

Cadogan Petroleum plc

REPORT AND FINANCIAL STATEMENTS

Year ended 31 December 2007

Company Registration No. 05718406

Cadogan Petroleum plc

DIRECTORS AND OFFICERS

DIRECTORS

S P Duffy	Non Executive Chairman
M C Tolley	Executive Director
A Sawka	Executive Director
V P Vivcharyk	Executive Director
P A Biddlestone	Executive Director (Served as Non-Executive Director prior to the 18 April 2008)
A J Cole	Non-Executive Director
N C Corby	Non-Executive Director
P J Dayer	Non-Executive Director
J C Donaldson	Non-Executive Director
N J Hooke	Non-Executive Director

SECRETARY

A Sawka

REGISTERED OFFICE

5th Floor
4/5 Grosvenor Place
London
SW1X 7HJ

AUDITORS

Deloitte & Touche LLP
Chartered Accountants
2 New Street Square
London
EC4A 3BZ

SOLICITORS

Denton Wilde Sapte LLP
One Fleet Place
London
EC4M 7WS

BANKERS

Barclays Bank plc
Level 27
1 Churchill Place
London
E14 5HP

BROKER

Fox-Davies Capital
Whitefriars House
6 Carmelite Street
London
EC4Y 0BS

Anglo Irish Bank Corporation plc
10 Old Jewry
London
EC2R 8DN

Cadogan Petroleum plc

CHIEF EXECUTIVE OFFICER'S REPORT

Operations

In 2007, the Cadogan Group enjoyed a period of intense activity as it continued with its asset development program and grew the business with strategic acquisitions. We made progress in our drilling programme in 2007 and have continued to increase our reserve base effectively through the drill bit and our acquisitions strategy. We are looking forward to 2008 as a value delivery phase as we begin to bring our major fields on stream and increase our production base.

Key field developments

The Pirkovskoe #460 workover was successfully concluded in December 2007, reopening the V-26 horizon at 5,430 metres. Commercial production is targeted to begin from this well in the second half of 2008.

Pirkovskoe #1 (Target depth ('TD') of 5,600 metres) was successfully well tested in the V-16 horizon, the results confirming reserves distribution and production potential of hydrocarbons within this separate reservoir block in the license area. Well testing was completed at the end of December 2007. Drilling has recommenced and at 1 April 2008 was at 5,025 metres.

Pirkovskoe #2 (TD of 5,400 metres) was successfully re-drilled to 3,010 metres. The rig was repaired and upgraded during 2007. Drilling has recommenced and at 1 April 2008 was at 3,053 metres.

Pokrovskoe #2 (TD of 5,400 metres), as the first well drilled on this exploration prospect containing prospective resources. The well has been drilled to a depth of 4,950 metres. Well testing is being conducted in April and May 2008 to prove up the commerciality of the prospect and the well will then be drilled to TD.

Pokrovskoe #1 (TD of 5,400 metres) was spudded on 23 February 2008 and at 1 April 2008 was at 2,200 metres. This will be the second obligation and development well on this prospect.

Borynya #3 in Western Ukraine was spudded in December 2007 having been drilled to a depth of 1,611 metres. This gas field holds contingent resources between the depths of 3,000 to 5,000 metres.

Bitlyanska #2 well site in Western Ukraine is being prepared and access roads are being completed. Rig mobilisation is expected to commence during Q2 2008. This is a 3,000 metres gas field.

Licence restructuring

In late 2007, the Company undertook a restructuring of the Group's interests in the Pirkovskoe, Bitlyanska, Zagoryanskoe, Krasnoyilska and Monastyretske licences. This was a significant step in enhancing the future economics of the Group's key licence areas, favourably positioning the Company as it seeks to increase its production.

Prior to the restructuring, the State owned oil and gas company, NAK Nadra (or its subsidiaries) held these licences, while the Group's working interests were held through Joint Activity Agreements ('JAA') which limited the marketing and sales opportunities from the Group's gas production.

New legislation enacted by the Government of Ukraine obliges any JAA participant with the government to either sell gas to the local population at significantly reduced set domestic prices (US\$63/1000m³), or to sell gas to industrial users at market prices but pay a seven times multiple of the production tax.

Following this change in Ukrainian legislation, Cadogan and NAK Nadra established companies to which NAK Nadra transferred its licences. These companies are owned 90 per cent by the Group and 10 per cent by NAK Nadra in order to reflect their respective intended future funding obligations.

Cadogan Petroleum plc

CHIEF EXECUTIVE OFFICER'S REPORT (CONTINUED)

Licence restructuring (continued)

As a result of the restructuring, the Group is permitted to sell gas produced from the restructured assets at the higher domestic industrial gas market rate rather than the lower residential capped rate and has a direct interest in these licences via its controlling interest in the JAA's. The Group also increased its working interests in these fields, which it now holds directly through the JAAs and indirectly through its controlling interests in the joint venture companies.

