only conditional upon a market condition.

If an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any expense not yet recognised for the award is recognised immediately. However, if a new award is substituted for the cancelled award and designated as a replacement award on the date that it is granted, the cancelled and new award are treated as if they were a modification of the original award, as described in the previous paragraph.

(y) **Income Tax**

Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the reporting date.

Deferred income tax is provided on all temporary differences at the reporting date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax liabilities are recognised for all taxable temporary differences except:

- when the deferred income tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and that, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; or
- when the taxable temporary difference is associated with investments in subsidiaries, associates or interests in Joint Ventures, and the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income tax assets are recognised for all deductible temporary differences, carry-forward of unused tax assets and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences and the carry-forward of unused tax credits and unused tax losses can be utilised, except:

- when the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; or
- when the deductible temporary difference is associated with investments in subsidiaries, associates or interests in Joint Ventures, in which case a deferred tax asset is only recognised to the extent that it is probable that the temporary difference will reverse in the foreseeable future and taxable profit will be available against which the temporary difference can be utilised.

The carrying amount of deferred income tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilised.

Unrecognised deferred income tax assets are reassessed at each reporting date and are recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the reporting date.

Income taxes relating to items recognised directly in equity are recognised in equity and not in profit or loss.

Deferred tax assets and deferred tax liabilities are offset only if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred tax assets and liabilities relate to the same taxable entity and the same taxation authority.

The amount of benefits brought to account or which may be realised in the future is based on the assumption that no adverse change will occur in income legislation and the anticipation that the Group will derive sufficient future assessable income to enable the benefit to be realised and comply with the conditions of deductibility imposed by the law.

NOTES TO THE FINANCIAL STATEMENTS

1. *Summary of Significant Accounting Policies (continued)*

(z) **Other taxes**

Revenues, expenses and assets are recognised net of the amount of GST except:

- when the GST incurred on a purchase of goods and services is not recoverable from the taxation authority, in which case the GST is recognised as part of the cost of acquisition of the asset or as part of the expense item as applicable; and
- receivables and payables, which are stated with the amount of GST included.

The net amount of GST recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the statement of financial position.

Cash flows are included in the Cash Flow Statement on a gross basis and the GST component of cash flows arising from investing and financing activities, which is recoverable from, or payable to, the taxation authority, are classified as operating cash flows.

Commitments and contingencies are disclosed net of the amount of GST recoverable from, or payable to, the taxation authority.

(aa) **Segment reporting**

An operating segment is a component of the entity that engages in business activities from which it may earn revenues and incur expenses, whose operating results are regularly reviewed by the entity's chief operating decision maker to make decisions about resources to be allocated to the segment and assess its performance and for which discrete financial information is available. Operating segments have been identified based on the information provided to the chief operating decision makers, being the executive management team.

(ab) **Financial instruments issued by the Company**

Debt and equity instruments are classified as either liabilities or as equity in accordance with the substance of the contractual arrangement.

Transaction costs arising on the issue of equity instruments, net of associated tax, are recognised directly in equity as a reduction of the proceeds of the equity instrument to which the costs relate. Transaction costs are the costs that are incurred directly in connection with the issue of those equity instruments and which would not have been incurred had those instruments not been issued.

*Convertible Note*

The Convertible Note is split into two components: a debt component and a component representing the embedded derivatives in the Convertible Note. The debt component represents the Group's liability for future interest coupon payments and the redemption amount. The embedded derivatives represent the value of the option that Convertible Note holders have to convert into ordinary shares in the Company.

The debt component of the Convertible Note is measured at amortised cost and therefore increases as the present value of the redemption amount increases, with a corresponding charge to finance cost as accretion expense. The carrying value of the call option component was based on the residual value of the Convertible Note after subtracting the debt value from the face value of the Convertible Note.

The transactions costs of the Convertible Note have been offset against the debt instruments. These costs are amortised over the three year life of debt instruments.

(ac) **Earnings per share**

Basic earnings per share is calculated as net profit attributable to members of the parent, adjusted to exclude any costs of servicing equity (other than dividends) and preference share dividends, divided by the weighted average number of ordinary shares, adjusted for any bonus element.

Diluted earnings per share is calculated as net profit attributable to members of the parent, adjusted for:

- costs of servicing equity (other than dividends) and preference share dividends;
- the after tax effect of dividends and interest associated with dilutive potential ordinary shares that have been recognised as expenses; and
- other non-discretionary changes in revenues or expenses during the period that would result from the dilution of potential ordinary shares; divided by the weighted average number of ordinary shares and dilutive potential ordinary shares, adjusted for any bonus element.

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**

	<b>Consolidated</b>	
	<b>2011</b>	2010
	<b>\$'000</b>	\$'000
<b>2. Revenue and Expenses</b>		
<b>(a) Revenue and Income</b>		
Interest revenue	<b>63</b>	88
Foreign exchange gains	<b>227</b>	600
Other income	<b>-</b>	322
	<b>290</b>	1,010
<b>(b) Expenses</b>		
<i>Administrative expenses include:</i>		
Employee benefits expense:		
Salaries, wages and directors' fees	<b>736</b>	858
Defined contribution superannuation expense	<b>31</b>	44
Share-based payments expense / (benefit)	<b>143</b>	(51)
Net expense from movement in provision for employee entitlements	<b>-</b>	2
Other employee benefit expense	<b>34</b>	121
	<b>944</b>	974
Depreciation	<b>7</b>	15
Operating lease rental expense	<b>98</b>	90
Loss on disposal of non-current assets	<b>-</b>	1
<i>Finance costs include:</i>		
Interest paid, including withholding tax	<b>1,219</b>	1,472
Accretion expense	<b>606</b>	642
Borrowing costs expensed	<b>41</b>	41
	<b>1,866</b>	2,155

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**

	<b>Consolidated</b>	
	<b>2011</b>	<b>2010</b>
	<b>\$'000</b>	<b>\$'000</b>
<b>3. Income Tax</b>		
<b>(a) The major components of income tax are:</b>		
<b>Statement of comprehensive income</b>		
Current income tax	-	-
Deferred income tax	-	-
Income tax expense reported in the statement of comprehensive income	-	-
<b>Amounts charged or credited directly to equity</b>		
Share issue costs	(169)	(142)
Unrecognised tax losses	169	142
Income tax benefit reported in equity	-	-
<b>(b) Income Tax Reconciliation</b>		
The reconciliation between tax expense and the product of accounting loss before income tax multiplied by the Company's applicable income tax rate is as follows:		
Loss before income tax	(43,006)	(2,945)
Income tax benefit at 30% (2010: 30%)	(12,902)	(884)
Non-assessable foreign exchange	(68)	(207)
Non-deductible impairment of development expenditure	8,459	-
Non-deductible impairment of deferred exploration and evaluation expenditure	3,064	-
Non-deductible impairment of receivables	313	-
Share-based payments	43	(15)
Other	1	1
Unrecognised tax losses	1,089	1,105
Total income tax expense	-	-
<b>(c) Deferred Income Tax</b>		
<i>Deferred Tax Assets</i>		
Share issue costs	166	315
Rehabilitation provision	-	386
Accruals	4	5
Leave entitlements	2	1
Other	2	2
Revenue tax losses	5,446	4,706
Deferred tax asset netted off against deferred tax liability	(39)	(111)
Unrecognised deferred tax assets	(5,581)	(5,304)
	-	-
<i>Deferred Tax Liabilities</i>		
Convertible notes	(39)	(111)
Deferred tax asset netted off against deferred tax liability	39	111
	-	-

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**

**3. Income Tax (continued)**

Net deferred tax assets have not been brought to account as it is not probable within the immediate future that tax profits will be available against which deductible temporary differences and tax losses can be utilised.