Acquisitions

Two strategic acquisitions were made during 2007 to provide the infrastructure and staff required to develop the large oil and gas reserve base acquired through USENCO in the latter part of 2006.

Momentum Energy International Inc. ('Momentum'), a shallow gas production company holding licenses in Western Ukraine, was acquired in May 2007 and has added a net 300 barrels of oil equivalent per day of production, a gas plant, equipment and a full team of operations personnel, including a gas sales team, to Cadogan. This company is well known to management, and although reserves are relatively small, the steady production base and experienced staff have provided Cadogan with the opportunity to fast track its Ukraine operations.

OJSC AgroNaftoGasTechService ('Agro') was acquired in December 2007. Agro is a Ukrainian oilfield service company and oilfield licence holder and the acquisition has added additional infrastructure including a railhead, warehouse base, and machine shops with a significant inventory of heavy equipment. Agro is also the 100% owner of an oilfield licence, Malynovetska.

In addition, Cadogan acquired a 90% interest in the Zagoryanskoe licence in November 2007, through its acquisition of the holding company, Radley Investments Ltd. The field is located adjacent to the Pirkovskoe field in the Poltava region and has significant contingent resources and near term production potential.

Reserves and resources

Cadogan's resources grew substantially with the acquisition of Momentum. The Group's aggregated reserves and resources as at 31 January 2008 are summarised in the following table:

Breakdown of net reserves and contingent resources (mmboe)			
Reserves	1P	2P	3P
Gas	19.6	57.6	105.8
Condensate / Oil	7.8	22.8	43.6
Total	27.4	80.4	149.4
Contingent resources	1C	2C	3C
Gas	128.7	284.9	499.9
Condensate / Oil	20.3	49.5	103.0
Total	149.0	334.4	602.9

Source: GCA reserve report dated April 2008 (except totals for 1C and 3C contingent resources)

For illustrative purposes, the Group has converted the net reserves and resources figures provided by GCA into mmboe using the conversion factor of one mmboe = 0.18 Bcf

Cadogan Petroleum plc

CHIEF EXECUTIVE OFFICER'S REPORT (CONTINUED)

Fund raising and planned use of proceeds

The second round of fund raising was concluded in June 2007 with a total of £12.1 million raised. All first round investors followed with investments in the second round. However, a number of new investors made substantial investments to add to the second round total including the European Bank of Reconstruction and Development, Ingalls and Snyder LLC and Argo Capital Investors Fund SPC.

Between September and December 2007, a third round of fundraising was carried out, with a total of £43.0 million raised. As part of this fundraising, DB UK Holdings Limited, part of Deutsche Bank, took a 5.3% stake in the Company.

The Group remains entirely dependent upon equity financing at present. Management believes that the income to be generated from future operations and the additional funding expected to be raised from the potential initial public offering on the London Stock Exchange in H1 2008 will provide sufficient working capital for the Group's, present requirements, that is for at least 12 months from the date of the proposed initial public offering.

The Group continues to balance its expenditure between the acquisition of strategic assets and developing the Group's existing operations on the Pirkovskoe, Pokrovskoe, Bitlyanska, Borynya and Zagoryanskoe fields to ensure they are fully funded and able to achieve the production and reserves conversion targets which management have set.

Outlook

We expect the next 12 months to be an exciting time for the Group as we continue to focus our resources on increasing our reserve base and bringing key fields on stream. We are focused on delivering significant near to medium term production growth.

The gas pricing environment in Ukraine continues to improve and during the course of 2007, the price payable by industrial companies increased to over \$150/1000 per thousand cubic metres (exclusive of VAT), and this trend appears to have continued in 2008.

Mark C Tolley
Chief Executive Officer
9 May 2008



Cadogan Petroleum plc

DIRECTORS' REPORT

The Directors present their report on the affairs of the Group, together with the financial statements and auditors' report for the year ended 31 December 2007.

Principal activities

The Group's principal activity is independent oil and gas exploration, development and production, focused exclusively in Ukraine. The Group has built a portfolio of assets through a series of acquisitions and currently has significant working interest in 11 licence areas covering 14 fields in Ukraine. The Group's assets are located in two major proven hydrocarbon basins in Ukraine, the Dniepr-Donets Basin in Eastern Ukraine and the Carpathian region in Western Ukraine.

Business review

The Company is required by the Companies Act to set out in this report a fair review of the business of the Group during the financial year ended 31 December 2007 and of the position of the Group at the end of the year and a description of the principal risks and uncertainties facing the Group ('business review'). Certain of the information that fulfils the requirements of the business review can be found within the Chief Executive Officer's Report on pages 3 to 5. The Chief Executive Officer's Report also includes details of expected future developments in the business of the Group and an indication of its exploration and development activities.

Given the stage of development of the Group's operations, the key performance indicators used by management for monitoring our progress and our strategic objectives for the business are as follows:

- the quantification of the Group's reserves and resources; and
- the progression of the Group's oil and gas projects from exploration to production.