**Franking Credits**

The franking account balance at year end was nil (2010: nil).

**Tax Consolidation Legislation**

Kairiki Energy Limited and its 100% owned subsidiaries have not formed a tax consolidated group.

	<b>Consolidated</b>	
	<b>2011</b>	2010
	<b>Cents</b>	Cents
<b>4. Earnings per Share</b>		
Basic earnings per share	<b>(5.22)</b>	(0.57)

The earnings and weighted average number of ordinary shares used in the calculation of basic earnings per share is as follows:

	<b>\$'000</b>	\$'000
Earnings – net loss for year	<b>(43,006)</b>	(2,945)
	<b>Number</b>	Number
Weighted average number of ordinary shares used in the calculation of basic earnings per share	<b>823,467,614</b>	514,861,231

The Company's potential ordinary shares, being its options granted and the shares to be issued for the conversion of the Convertible Notes, are not considered dilutive as the conversion of these options would result in a decrease in the net loss per share.

**5. Cash and Cash Equivalents**

Cash at bank and on hand	<b>1,802</b>	9,028
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**(i) Reconciliation of loss for the year to net cash flows used in operating activities**

Loss for the year	<b>(43,006)</b>	(2,945)
Adjustments for:		
Depreciation	<b>7</b>	15
Loss on disposal of non-current assets	<b>-</b>	1
Impairment of oil and gas properties	<b>28,198</b>	-
Impairment of deferred exploration and evaluation expenditure	<b>10,212</b>	-
Impairment of receivables for deferred consideration for sale of interest in oil and gas properties	<b>1,045</b>	-
Accretion expense	<b>606</b>	642
Amortisation of borrowing costs	<b>41</b>	41
Share-based payments	<b>143</b>	(51)
Foreign exchange gains	<b>(227)</b>	(600)
Sale of prospects classified as investing cash flows	<b>-</b>	(322)
Change in operating assets and liabilities:		
(Increase) / decrease in receivables	<b>56</b>	(24)
Increase / (decrease) in payables	<b>(96)</b>	190
Increase / (decrease) in provisions	<b>-</b>	2
Net cash flows used in operating activities	<b>(3,021)</b>	(3,051)

**(ii) Non-Cash Financing and Investing Activities**

There were no non-cash financing or investing activities.

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**

	<b>Consolidated</b>	
	<b>2011</b>	2010
	<b>\$'000</b>	\$'000
<b>6. Trade and other receivables</b>		
<b>Current</b>		
Receivable for sale of interest in oil and gas permits	-	2,704
Sundry debtors	<b>20</b>	20
GST refunds due	<b>23</b>	62
Prepayments	<b>11</b>	-
	<b>54</b>	<b>2,786</b>

*Fair Value and Risk Exposures*

- (i) Due to the short term nature of these receivables, their carrying value is assumed to approximate their fair value.
- (ii) The maximum exposure to credit risk is the fair value of receivables. Collateral is not held as security.
- (iii) Details regarding foreign exchange risk exposure are disclosed in Note 24.
- (iv) Other receivables generally have repayments between 30 and 90 days.

Receivables do not contain past due or impaired assets as at 30 June 2011 (2010: none).

Amounts receivable for the sale of interest in oil and gas permits in 2010 related to deferred consideration for the sale of a 4.9% interest in SC 54A to TG World (BVI) Corp.

**7. Inventories**

Oil in storage at lower of cost or net realisable value	-	2,407
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**8. Plant and Equipment**

Plant and equipment – at cost	<b>41</b>	57
Accumulated depreciation and impairment	<b>(34)</b>	(44)
	<b>7</b>	<b>13</b>

*Reconciliation of Plant and Equipment*

Carrying amount at beginning of period	<b>13</b>	26
Additions	<b>6</b>	5
Disposals	<b>(2)</b>	(1)
Depreciation	<b>(7)</b>	(15)
Foreign currency translation movements	<b>(3)</b>	(2)
Carrying amount at end of period	<b>7</b>	<b>13</b>

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**

	<b>Consolidated</b>	
	<b>2011</b>	2010
	<b>\$'000</b>	\$'000
<b>9. Oil and Gas Properties</b>		
Development phase, at cost	-	13,787
<i>Reconciliation of Oil and Gas Properties</i>		
Carrying amount at beginning of period	<b>13,787</b>	-
Transfers from exploration and evaluation	-	6,668
Additions	<b>22,321</b>	13,390
Sale of interests in oil and gas permits	-	(5,692)
Sale of oil produced during the period, net of sales costs	<b>(4,078)</b>	-
Transfer of oil produced during extended well test to inventory	-	(2,407)
Additions to / (reversal of) restoration asset	<b>(1,092)</b>	1,286
Expenditure written off during the year	<b>(28,198)</b>	-
Foreign currency translation movements	<b>(2,740)</b>	542
Carrying amount at end of period	<b>-</b>	<b>13,787</b>

Oil and gas properties represent Kairiki's interest in the Tindalo oil field in the Philippines SC 54 permit, Area 'A'. The carrying value was written off in December 2010 following the Joint Venture Partners' decision to abandon the Tindalo Well.

**10. Deferred Exploration and Evaluation Expenditure**

Deferred oil and gas expenditure	<b>14,343</b>	24,254
<i>Reconciliation of Deferred Exploration and Evaluation Expenditure</i>		
Carrying amount at beginning of period	<b>24,254</b>	35,926
Additions	<b>5,018</b>	804
Transfers to oil and gas properties	-	(6,668)
Sale of interests in oil and gas permits	-	(2,971)
Expenditure written off during the year	<b>(10,212)</b>	-
Foreign currency translation movements	<b>(4,717)</b>	(2,837)
Carrying amount at end of period	<b>14,343</b>	<b>24,254</b>

Deferred oil and gas expenditure represents expenditures relating to the Yakal discovery and residual areas of the SC 54 Area 'A' permit, plus Kairiki's Philippine SC 54 permit, Area 'B'. Deferred expenditure relating to the Gindara-1 well was written off in June 2011 after drilling established that the well was non-commercial.

The ultimate recoupment of exploration and evaluation expenditure carried forward is dependent on successful development and commercial exploitation or, alternatively, sale of the respective areas.