Details of the Company's plans to progress the Group's oil and gas projects are provided in the Chief Executive Officer's Report on pages 3 to 5.

The subsidiary undertakings principally affecting the Group's losses and net assets in the year are listed in note 18 to the financial statements.

Risk and uncertainties

The principal risks and uncertainties facing the Group are as follows:

Operating environment

The Ukrainian economy continues to display certain characteristics consistent with that of an economy in transition. These characteristics which include low levels of liquidity in the capital markets, relatively high inflation and the existence of currency control, cause the national currency to be illiquid outside Ukraine. The stability of the Ukrainian economy will be significantly impacted by the Ukrainian's government's policies and actions in relation to supervisory, legal and economic reforms. The Ukrainian government therefore exercises, and it is expected to continue to exercise influence over the sector.

Domestic demand is rising in line with Ukrainian economic growth, and the government of Ukraine has been taking measures, including permitting sales to industrial customers at market prices, to stimulate domestic production and reduce dependency on imported gas supplies which have been rising in price.

The oil and gas sector is of considerable importance to Ukraine for various reasons, including economic and strategic considerations. As a result of the economic and strategic importance of the oil and gas sector, the Group's ability to sell hydrocarbon products to industrial customers in Ukraine at attractive prices will be driven by Ukrainian government policies towards the oil and gas sector generally, and in particular pricing, taxation and licensing policies.

Drilling and workover activities

Higher production volumes, and resulting revenues, operating profits and cash flows, are dependent on the effectiveness of the Group's drilling and workover activities on its existing and planned wells. Due to the deep horizons within which the Group's main gas reservoirs are located, successful hydrocarbon extraction at commercial rates of production will depend upon the ability of the Group to drill and workover its wells in a timely and cost effective manner. Application of well stimulation techniques to remove formation damage and enhance flow rates will also contribute to the Group's ability to achieve commercial production.

Cadogan Petroleum plc

DIRECTORS' REPORT (CONTINUED)

Risk and uncertainties (continued)

Production volumes and reserve and resource levels

The Group's current exploration, development and production strategy is focused on achieving commercial production on Pirkosvskoe, as these provide the lowest risk and cost of extraction, and on transferring those hydrocarbons that are currently classified as contingent or prospective resources into reserves through exploration and appraisal drilling.

The Group's future production volumes will be determined by the number of wells drilled, their depth, the amount of time and resource it takes to bring planned wells into production, and the flow rates achieved in the Group's existing and planned wells.

Political and licensing issues

The Ukrainian government authorises all exploration, development and production of hydrocarbons in Ukraine, and closely monitors compliance with hydrocarbon license obligations. Exploration, development and production licenses entitle the holder to the rights to revenue and profits from hydrocarbon production in the licensed field according to the level of the holder's working interest in the ownership of the license, subject to certain work programme obligations and other requirements on the part of the license holder.

Reserves and resources

Commercial reserves are proven and probable oil and gas reserves, which are defined as the estimated quantities of crude oil, natural gas and natural gas liquids which geological, geophysical and engineering data demonstrate with a specified degree of certainty to be recoverable in future years from known reservoirs and which are considered commercially producible. There should be a 50 per cent statistical probability that the actual quantity of recoverable reserves will be more than the amount estimated as a proven and probable reserves and a 50 per cent statistical probability that it will be less.

Commercial reserves are determined using estimates of oil and gas in place, recovery factors and future oil and gas prices. The Group relies upon competent persons reports (CPR) provided by independent advisors for the determination of oil and gas reserves and resources.

Financial risks

Details about the Group's exposure to financial risks are set out in note 28 to the financial statements.

Details about the use of financial instruments used by the Company and its subsidiaries as well as exposure to financial risks, are given in note 28 to the financial statements.

Dividends

The Directors do not recommend a dividend for the year ended 31 December 2007 (2006: £nil).

Capital structure

Details of the authorised and issued share capital, together with details of movements in the Company's issued share capital during the year are shown in note 24. The Company has one class of ordinary shares. Each share carries the right to one vote at the annual general meeting ('AGM') of the Company.

Details of share option schemes provided to certain Directors are set in note 25.

No person has any special rights of control over the Company's share capital and all issued shares are fully paid.

With regard to the appointment and replacement of Directors, the Company is governed by its Articles of Association, the Companies Act and related legislation. The articles may be amended themselves by special resolution of the shareholders.

Cadogan Petroleum plc

DIRECTORS' REPORT (CONTINUED)

Directors

The following Directors held office during the year:

W P Jeffcock - Chairman	Resigned 18 April 2008
M C Tolley - Chief Executive Officer	Appointed 10 March 2006
A Sawka - Chief Financial Officer	Appointed 13 April 2006
V Vivcharyk - Chief Operating Officer	Appointed 5 June 2007
P A Biddlestone - Asset Development Director	Appointed 20 April 2006
I R Baron - Non-Executive Director	Resigned 18 April 2008
N C Corby - Non-Executive Director	Appointed 19 December 2006
J C Donaldson - Non-Executive Director	Appointed 5 March 2007

The Company has approved the appointment of four new Non-Executive Directors. They are expected to be appointed to the Board prior to the 2008 AGM.

Third party indemnity provision for directors

The Company has made qualifying third party indemnity provisions for the benefit of its Directors which were made during the year and remain in force at the date of this report.

Creditor payment policy

The Group's policy is to ensure that, in the absence of dispute, all suppliers are dealt with in accordance with its standard payment practice whereby all outstanding trade accounts are settled within the term agreed with the supplier at the time of the supply or otherwise 30 days from receipt of the relevant invoice. The Group's trade creditor balances at 31 December 2007 were £1,493,679 (2006: £2,018,298) equivalent to 45 (2006: 30) days' purchases, based on an average daily amount invoiced during the year.

Charitable and political donations

During the year, the Group made £122,276 (2006: £nil) of charitable donations and made no political contributions (2006: £nil).

Substantial shareholdings

On 9 May 2008, substantial shareholdings in the Company were as follows:

Name	No. of shares	Percentage held
HBK Master Fund LP	47,578,000	10.54
Altima Global Special Situations Master Fund	29,811,461	6.60
3Legs Resources plc	28,591,505	6.33
European Bank for Reconstruction and Development	24,511,517	5.43
DB UK Holdings Ltd	24,390,242	5.40
Ingalls and Snyder LLC	22,000,000	4.87
Hillside Apex Fund Ltd	18,492,200	4.10
Altima Global Special Opportunities Master Fund Ltd	17,520,000	3.88
Mr Roy Grainger Williams (1)	14,665,193	3.25
Chase Nominees Ltd	14,250,000	3.16
Argo Capital Investors Fund SPC	14,100,000	3.12
QVT Fund LP	13,718,149	3.04

Notes:

(1) Mr Roy Williams has an interest in the Company's shares held by 3Legs Resources plc in addition to those shares he holds personally, as a result of his interest in Cardinal Group Limited and Mustardseed Estates Limited, both of which are shareholders of 3Legs Resources plc.

Events after balance sheet date

Events after the balance sheet date have been disclosed in note 31 to the financial statements.

Cadogan Petroleum plc

DIRECTORS' REPORT (CONTINUED)

Statement as to disclosure of information to auditors

Each of the persons who is a Director at the date of approval of this Annual Report confirms that:

- so far as the Director is aware, there is no relevant audit information of which the Company's auditors are unaware; and
- the Director has taken all the steps that he ought to have taken as a Director in order to make himself aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of s234ZA of the Companies Act 1985.

Deloitte & Touche LLP have expressed their willingness to continue in office as auditors and a resolution to reappoint them will be proposed at the forthcoming AGM.

5th Floor
4/5 Grosvenor Place
London SW1X 7HJ

By Order of the Board,



Director

9 May 2008

Cadogan Petroleum plc

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The Directors are responsible for preparing the Annual Report and the financial statements. The Directors have elected to prepare financial statements for the Group and the Company in accordance with International Financial Reporting Standards as adopted by the European Union ('IFRSs'). Company law requires the Directors to prepare such financial statements in accordance with IFRSs, the Companies Act 1985 and Article 4 of the IAS Regulation.

International Accounting Standard 1 requires that financial statements present fairly for each financial year the Company's financial position, financial performance and cash flows. This requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the International Accounting Standards Board's 'Framework for the preparation and Presentation of Financial Statements'. In virtually all circumstances, a fair presentation will be achieved by compliance with all applicable IFRSs. Directors are also required to:

- properly select and apply accounting policies;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information; and
- provide additional disclosures when compliance with the specific requirements in IFRSs is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance.

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company, for safeguarding the assets, for taking reasonable steps for the prevention and detection of fraud and other irregularities and for the preparation of a Directors' report which complies with the requirements of the Companies Act 1985.

The Directors are responsible for the maintenance and integrity of the Company website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements differs from legislation in other jurisdictions.

Cadogan Petroleum plc

INDEPENDENT AUDITORS' REPORT

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF CADOGAN PETROLEUM PLC

We have audited the Group and parent company financial statements (the 'financial statements') of Cadogan Petroleum plc for the year ended 31 December 2007 which comprise the Consolidated income statement, the Consolidated and Company balance sheets, the Consolidated and Company cash flow statements, the Consolidated and Company statement of changes in equity and the related notes 1 to 31. These financial statements have been prepared under the accounting policies set out therein.

This report is made solely to the Company's members, as a body, in accordance with section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and auditors

The Directors' responsibilities for preparing the Annual Report and the financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the Directors' Report is consistent with the financial statements.

In addition we report to you if, in our opinion, the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding Directors' remuneration and other transactions is not disclosed.

We read the other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any further information outside the Annual Report.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the Directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Group's and Company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion, we also evaluated the overall adequacy of the presentation of information in the financial statements.