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**

	<b>Consolidated</b>	
	<b>2011</b>	2010
	<b>\$'000</b>	\$'000
<b>11. Trade and Other Payables</b>		
<b>Current</b>		
Trade payables and accruals	<b>2,897</b>	4,312

*Fair Value and Risk Exposures*

- (i) Due to the short term nature of these payables, their carrying value is assumed to approximate their fair value.
- (ii) Details regarding foreign exchange and liquidity risk are disclosed in Note 24.
- (iii) Trade and other payables are unsecured and usually paid within 60 days of recognition.

**12. Provisions**

**Current**

Employee benefits	<b>5</b>	5
Restoration	-	1,286
	<b>5</b>	1,291

*Reconciliation of Restoration Provision*

Carrying amount at beginning of period	<b>1,286</b>	-
Arising during the period	-	1,286
Reversed during the period	<b>(1,092)</b>	-
Foreign currency translation movements	<b>(194)</b>	-
Carrying amount at end of period	-	1,286

During the year ended 30 June 2010, the Group recognised a provision for the estimated cost of restoration work required at the end of the useful life of the Tindalo oil field. The provision was been created on the basis of internal management estimates based on the current economic environment. The provision was reversed in December 2010 following the Joint Venture Partners' decision to abandon the Tindalo Well.

All required abandonment obligations in relation to drilling conducted at Yakal have been met. Future abandonment costs will be required in the event that the well is completed and moves into production.

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**

	<b>Consolidated</b>	
	<b>2011</b>	2010
	<b>\$'000</b>	\$'000
<b>13. Convertible Notes</b>		
Financial liability measured at amortised cost	<b>6,967</b>	10,271
<i>Reconciliation of Convertible Notes</i>		
Carrying amount at beginning of period	<b>10,271</b>	11,181
Repayment of debt	<b>(1,921)</b>	(910)
Accretion of debt	<b>606</b>	642
Amortisation of issuance costs	<b>41</b>	41
Foreign currency translation movements	<b>(2,030)</b>	(683)
Carrying amount at end of period	<b>6,967</b>	10,271
Amount classified as current	<b>6,967</b>	-
Amount classified as non-current	<b>-</b>	10,271
	<b>6,967</b>	10,271
<b>Carrying Value of Convertible Notes</b>		
- Debt portion	<b>6,967</b>	10,271
- Equity portion (refer to Note 14)	<b>1,890</b>	1,951
	<b>8,857</b>	12,222

The principal terms and conditions of the Convertible Note are as follows:

- i) Bond Holder: IMC Oil and Gas Investments Limited (“IMC”)
- ii) Maturity date: 8 September 2011 (US\$8.5 million note) and 22 October 2011 (US\$1.5 million note) (3 years from issue).
- iii) Interest payable at 12% per annum with interest accruing and capitalised to the loan through to 31 December 2008 and thereafter payable monthly.
- iv) Conversion price is as the lesser of:
  - (a) A\$0.185; and
  - (b) the closing price of the ordinary shares on ASX on the conversion date, provided that, if this price is lower than A\$0.16, the conversion price will be A\$0.16;
- v) IMC may convert at any time prior to the Repayment Date, subject to a limit of 3 conversions with each conversion being in respect of a number of Convertible Notes which are convertible into at least 10 million shares;
- vi) Repayment rights: IMC shall have the right, each month to require the Company to use all or a specified part of any cash balance held in a special repayment account, established for receipt of future net proceeds as defined and option conversion monies, to repay a portion of the outstanding amount in respect of the Convertible Notes;
- vii) IMC has the right to appoint a representative to the board of Kairiki Energy Limited;
- viii) IMC has an option to farm-in at up to 20% in SC 54B, subject to certain conditions. This option must be exercised no later than 6 months before the spud date of a well in SC 54B;
- ix) Redemption provisions for such events including failure to participate in a commercial SC 54 shallow water development, change of control, event of default; and
- x) Security: fixed and floating charge over all the assets of Kairiki Energy Limited and its subsidiary Yilgarn Petroleum Philippines Pty Ltd, but excluding certain property.

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**

**13. Convertible Notes (continued)**

The Convertible Note has been classified into two components: a debt component (a contractual arrangement to deliver cash) and an embedded derivative call option component (a call option granting the holder the right, for a specified period of time, to convert it into a number of ordinary shares of Kairiki, based on the outstanding balance at date of conversion).

The debt component of the Convertible Note is measured at its amortised cost of US dollars and increases to the amount owing at maturity over the life of the Convertible Note with a corresponding charge over this period to the statement of comprehensive income as a finance cost (accretion expense).

**Equity Component**

The carrying value of the call option component was based on the residual value of the Convertible Note after subtracting the debt value from the face value of the Convertible Note.

Subsequent to year end (refer to Note 26) a number of amendments were made to the Convertible Note agreement. Furthermore, the amount due on the Convertible Notes was reduced by the payment of US\$1 million on 6 September 2011, resulting in an amount owing at the date of this report of US\$6.7 million.

	<b>Consolidated</b>	
	<b>2011</b>	2010
	<b>\$'000</b>	\$'000
<b>14. Issued Capital</b>		
<b>(a) Share capital</b>		
Ordinary shares fully paid	<b>68,344</b>	48,975
Equity portion of Convertible Note – refer to Note 13	<b>1,890</b>	1,951
	<b>70,234</b>	50,926
<b>(b) Movement in ordinary shares on issue</b>		
	<b>Number</b>	<b>\$'000</b>
<b>At 30 June 2009</b>	512,959,998	42,780
Exercise of options during the year	1,250,000	131
Placement of shares (14 cents per share)	46,700,000	6,538
Share issue transaction costs	-	(474)
<b>At 30 June 2010</b>	<b>560,909,998</b>	<b>48,975</b>
Exercise of options during the year		
Placement of shares (4 cents per share)	<b>84,000,000</b>	<b>3,360</b>
Rights issue (4 cents per share)	<b>128,982,000</b>	<b>5,159</b>
Placement of shares (3 cents per share)	<b>116,000,000</b>	<b>3,480</b>
Rights issue (3 cents per share)	<b>296,630,666</b>	<b>8,899</b>
Placement of shares (3 cents per share)	<b>1,000,000</b>	<b>30</b>
Share issue transaction costs	-	<b>(1,559)</b>
<b>At 30 June 2011</b>	<b>1,187,522,664</b>	<b>68,344</b>
	<b>2011</b>	2010
	<b>\$'000</b>	\$'000
<b>(c) Movement in equity component of convertible note</b>		
Carrying value at beginning of period	<b>1,951</b>	2,064
Equity component of repayment	<b>(61)</b>	(113)
Carrying value at the end of period	<b>1,890</b>	1,951

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**

**14. Issued Capital (continued)**

**(d) Options at 30 June 2011**

	<i>Number</i>	<i>Exercise Price</i>	<i>Exercise Date</i>
Listed Options	305,192,095	4 cents	Between 1/8/2011 and 31/8/2011
Unlisted Options	49,000,000	6.5 cents	Between 16/5/2012 and 16/5/2014
	<u>354,192,095</u>		

During the year:

- (i) 2,000,000 unlisted options were forfeited on resignation;
- (ii) 500,000 unlisted options expired;
- (iii) 305,192,095 listed options were issued as part of a rights issue;
- (iv) 49,000,000 unlisted options were granted to directors and employees.

**(e) Terms and conditions of contributed equity**

*Ordinary Shares:*

Ordinary shares have the right to receive dividends as declared and, in the event of winding up the Company, to participate in the proceeds from the sale of all surplus assets in proportion to the number of and amounts paid up on shares held.

Ordinary shares entitle their holder to one vote, either in person or by proxy, at a meeting of the Company.

**Capital Management**

When managing capital, management's objective is to ensure the entity continues as a going concern as well as to maintain optimal returns to shareholders and benefits for other stakeholders. Management also aims to maintain a capital structure that ensures the lowest cost of capital available to the entity.

Management may in the future adjust the capital structure to take advantage of favourable costs of capital and issue further shares in the market. Management has no current plans to adjust the capital structure other than as disclosed in the financial statements. There are no plans to distribute dividends in the next year.

The Convertible Note with the IMC imposes certain restrictions on the Company in regard to its future debt funding capabilities (refer to Note 13).

**15. Reserves**

*Nature and purpose of reserves:*

**Option Reserve**

This reserve is used to record the value of equity benefits provided to Directors and employees as part of their remuneration.

**Foreign Currency Translation Reserve**

The foreign currency translation reserve is used to record exchange differences arising from the translation of the financial statements of foreign subsidiaries.

**16. Contingent Assets and Liabilities**

*Contingent Assets*

- i) In March 2009, Kairiki entered into agreements with a previous partner, Alpine Oil & Gas Pty Ltd (AOG) to sell Kairiki's 30% interest in each of the Sicily Channel exploration permits, Pantelleria and Kerkouane. As consideration, AOG agreed to pay US\$280,000 cash (A\$326,836) for each permit if and when AOG disposes of an interest in those permits. US\$280,000 was received in June 2010 in relation to the Kerkouane permit.
- ii) Kairiki is entitled to receive 10% of net proceeds of certain Australian mineral tenements up to a sum of A\$250,000 and a 1% net smelter royalty and for the remaining tenements, 10% of the net revenue after 5,000 ounces of gold has been produced.

*Contingent Liabilities*

There are no contingent liabilities.

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**

	<b>Consolidated</b>	
	<b>2011</b>	2010
	<b>\$'000</b>	\$'000
<b>17. Commitments</b>		
<b>Operating leases (non-cancellable):</b>		
- Within one year	<b>104</b>	89
- More than one year but not later than five years	<b>61</b>	138
	<b>165</b>	227

These non-cancellable operating leases are primarily for office premises.

**Exploration Commitments**

In order to maintain current rights of tenure to its SC 54 permit, the consolidated entity has certain obligations to perform minimum exploration work and expend minimum amounts of money. These commitments may be varied as a result of renegotiations, relinquishments, farm-outs, sales or carrying out work in excess of the permit obligations. The following exploration expenditure requirements have not been provided for in the financial report and are payable:

- Within one year	-	-
- More than one year but not later than five years	-	2,108
	-	2,108

**Joint Venture Capital Commitments**

The consolidated entity's share of capital expenditures contracted for at the balance date for which no amounts have been provided for in the financial statements are payable:

- Within one year	-	14,778
- More than one year but not later than five years	-	-
	-	14,778

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**

**18. Key Management Personnel Disclosures**

**(a) Compensation of Key Management Personnel**

	<b>Consolidated</b>	
	<b>2011</b>	2010
	\$	\$
Short-term employment benefits	<b>555,218</b>	886,784
Post-employment benefits	<b>21,431</b>	34,368
Share-based payment	<b>138,344</b>	87,696
	<b>714,993</b>	1,008,848
	<b>714,993</b>	1,008,848

**(b) Option holdings of Key Management Personnel**

<b>2011</b>	Balance at 1 July 2010	Granted as remuneration	Rights Issue Entitlement	Expired or Change due to Resignation	Balance at 30 June 2011	Non Vested	Number vested and exercisable
<b>Directors</b>							
P Fry	-	12,500,000	516,666	-	13,016,666	12,500,000	516,666
M Fenton	-	20,000,000	-	-	20,000,000	20,000,000	-
D. Maclean <sup>(i)</sup>	-	7,500,000	-	-	7,500,000	7,500,000	-
L. Brown <sup>(ii)</sup>	-	-	-	-	-	-	-
J Baker <sup>(iii)</sup>	2,000,000	-	-	(2,000,000)	-	-	-
J. Morton <sup>(iv)</sup>	-	-	-	-	-	-	-
<b>Executives</b>							
N Bassett <sup>(v)</sup>	-	7,500,000	-	-	7,500,000	7,500,000	-
	2,000,000	47,500,000	516,666	(2,000,000)	48,016,666	47,500,000	516,666

(i) Appointed 31 March 2011.

(ii) Resigned 30 August 2010.

(iii) Resigned 25 August 2010.

(iv) Appointed 30 August 2010, resigned 28 September 2010.

(v) Appointed as a Director on 28 September 2010, resigned 31 March 2011. Continues as Company Secretary.

<b>2010</b>	Balance at 1 July 2009	Granted as remuneration	Options exercised	Expired or Change due to Resignation	Balance at 30 June 2010	Non Vested	Number vested and exercisable
<b>Directors</b>							
P Fry	2,500,000	-	-	(2,500,000)	-	-	-
M Fenton	-	-	-	-	-	-	-
L Brown <sup>(i)</sup>	2,500,000	-	-	(2,500,000)	-	-	-
R Jefferies <sup>(ii)</sup>	2,500,000	-	-	(2,500,000)	-	-	-
J Baker <sup>(iii)</sup>	-	2,000,000	-	-	2,000,000	2,000,000	-
<b>Executives</b>							
N Bassett <sup>(iv)</sup>	500,000	-	-	(500,000)	-	-	-
	8,000,000	2,000,000	-	(8,000,000)	2,000,000	2,000,000	-

(i) Resigned 30 August 2010.

(ii) Resigned 18 August 2009.

(iii) Resigned 25 August 2010.

(iv) Appointed as a Director on 28 September 2010, resigned 31 March 2011. Continues as Company Secretary.

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**

**18. Key Management Personnel Disclosures (continued)**

**(c) Shareholdings of Key Management Personnel**

	Balance at beginning of the year	Options exercised	Change due to appointment	Change due to resignation	Net Change Other	Balance at end of the year
<b>2011</b>						
<b>Directors</b>						
P Fry	9,692,185	-	-	-	1,033,333	10,725,518
M Fenton	107,000	-	-	-	-	107,000
D Maclean <sup>(i)</sup>	-	-	2,198,000	-	1,000,000	3,198,000
L Brown <sup>(ii)</sup>	12,427,372	-	-	(12,427,372)	-	-
J Baker <sup>(iii)</sup>	70,000	-	-	(70,000)	-	-
J Morton <sup>(iv)</sup>	-	-	28,571	(28,571)	-	-
<b>Executives</b>						
N Bassett <sup>(v)</sup>	500,000	-	-	-	100,000	600,000
	<b>22,796,557</b>	<b>-</b>	<b>2,226,571</b>	<b>(12,525,943)</b>	<b>2,133,333</b>	<b>14,630,518</b>

(i) Appointed 31 March 2011.