Emphasis of matter – Going concern

Without qualifying our opinion, we draw attention to the disclosures made in note 3(a) and 4(a) of the financial statements concerning the Group's ability to continue as a going concern. The Group incurred a net loss of £15,199,221 for the year ended 31 December 2007 and, as of the date of this report, the Group had insufficient cash resources to continue its operations and development programme for at least the next 12 months and is therefore reliant on obtaining further funding. These conditions indicate the existence of a material uncertainty which may cast significant doubt about the Group's ability to continue as a going concern. The financial statements do not include the adjustments that would result if the Group was unable to continue as a going concern.

Cadogan Petroleum plc

INDEPENDENT AUDITORS' REPORT (CONTINUED)

Opinion

In our opinion:

- the financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the Group's affairs as at 31 December 2007 and of its loss for the year then ended;
- the parent company's financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union as applied in accordance with the provisions of the Companies Act 1985, of the state of the parent company's affairs as at 31 December 2007;
- the financial statements have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the Directors' Report is consistent with the financial statements.



Deloitte & Touche LLP

Chartered Accountants and Registered Auditors

London

9 May 2008

Cadogan Petroleum plc

Consolidated income statement Year ended 31 December 2007

	Notes	2007 £	2006 £
Revenue	5	665,627	-
Cost of sales		(611,345)	-
Gross profit		<u>54,282</u>	<u>-</u>
Administrative expenses		(12,355,428)	(4,016,497)
Other operating expenses	7	(2,926,342)	(1,224,996)
Operating loss		<u>(15,227,488)</u>	<u>(5,241,493)</u>
Investment revenue	10	277,984	88,085
Finance costs	11	(28,154)	(18,567)
Loss before tax		<u>(14,977,658)</u>	<u>(5,171,975)</u>
Tax – foreign	12	(221,563)	(11,423)
Loss for the year	8	<u>(15,199,221)</u>	<u>(5,183,398)</u>
Attributable to:			
Equity holders of the parent		(15,197,276)	(5,183,398)
Minority interest		(1,945)	-
		<u>(15,199,221)</u>	<u>(5,183,398)</u>
Loss per share			
Basic and diluted	13	<u>(4.77p)</u>	<u>(2.80p)</u>

All operations were continuing throughout both years.

Cadogan Petroleum plc

Consolidated balance sheet As at 31 December 2007

	Notes	2007 £	2006 £
Non-current assets			
Goodwill	14	2,804,199	-
Intangible exploration and evaluation assets	15	28,687,262	5,771,074
Other intangible assets	16	12,537	24,666
Property, plant and equipment	17	22,732,979	4,939,541
Other receivables	20	3,059,654	-
		<u>57,296,631</u>	<u>10,735,281</u>
Current assets			
Inventories	21	1,654,464	835,552
Trade and other receivables	20	1,686,477	3,873,901
Cash and cash equivalents	20	13,956,712	8,688,261
		<u>17,297,653</u>	<u>13,397,714</u>
Total assets		<u>74,594,284</u>	<u>24,132,995</u>
Current liabilities			
Trade and other payables	22	(3,055,129)	(2,448,999)
Financial liability	22	(1,583,333)	-
Current provisions	23	(374,291)	(141,124)
		<u>(5,012,753)</u>	<u>(2,590,123)</u>
Net current assets		<u>12,284,900</u>	<u>10,807,591</u>
Non-current liabilities			
Deferred tax liabilities	21	(967,369)	(275,867)
Long-term provisions	23	(398,703)	(412,353)
		<u>(1,366,072)</u>	<u>(688,220)</u>
Total liabilities		<u>(6,378,825)</u>	<u>(3,278,343)</u>
Net assets		<u>68,215,459</u>	<u>20,854,652</u>
Equity			
Share capital	24	4,169,409	2,570,789
Share premium		78,027,552	23,743,164
Shares to be issued		2,260,209	-
Accumulated deficit		(21,517,721)	(6,320,445)
Cumulative translation reserves		(491,840)	(157,824)
Other reserves		5,564,027	1,018,968
Equity attributable to equity holders of the parent		<u>68,011,636</u>	<u>20,854,652</u>
Minority interest		<u>203,823</u>	<u>-</u>
Total equity		<u>68,215,459</u>	<u>20,854,652</u>

The financial statements were approved by the board of Directors and authorised for issue on 9 May 2008.
They were signed on its behalf by:

Alex Sawka
9 May 2008

Director

The notes on pages 20 to 58 form part of these financial statements.