(ii) Resigned 30 August 2010.

(iii) Resigned 25 August 2010.

(iv) Appointed 30 August 2010, resigned 28 September 2010.

(v) Appointed as a Director on 28 September 2010, resigned 31 March 2011. Continues as Company Secretary.

	Balance at beginning of the year	Options exercised	Change due to appointment	Change due to resignation	Net Change Other	Balance at end of the year
<b>2010</b>						
<b>Directors</b>						
P Fry	9,692,185	-	-	-	-	9,692,185
M Fenton	-	-	107,000	-	-	107,000
L Brown <sup>(i)</sup>	12,427,372	-	-	-	-	12,427,372
R Jefferies <sup>(ii)</sup>	-	-	-	-	-	-
J Baker <sup>(iii)</sup>	70,000	-	-	-	-	70,000
<b>Executives</b>						
N Bassett <sup>(iv)</sup>	500,000	-	-	-	-	500,000
	<b>22,689,557</b>	<b>-</b>	<b>107,000</b>	<b>-</b>	<b>-</b>	<b>22,796,557</b>

(i) Resigned 30 August 2010.

(ii) Resigned 18 August 2009.

(iii) Resigned 25 August 2010.

(iv) Appointed as a Director on 28 September 2010, resigned 31 March 2011. Continues as Company Secretary.

All equity transactions with Key Management Personnel other than those arising from the exercise of remuneration options have been entered into under terms and conditions no more favourable than those the entity would have adopted if dealing at arms-length.

**(d) Other transactions and balances with Key Management Personnel**

IMC Oil & Gas Investments Limited, an entity with which former directors Ms Jyn Sim Baker and Mr John Morton were related, is the holder of the Convertible Notes which Kairiki has issued. Full details of the Convertible Notes are disclosed in Note 13, and finance costs are disclosed in Note 2(b).

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**

**19. Other Related Party Transactions**

**Parent entity**

The ultimate parent entity within the Group is Kairiki Energy Limited.

**Subsidiaries**

Name of Controlled Entity	Class of Share	Place of Incorporation	% Held by Parent Entity	
			2011	2010
Great Southern Mines NL	Ordinary	Australia	100%	100%
Yilgarn Petroleum Philippines Pty Ltd	Ordinary	Australia	100%	100%
Kairiki Energy Asia Pty Ltd	Ordinary	Australia	100%	100%
Kairiki Energy Africa Pty Ltd	Ordinary	Australia	100%	100%
Kairiki Energy Italy Pty Ltd	Ordinary	Australia	100%	100%

**Key management personnel**

Disclosures relating to key management personnel are set out in Note 18.

**Transactions with related parties**

The parent entity loans funds to its subsidiaries to fund exploration and development activities. No interest is charged and no repayment schedule exists for the inter-company loans. They are payable upon demand and the fair value approximates the carrying value. An allowance for impairment is recognised when there is objective evidence that the loans receivable are impaired.

**20. Share-based Payments**

**(a) Value of share-based payments in the financial statements**

	Consolidated	
	2011	2010
	\$'000	\$'000
Share-based payments expensed	<b>143</b>	(51)

**(b) Summary of share-based payments**

Set out below are the summaries of options granted as share-based payments:

Grant Date	Expiry Date	Exercise Price	Balance at start of the year Number	Granted during the year Number	Exercised during the year Number	Expired or Change due to Resignation Number	Balance at end of the year Number	Vested and exercisable at end of the year Number
<b>Consolidated and parent entity – 2011</b>								
<i>Key Management Personnel – unlisted options</i>								
14/12/2009	14/12/2012	15c	2,000,000	-	-	(2,000,000)	-	-
16/5/2011	16/5/2014	6.5c	-	47,500,000	-	-	47,500,000	-
<i>Employees- unlisted options</i>								
10/11/2008	31/5/2011	30c	500,000	-	-	(500,000)	-	-
16/5/2011	16/5/2014	6.5c	-	1,500,000	-	-	1,500,000	-
			2,500,000	49,000,000	-	(8,000,000)	2,500,000	-
Weighted average exercise price (\$)			0.18	0.065	-	0.18	0.065	-

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**

**20. Share-based Payments (continued)**

**(b) Summary of share-based payments (continued)**

Grant Date	Expiry Date	Exercise Price	Balance at start of the year Number	Granted during the year Number	Exercised during the year Number	Expired or Change due to Resignation Number	Balance at end of the year Number	Vested and exercisable at end of the year Number
<b>Consolidated and parent entity – 2010</b>								
<i>Key Management Personnel – unlisted options</i>								
3/10/2007	3/10/2009	10.5c	1,250,000	-	-	(1,250,000)	-	-
3/10/2007	3/10/2010	13.5c	1,250,000	-	-	(1,250,000)	-	-
30/11/2007	30/11/2009	30c	3,300,000	-	-	(3,300,000)	-	-
30/11/2007	30/11/2009	35c	2,200,000	-	-	(2,200,000)	-	-
14/12/2009	14/12/2012	15c	-	2,000,000	-	-	2,000,000	-
<i>Employees- unlisted options</i>								
10/11/2008	31/5/2011	30c	500,000	-	-	-	500,000	500,000
			8,500,000	2,000,000	-	(8,000,000)	2,500,000	500,000
Weighted average exercise price			0.26	0.15	-	0.26	0.18	0.30

No options were exercised during the year ended 30 June 2011. The weighted average share price at the date of exercise of options exercised during the year ended 30 June 2010 was 17 cents.

The assessed fair values of the options were determined using a binomial option pricing model, taking into account the exercise price, term of option, the share price at grant date and expected price volatility of the underlying share, expected dividend yield and the risk-free interest rate for the term of the option. The inputs to the model used were:

**2011**

Grant date	16/5/2011
Dividend yield (%)	-
Expected volatility (%)	100.00
Risk-free interest rate (%)	4.82%
Expected life of options (years)	2.50
Underlying share price (\$)	0.045
Option exercise price (\$)	0.065
Value of option (\$)	0.023

**2010**

Grant date	14/12/2009
Dividend yield (%)	-
Expected volatility (%)	100.00
Risk-free interest rate (%)	4.48%
Expected life of options (years)	2.50
Underlying share price (\$)	0.14
Option exercise price (\$)	0.15
Value of option (\$)	0.081

The expected life of the options is based on historical data and is not necessarily indicative of exercise patterns that may occur. The expected volatility reflects the assumption that the historical volatility is indicative of future trends, which may also not necessarily be the actual outcome. No other features of options granted were incorporated into the measurement of fair value.

20. *Share-based Payments (continued)*

(c) **Weighted average fair value**

The weighted average fair value of share-based payment options granted during the year was \$0.023 (2010: \$0.081).

(d) **Weighted average remaining contractual life**

The weighted average remaining contractual life of share-based payment options outstanding as at 30 June 2011 was 2.9 years (2010: 2.1 years).

	<b>Consolidated</b>	
	<b>2011</b>	2010
	\$	\$
<b>21. Auditors' Remuneration</b>		
Amount received or due and receivable by the auditor of Kairiki Energy Limited for:		
Auditing and reviewing the financial statements	<b>22,000</b>	27,500
Amount received or due and receivable by other audit firms:		
Audit of foreign subsidiary financial statements	<b>24,212</b>	-
Taxation consulting	<b>20,235</b>	-
	<b>66,447</b>	27,500

22. *Joint Venture*

The consolidated entity had the following interests in a Joint Venture operation:

<b>Joint Venture</b>	<b>Principal Activities</b>	<b>Percentage Interest</b>	
		<b>2011</b>	2010
SC 54 Joint Venture – Area 'A'	Oil and gas exploration and development	30.1%	30.1%
SC 54 Joint Venture – Area 'B'	Oil and gas exploration	22%	40%

The Joint Venture is not a separate legal entity. It is a contractual arrangement between participants for the sharing of costs and outputs and does not in itself generate revenue or profit. The Joint Venture parties share development, exploration and evaluation costs and output in proportion to their ownership of Joint Venture assets and accordingly the Group's share of exploration evaluation and development expenditure is accounted for in accordance with the policy set out in Note 1.

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**

**22. Joint Venture (continued)**

**Assets utilised in the Joint Venture**

The following amounts represent the Group's interest in the assets employed in Joint Ventures. These amounts are included in the consolidated financial statements under their respective categories as follows:

	<b>Consolidated</b>	
	<b>2011</b>	2010
	<b>\$'000</b>	\$'000
<b>ASSETS</b>		
<b>Current Assets</b>		
Inventories	-	2,407
Total Current Assets	-	2,407
<b>Non-Current Assets</b>		
Oil and gas properties	-	13,787
Deferred exploration and evaluation expenditure	14,343	24,254
Total Non-Current Assets	14,343	38,041
<b>Total Assets</b>	14,343	40,448
<b>LIABILITIES</b>		
<b>Current Liabilities</b>		
Trade and other payables	2,612	3,992
Total Current Liabilities	2,612	3,992
<b>Non-Current Liabilities</b>		
Provisions	-	1,286
Total Non-Current Liabilities	-	1,286
<b>Total Liabilities</b>	2,612	5,278
<b>Net Assets</b>	11,731	35,170

**Commitments Relating to Joint Venture**

Capital expenditure commitments in respect of Joint Ventures are disclosed in Note 17.

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**

**23. Segment reporting**

The Group has identified its operating segments based on the internal reports that are used by the executive management team (the chief operating decision makers) in assessing performance and in determining the allocation of resources.

The operating segments are identified by management based on the phase of operation within the oil and gas industry. For management purposes, the Group has organised its operations into two reportable segments on the basis of stage of development as follows:

- Development assets
- Exploration and evaluation assets, which includes assets that are associated with the determination and assessment of the existence of commercial economic reserves.

Corporate costs, finance costs, interest revenue and foreign currency gains and losses are not allocated to segments as they are not considered part of the core operations of the segments and are managed on a Group basis.

<b>Consolidated</b>	<b>Oil &amp; Gas - Development \$'000</b>	<b>Oil &amp; Gas - Exploration \$'000</b>	<b>Total \$'000</b>
<b>30 June 2011</b>			
<b>Segment revenue</b>	-	-	-
Unallocated items:			
Interest revenue			63
Foreign exchange gains			227
<b>Total revenue and other income</b>			<b>290</b>
<b>Segment result</b>	<b>(29,263)</b>	<b>(10,232)</b>	<b>(39,495)</b>
Unallocated items:			
Unallocated revenue and other income			290
Administrative and other costs			(1,935)
Finance costs			(1,866)
<b>Loss after tax as per the statement of comprehensive income</b>			<b>(43,006)</b>
<b>Segment assets</b>	-	<b>14,343</b>	<b>14,343</b>
Unallocated items:			
Cash			1,802
Other corporate assets			61
<b>Total assets</b>			<b>16,206</b>
<b>Segment capital expenditure</b>	<b>22,321</b>	<b>5,018</b>	<b>27,339</b>
Unallocated corporate capital expenditure			6
<b>Total capital expenditure</b>			<b>27,345</b>

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**

**23. Segment reporting (continued)**

<b>Consolidated</b>	<b>Oil &amp; Gas - Development \$'000</b>	<b>Oil &amp; Gas - Exploration \$'000</b>	<b>Total \$'000</b>
<b>30 June 2010</b>			
<b>Segment revenue</b>	-	-	-
Unallocated items:			
Interest revenue			88
Foreign exchange gains			600
Other income			322
<b>Total revenue and other income</b>			<b><u>1,010</u></b>
<b>Segment result</b>	<b>(12)</b>	<b>(13)</b>	<b>(25)</b>
Unallocated items:			
Unallocated revenue and other income			1,010
Administrative and other costs			(1,800)
Finance costs			(2,155)
<b>Loss after tax as per the statement of comprehensive income</b>			<b><u>(2,945)</u></b>
<b>Segment assets</b>	<b>18,898</b>	<b>24,254</b>	<b>43,152</b>
Unallocated items:			
Cash			9,028
Other corporate assets			95
<b>Total assets</b>			<b><u>52,275</u></b>
<b>Segment capital expenditure</b>	<b>13,390</b>	<b>804</b>	<b>14,194</b>
Unallocated corporate capital expenditure			5
<b>Total capital expenditure</b>			<b><u>14,199</u></b>

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**

**24. Financial Risk Management Objectives and Policies**

The Group's principal financial instruments comprise cash, short-term deposits and Convertible Notes. The main purpose of these financial instruments is to provide working capital for the Group's operations.

The Group has various other financial instruments such as trade debtors and trade creditors, which arise directly from its operations.

It is, and has been throughout the period under review, the Group's policy that no trading in financial instruments shall be undertaken.

The main risks arising from the Group's financial instruments are interest rate risk, liquidity risk, credit risk, foreign currency risk and commodity risk. The Board reviews and agrees on policies for managing each of these risks and they are summarised below.

**Interest Rate Risk**

At balance date the Group's exposure to market risk for changes in interest rates relates primarily to the Company's short-term cash deposits. The Group constantly analyses its exposure to interest rates, with consideration given to potential renewal of existing positions, the mix of fixed and variable interest rates and the period to which deposits may be fixed. The Group is not exposed to cash flow volatility from interest rate changes on borrowings as the Convertible Note carries a fixed rate of interest of 12% per annum.

At balance date, the Group had the following financial assets exposed to variable interest rates that are not designated in cash flow hedges:

	<b>Consolidated</b>	
	<b>2011</b>	2010
	<b>\$'000</b>	\$'000
<i>Financial Assets:</i>		
Cash and cash equivalents held in interest-bearing accounts	<b>1,799</b>	9,024
Net exposure	<b>1,799</b>	9,024

The following sensitivity analysis is based on the interest rate risk exposures in existence at the reporting date. The 0.5% sensitivity is based on reasonably possible changes, over a financial year, using an observed range of historical LIBOR movements over the last 3 years.