Cadogan Petroleum plc

Company balance sheet As at 31 December 2007

	Notes	2007 £	2006 £
Non-current assets			
Investments	18	4,144,682	1,598,016
Amounts due from subsidiaries	30	82,298,170	23,378,531
		<u>86,442,852</u>	<u>24,976,547</u>
Current assets			
Trade and other receivables	20	64,251	45,269
Cash and cash equivalents	20	84,629	1,405,388
		<u>148,880</u>	<u>1,450,657</u>
Total assets		<u>86,591,732</u>	<u>26,427,204</u>
Current liabilities			
Trade and other payables	22	(324,142)	(120,000)
Financial liability	22	(1,583,333)	-
		<u>(1,907,475)</u>	<u>(120,000)</u>
Net current (liabilities) /assets		<u>(1,758,595)</u>	<u>1,330,657</u>
Total liabilities		<u>(1,907,475)</u>	<u>(120,000)</u>
Net assets		<u>84,684,257</u>	<u>26,307,204</u>
Equity			
Share capital	24	4,169,409	2,570,789
Share premium		78,027,552	23,743,164
Shares to be issued		2,260,209	-
Accumulated deficit		(4,447,406)	(136,183)
Other reserves		4,674,493	129,434
Total equity		<u>84,684,257</u>	<u>26,307,204</u>

The financial statements were approved by the board of Directors and authorised for issue on 9 May 2008.
They were signed on its behalf by:

Alex Sawka
9 May 2008

Director

The notes on pages 20 to 58 form part of these financial statements.

Cadogan Petroleum plc

Consolidated cash flow statement Year ended 31 December 2007

	Notes	2007 £	2006 £
Net cash outflow from operating activities	27	<u>(12,286,361)</u>	<u>(7,498,423)</u>
Investing activities			
Acquisition of subsidiaries	26	(18,356,764)	(1,145,853)
Purchases of property, plant and equipment		(4,600,831)	(5,127,908)
Purchases of intangible exploration and evaluation assets		(17,493,816)	(2,814,470)
Purchase of other intangible assets		(8,924)	(24,666)
Proceeds from sale of property, plant and equipment		260,789	13,754
Interest received		267,784	88,085
Net cash used in investing activities		<u>(39,931,762)</u>	<u>(9,011,058)</u>
Financing activities			
Proceeds from issue of shares		55,060,780	26,041,031
Proceeds from shares to be issued		2,584,032	-
Proceeds from issue of other equity instruments		-	57,500
Interest paid		-	(9,192)
Redemption of other equity instruments		-	(900,000)
Loan repayment		-	(180,000)
Cash received from minority shareholders on incorporation of subsidiaries		8,766	-
Net cash from financing activities		<u>57,653,578</u>	<u>25,009,339</u>
Net increase in cash and cash equivalents		5,435,455	8,499,858
Effect of foreign exchange rate changes		(167,004)	(59,773)
Cash and cash equivalents at beginning of year		<u>8,688,261</u>	<u>248,176</u>
Cash and cash equivalents at end of year		<u><u>13,956,712</u></u>	<u><u>8,688,261</u></u>

Cadogan Petroleum plc

Company cash flow statement Year ended 31 December 2007

	Notes	2007 £	Period from 22 February 2006 to 31 December 2006 £
Net cash outflow from operating activities	27	<u>(212,493)</u>	<u>(130,957)</u>
Investing activities			
Acquisition of subsidiary		(14,614)	-
Interest received		181,175	69,505
Loans to subsidiary company		<u>(58,919,639)</u>	<u>(23,378,531)</u>
Net cash used in investing activities		<u>(58,753,078)</u>	<u>(23,309,026)</u>
Financing activities			
Proceeds from issue of shares		55,060,780	24,845,371
Proceeds from shares to be issued		<u>2,584,032</u>	<u>-</u>
Net cash from in financing activities		<u>57,644,812</u>	<u>24,845,371</u>
Net (decrease)/increase in cash and cash equivalents		<u>(1,320,759)</u>	<u>1,405,388</u>
Cash and cash equivalents at beginning of period		<u>1,405,388</u>	<u>-</u>
Cash and cash equivalents at end of period		<u><u>84,629</u></u>	<u><u>1,405,388</u></u>

Cadogan Petroleum plc

Consolidated statement of changes in equity Year ended 31 December 2007

	Share capital £	Share premium £	Shares to be issued £	Accumulated deficit £	Cumulative translation reserves £	Other £	Minority interest £	Total £
As at 1 January 2006	20,539	1,285,465	-	(1,087,047)	-	865,836	-	1,084,793
Issue of equity shares	1,503	1,164,207	-	-	-	-	-	1,165,710
Premium arising on issue of options	-	15,836	-	-	-	(15,836)	-	-
Redemption of other equity instruments	-	-	-	(50,000)	-	(850,000)	-	(900,000)
	22,042	2,465,508	-	(1,137,047)	-	-	-	1,350,503
Group reorganisation (see notes 4(b) and 18)	(22,042)	(2,465,508)	-	-	-	2,487,550	-	-
Share exchange (see note 18)	1,598,016	-	-	-	-	(1,598,016)	-	-
Issue of equity shares	972,773	25,265,190	-	-	-	-	-	26,237,963
Expenses of issue of equity shares	-	(1,392,592)	-	-	-	-	-	(1,392,592)
Share-based payments (see note 25)	-	(129,434)	-	-	-	129,434	-	-
Net loss for the year	-	-	-	(5,183,398)	-	-	-	(5,183,398)
Exchange translation differences on foreign operations	-	-	-	-	(157,824)	-	-	(157,824)
As at 1 January 2007	2,570,789	23,743,164	-	(6,320,445)	(157,824)	1,018,968	-	20,854,652
Issue of equity shares	1,598,620	57,504,752	-	-	-	-	-	59,103,372
Equity shares to be issued	-	-	2,260,209	-	-	-	-	2,260,209
Minority interest on incorporation of subsidiaries	-	-	-	-	-	-	8,766	8,766
Minority interest on acquisition of subsidiary (see note 26)	-	-	-	-	-	-	197,002	197,002
Expenses of issue of equity shares	-	(2,919,192)	-	-	-	-	-	(2,919,192)
Share-based payments (see note 25)	-	(301,172)	-	-	-	4,545,059	-	4,243,887
Net loss for the year	-	-	-	(15,197,276)	-	-	(1,945)	(15,199,221)
Exchange translation differences on foreign operations	-	-	-	-	(334,016)	-	-	(334,016)
As at 31 December 2007	4,169,409	78,027,552	2,260,209	(21,517,721)	(491,840)	5,564,027	203,823	68,215,459

Cadogan Petroleum plc

Company statement of changes in equity Year ended 31 December 2007

	Share capital £	Share premium £	Shares to be issued £	Accumulated deficit £	Other £	Total £
As at 22 February 2006	-	-	-	-	-	-
Share exchange (see note 18)	1,598,016	-	-	-	-	1,598,016
Issue of equity shares	972,773	25,265,190	-	-	-	26,237,963
Expenses of issue of equity shares	-	(1,392,592)	-	-	-	(1,392,592)
Share-based payment (see note 25)	-	(129,434)	-	-	129,434	-
Net loss for the year	-	-	-	(136,183)	-	(136,183)
	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
As at 1 January 2007	2,570,789	23,743,164	-	(136,183)	129,434	26,307,204
Issue of equity shares	1,598,620	57,504,752	-	-	-	59,103,372
Equity shares to be issued	-	-	2,260,209	-	-	2,260,209
Expenses of issue of equity shares	-	(2,919,192)	-	-	-	(2,919,192)
Share-based payment (see note 25)	-	(301,172)	-	-	4,545,059	4,243,887
Net loss for the year	-	-	-	(4,311,223)	-	(4,311,223)
	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
As at 31 December 2007	<u>4,169,409</u>	<u>78,027,552</u>	<u>2,260,209</u>	<u>(4,447,406)</u>	<u>4,674,493</u>	<u>84,684,257</u>

Cadogan Petroleum plc

Notes to the financial statements Year ended 31 December 2007

1. General information

Cadogan Petroleum plc ('the Company'), together with its subsidiaries ('the Group'), is a company incorporated in Great Britain on 22 February 2006 under the Companies Act 1985, which acts as the holding company for the Group. The address of the registered office is 5th Floor, 4/5 Grosvenor Place, London SW1X 7HJ.

The nature of the Group's operations is exploration and development of oil and gas reserves in Ukraine.

The financial statements are presented in pounds sterling, the functional currency of the Company. Foreign operations are included in accordance with the policies set out in note 3(b).

2. Adoption of new and revised Standards

In the current year, the Group has adopted IFRS 7 *Financial Instruments: Disclosures* which is effective for annual reporting periods beginning on or after 1 January 2007, and the related amendment to IAS 1 *Presentation of financial Statements*. The impact of the adoption of IFRS 7 and the changes to IAS 1 has been to expand the disclosures provided in these financial statements regarding the Group's financial instruments and management capital (see note 28). There was no effect on the Group's reported income or net assets as a result of the adoption of these new Standards.

At the date of authorisation of the financial statements, the following Standards and Interpretations which have not been applied in the financial statements were in issue but not yet effective:

- IFRS 3: *Business Combinations (Revised 2008)* – Comprehensive revision on applying the acquisition method
- IFRS 8: *Operating Segments*
- IAS 1 (Revised 2007): *Presentation of Financial Statements* – Comprehensive revision including a statement on comprehensive income
- IAS 23 (Revised 2007): *Borrowing Costs* – Comprehensive revision to prohibit immediate expensing
- IAS 27 (Revised 2008): *Consolidated and Separate Financial Statements*
- IFRIC 11: *IFRS 2 - Group and Treasury Share Transactions*
- IFRIC 12: *Service Concession Arrangements*
- IFRIC 13: *Customer Loyalty Programme*
- IFRIC 14: *IAS 19 - The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction*

The Directors anticipate that the adoption of these Standards and Interpretations in future periods will have no material impact upon the financial statements of the Company or the Group.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

3. Significant accounting policies

A summary of the principal accounting policies, all of which have been consistently applied throughout the current year and prior year, is set out below.