At 30 June 2011, if interest rates had moved, as illustrated in the table below, with all other variables held constant, post tax profit and equity relating to financial assets of the Group would have been affected as follows:

	<b>Consolidated</b>	
	<b>2011</b>	2010
	<b>\$'000</b>	\$'000
Judgements of reasonably possible movements:		
<i>Post tax profit - higher / (lower)</i>		
+ 0.5%	<b>9</b>	45
- 0.5%	<b>(9)</b>	(45)
<i>Equity - higher / (lower)</i>		
+ 0.5%	<b>9</b>	45
- 0.5%	<b>(9)</b>	(45)

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**

**24. Financial Risk Management Objectives and Policies (continued)**

**Liquidity Risk**

The Group's objective is to maintain a balance between continuity of funding and flexibility through the use of its cash and funding requirements.

The table below reflects all contractually fixed pay-offs, repayments and interest resulting from recognised financial liabilities as of 30 June 2011. These amounts represent contractual undiscounted cash flows.

The contractual maturities of the Group's financial liabilities are:

	<b>Consolidated</b>	
	<b>2011</b>	2010
	<b>\$'000</b>	\$'000
6 months or less	<b>10,290</b>	4,979
6-12 months	<b>182</b>	667
1-5 years	<b>-</b>	11,476
	<b>10,472</b>	17,122

**Credit risk**

Credit risk refers to the risk that a counterparty will default on its contractual obligations resulting in financial loss to the Company. The Company has adopted the policy of dealing with creditworthy counterparties and obtaining sufficient collateral or other security where appropriate, as a means of mitigating the risk of financial loss from defaults. The Company measures credit risk on a fair value basis.

Cash is primarily deposited only with AA (Moody's) rated financial institutions. The Company does not have any other significant credit risk exposure to a single counterparty or any group of counterparties having similar characteristics.

**Foreign Currency Risk**

As the functional currency of the parent entity Kairiki Energy Limited and the subsidiary Yilgarn Petroleum Philippines Pty Ltd is USD and the presentation currency of the Group is AUD, and transactions occur in both currencies, the Group's statement of financial position and result can be affected by movements in the AUD/USD exchange rates. Foreign currency gains or losses in the statement of comprehensive income result from the settlement of transactions in currencies other than the functional currency and the translation at period-end exchange rates of monetary assets and liabilities denominated in currencies other than the functional currency (primarily AUD).

The Group manages its foreign exchange risk by constantly reviewing its exposure to commitments payable and ensuring cash balances are maintained in appropriate currencies to meet operational commitments.

At 30 June 2011, the Group had the following exposures to USD and AUD currencies that are not designated in cash flow hedges:

	<b>2011</b>		2010	
	<b>USD</b>	<b>AUD</b>	<b>USD</b>	<b>AUD</b>
	<b>AUD \$'000</b>	<b>AUD \$'000</b>	<b>AUD \$'000</b>	<b>AUD \$'000</b>
<i>Financial Assets:</i>				
Cash and cash equivalents	<b>957</b>	<b>845</b>	7,256	1,772
Trade and other receivables	<b>-</b>	<b>54</b>	2,704	82
<i>Financial Liabilities:</i>				
Trade and other payables	<b>(2,611)</b>	<b>(285)</b>	(3,992)	(320)
Convertible notes	<b>(6,967)</b>	<b>-</b>	(10,271)	-
Net exposure	<b>(8,621)</b>	<b>614</b>	(4,303)	1,534

Because the functional currency of the parent entity and major subsidiary is USD, foreign currency risk arises on AUD balances.

The following sensitivity analysis is based on the foreign currency risk exposures in existence at the reporting date. The 5% sensitivity is based on reasonably possible changes, over a financial year, using an observed range of actual historical rates, for the AUD/USD exchange rate, for the preceding 5 years.

**KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES**

**NOTES TO THE FINANCIAL STATEMENTS**

**24. Financial Risk Management Objectives and Policies (continued)**

At 30 June, if the AUD/USD exchange rate had moved as illustrated in the table below, with all other variables held constant, post tax profit and equity would have been affected as follows:

	<b>Consolidated</b>	
	<b>2011</b>	2010
	<b>\$'000</b>	\$'000
Judgments of reasonably possible movements:		
<i>Post tax profit - higher / (lower)</i>		
AUD/USD + 5 %	<b>29</b>	73
AUD/USD - 5 %	<b>(32)</b>	(81)
<i>Equity - higher / (lower)</i>		
AUD/USD + 5 %	<b>29</b>	73
AUD/USD - 5 %	<b>(32)</b>	(81)

The reasonably possible movements in 2011 are lower than those in 2010 primarily due to the reduced amount of AUD cash and the lower amount owing on the convertible notes.

Management believes the balance date risk exposures are representative of the risk exposure inherent in financial instruments.

**Commodity Price Risk**

At 30 June 2011, the Group had no open oil price swap and option contracts (2010: nil).

**Fair Value**

The methods of estimating fair value are outlined in the relevant notes to the financial statements.

**25. Parent Entity Information**

	<b>Parent</b>	
	<b>2011</b>	2010
	<b>\$'000</b>	\$'000
Current assets	<b>1,813</b>	9,819
Total assets	<b>13,595</b>	46,752
Current liabilities	<b>(7,258)</b>	(325)
Total liabilities	<b>(7,258)</b>	(10,596)
<b>Net assets</b>	<b>6,337</b>	36,155
Issued capital	<b>70,234</b>	50,926
Share-based payments reserve	<b>2,980</b>	2,837
Foreign currency translation reserve	<b>(8,126)</b>	(397)
Accumulated losses	<b>(58,751)</b>	(17,211)
<b>Total equity</b>	<b>6,337</b>	36,155
Loss of the parent entity after tax	<b>(41,540)</b>	(2,157)
Other comprehensive (loss)/income, net of tax	<b>(7,729)</b>	(2,120)
<b>Total comprehensive loss of the parent entity</b>	<b>(49,269)</b>	(4,277)

**26. Events Subsequent to Year End**

**(i) Underwritten Rights Issue**

On 26 August 2011 the Company completed a \$6,000,000 (before expenses of the issue) capital raising via a pro-rata renounceable rights issue that was underwritten by Patersons Securities Limited, the Company's Lead Manager. The Rights Issue was offered to eligible shareholders, on the basis of three (3) new share for every two (2) shares held at an issue price of 0.4 cents per share. For every four shares subscribed for in the Rights Issue, the applicant received 1 "piggy back" option. The primary option is exercisable at 0.4 cents during June 2013 and will expire on 30 June 2013. The primary option is exercisable into one share and a secondary option which is exercisable at 0.4 cents and expires on 30 June 2015.

Pursuant to the Rights Issue the Company allotted the following securities on 6 September 2011:

- 2,688,078,239 ordinary shares; and
- 750,133,177 Attaching Options expiring 30 June 2013 and exercisable at \$0.004 cents were issued.

The funds raised are being utilised towards the ongoing participation in the Company's interest in the Philippines Offshore Exploration Service Contract SC 54A and SC 54B, repayment of US\$1 million of the outstanding balance of the Convertible Note, costs of the offer and for additional working capital.

**(ii) Convertible Note Amendments**

On 24 August 2011 the Company negotiated the following amendments to the Convertible Note agreement:

- i) The repayment date of the Convertible Notes has been extended by two years from September/October 2011 to September/October 2013;
- ii) The interest rate paid on the outstanding balance of the Convertible Notes has been reduced from 12% to 4% with the remaining 8% capitalised to the balance of the Convertible Notes and payable on maturity; and
- iii) The conversion price of the Convertible Notes is now based on a 10% discount to the 20 day volume weighted average price with a minimum conversion price of 0.4 cents.

These amendments were approved at a shareholders' meeting held on 25 August 2011.

**(iii) SC 54A Farmin**

On 11 July 2011 the Company announced that it has selected its preferred farminee party ("Party") for entry into SC 54A. The Party has completed technical due diligence and is in the process of working through its legal due diligence.

A condition of the farm-in negotiations requires the identity of the Party together with the terms of the farm-in agreement to remain confidential until the necessary documents have been executed.

The transaction contemplated will result in Kairiki reducing its interest in SC 54A from 30.1% to 15.05% in return for a funded work programme involving drilling within the permit.

No other matters or circumstances have arisen since the end of the financial year which significantly affected or may significantly affect the operations of the Group, the results of those operations, or the state of affairs of the Group in future financial years.

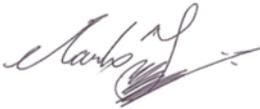
# KAIRIKI ENERGY LIMITED AND ITS CONTROLLED ENTITIES

## DIRECTORS' DECLARATION

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1. In the opinion of the Directors:
  - a) The financial statements and notes and additional disclosures included in the Directors' Report designated as audited, are in accordance with the Corporations Act 2001, including:
    - i) giving a true and fair view of the Company's and consolidated entity's financial position as at 30 June 2011 and of their performance for the year then ended; and
    - ii) complying with Australian Accounting Standards (including the Australian Accounting Interpretations) and the Corporations Regulations 2001; and
  - b) the financial statements and notes thereto are in accordance with International Financial Reporting Standards issued by the International Accounting Standards Board, as disclosed in note 1(c); and
  - c) and 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. This declaration has been made after receiving the declarations required to be made to the directors in accordance with Section 295A of the Corporations Act 2001 for the financial year ended 30 June 2011.

This declaration is signed in accordance with a resolution of the Board of Directors.



**Dr Mark Fenton**  
Managing Director  
Perth, Western Australia  
29 September 2011



Level 18, Central Park Building, 152-158 St Georges Terrace, Perth WA 6000  
P.O. Box 8716, Perth Business Centre WA 6849  
Phone (08) 6364 5076 www.rothsay.com.au

**INDEPENDENT AUDIT REPORT TO THE MEMBERS OF  
KAIRIKI ENERGY LIMITED**

**Report on the financial report**

We have audited the accompanying financial report of Kairiki Energy Limited (the Company) which comprises the balance sheet as at 30 June 2011 and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year ended on that date, a summary of significant accounting policies, other explanatory notes and the directors' declaration of the consolidated entity comprising the company and the entities it controlled at the year's end or from time to time during the year.

**Directors Responsibility for the Financial Report**

The Directors of the Company are responsible for the preparation and true and fair presentation of the financial report in accordance with the Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Act 2001*. This includes responsibility for the maintenance of adequate accounting records and internal controls that are designed to prevent and detect fraud and error, and for the accounting policies and accounting estimates inherent in the financial report. The Directors are also responsible for the remuneration disclosures contained in the directors' report.

**Auditor's Responsibility**

Our responsibility is to express an opinion on the financial report based on our audit. We conducted our audit in accordance with Australian Auditing Standards. These Auditing Standards require that we comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance as to whether the financial report is free of material misstatement.

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

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

**Independence**

We are independent of the Company, and have met the independence requirements of Australian professional ethical requirements and the *Corporations Act 2001*.



Chartered Accountants

Liability limited by the Accountants Scheme, approved  
under the Professional Standards Act 1994 (NSW).



**Audit opinion**

In our opinion the financial report of Kairiki Energy Limited is in accordance with the *Corporations Act 2001*, including:

- a) (i) giving a true and fair view of the consolidated entity's financial position as at 30 June 2011 and of their performance for the year ended on that date; and  
(ii) complying with Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Regulations 2001*;
- b) the consolidated financial report also complies with International Financial Reporting Standards as issued by the International Accounting Standards Board

**Report on the remuneration report**

We have audited the remuneration report included in the directors' report for the year ended 30 June 2011. 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 responsibility is to express an opinion on the remuneration report, based on our audit conducted in accordance with Australian Auditing Standards.

**Audit opinion**

In our opinion the remuneration report of Kairiki Energy Limited for the year ended 30 June 2011 complies with section 300A of the *Corporations Act 2001*.

Rothsay

Graham R Swan  
Partner

Dated 29 September 2011



# KAIRIKI ENERGY LIMITED

## SUPPLEMENTARY INFORMATION

Additional information included in accordance with Listing Rules of the Australian Stock Exchange Limited

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### 3. Unlisted Options

Details of unlisted option holders are as follows:

Class of unlisted options	Number of Options	Number of Holders
Options exercisable at 6.5 cents each between 16 May 2012 and 16 May 2014	49,000,000	7
Holdings of more than 20% of this class		
- Mark Fenton	20,000,000	
- Paul Fry	12,500,000	

### 4. Convertible Notes

10,000,000 Convertible Notes at US\$0.953 each, held by IMC Oil & Gas Investments Ltd. Full details are provided in the notes to the financial statements in this financial report.

### 5. Restricted Securities

There are no restricted securities or securities subject to voluntary escrow.

### 6. Substantial Shareholders

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

	Number of Shares	Percentage of Issued Capital
Yandal Investments Pty Ltd	188,410,000	7.01
HSBC Custody Nominees (Australia) Limited	162,706,665	6.05

### 7. Voting Rights

#### *Shares*

On a show of hands every member present in person or by proxy or attorney or being a corporation by its authorised representative who is present in person or by proxy, shall have one vote for every fully paid ordinary share of which he is a holder.

#### *Options*

Options have no voting rights until such options are exercised as fully paid ordinary shares.

#### *Convertible Notes*

Convertible Notes have no voting rights until such Convertible Notes are converted to fully paid ordinary shares.

### 8. On-market Buy-back

Currently there is no on-market buy-back of the Company's securities.

## PHILIPPINES INTERESTS

Philippines Offshore Oil and Gas Permit (SC 54 Area 'A') – 30.1% Participating Interest

Philippines Offshore Oil and Gas Permit (SC 54 Area 'B') – 22.0% Participating Interest