(a) Basis of accounting

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by European Union and related interpretations. The financial statements have been prepared on the historical cost convention, except for share-based payments and the financial liability that have been measured at fair value, and using accounting policies consistent with IFRS.

The Group is currently dependent upon the financial support received from its investors and other related parties and will be until its revenues from primary business activities are sufficient to satisfy its obligations and fully finance its exploration and development programme. The Group incurred a net loss of £15,199,221 during the year ended 31 December 2007 and, as of the date of this report, the Group had insufficient cash resources to continue its operations and development programme for at least the next twelve months and is therefore reliant on obtaining further funding. These conditions indicate the existence of a material uncertainty which may cast doubt about the Group's ability to continue as a going concern. The Group's management believe that the capital resources available at the date of issue of these financial statements, together with income to be generated from future operations and additional funding expected to be raised from the proposed initial public offering on the London Stock Exchange expected to be completed in H1 2008, are sufficient for the Group to continue as a going concern for the foreseeable future. Accordingly, the financial statements have been presented on the assumption that the Group will continue as a going concern and does not include any adjustments that may be required if the Group were unable to continue realising its assets and discharging its liabilities in the ordinary course of business.

The separate financial statements of the Company are presented as required by the Companies Act 1985. As permitted by that Act, the separate financial statements have been prepared in accordance with IFRS. In accordance with the provisions of section 230 of the Companies Act, the income statement of the Company is not presented separately.

(b) Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries) made up to 31 December each year. Control is achieved where the Company has the power to govern the financial and operating policies of an investee entity so as to obtain benefits from its activities.

Minority interests in the net assets of consolidated subsidiaries are identified separately from the Group's equity therein. Minority interests consist of the amount of those interests at the date of the original business combination (see below) and the minority's share of changes in equity since the date of the combination. Losses applicable to the minority in excess of the minority's interest in the subsidiary's equity are allocated against the interests of the Group except to the extent that the minority has a binding obligation and is able to make an additional investment to cover the losses.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring the accounting policies used into line with those used by the Group.

All intra-group transactions, balances, income and expenses are eliminated on consolidation.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

3. Significant accounting policies (continued)

(c) *Interests in joint ventures*

A joint venture is a contractual arrangement whereby the Group and other parties undertake an economic activity that is subject to joint control.

Where a consolidated member of the Group participates in unincorporated joint ventures, that member accounts directly for its share of the jointly controlled assets, liabilities and related income and expenses which are then similarly included in the consolidated financial statements of the Group.

(d) *Business combinations*

The acquisition of subsidiaries is accounted for using the purchase method. The cost of the acquisition is measured at the aggregate of the fair values, at the date of exchange, of assets given, liabilities incurred or assumed, and equity instruments issued in exchange for control of the acquiree, plus any costs directly attributable to the business combination.

The acquiree's identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition under IFRS 3 *Business Combinations* are recognised at their fair value at the acquisition date, except for non-current assets (or disposal groups) that are classified as held for resale in accordance with IFRS 5 *Non Current Assets Held for Sale and Discontinued Operations*, which are recognised and measured at fair value less costs to sell.

Goodwill arising on acquisition is recognised as an asset and initially measured at cost, being the excess of the cost of the business combination over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities recognised. If, after reassessment, the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities exceed the cost of the business combination, the excess is recognised immediately in profit or loss.

The interest of minority shareholders in the acquiree is initially measured at the minority's proportion of the net fair value of the assets, liabilities and contingent liabilities recognised.

(e) *Investments*

Fixed asset investments, including investments in subsidiaries, are stated at cost and reviewed for impairment if there are any indications that the carrying value may not be recoverable.

(f) *Goodwill*

Goodwill is initially recognised as an asset at cost and is subsequently measured at cost less any accumulated impairment loss. Goodwill which is recognised as an asset is reviewed for impairment at least annually. Any impairment is recognised immediately in the income statement and is not subsequently reversed.

For the purpose of impairment testing, goodwill is allocated to each of the Group's cash-generating units expected to benefit from the synergies of the combination. Cash-generating units to which goodwill has been allocated are tested for impairment annually, or more frequently when there is an indication that the unit may be impaired. If the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the carrying amount of any goodwill to the unit and then to the other assets in the unit pro rata on the basis of the carrying amount of each asset in the unit. An impairment loss recognised for goodwill is not reversed in a subsequent period.

On disposal of a subsidiary, associate or jointly controlled entity, the attributable amount of goodwill is included in the determination of the profit or loss on disposal.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

3. Significant accounting policies (continued)

(g) Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for hydrocarbon products and services provided in the normal course of business, net of discounts, VAT and other sales-related taxes.

Sales are recognised when hydrocarbons are delivered and title has passed.

Interest income is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.

To the extent that revenue arises from test production during an evaluation programme, an amount is charged from evaluation costs to cost of sales, so as to reflect a zero net margin.

(h) Foreign currencies

The individual financial statements of each Group company are presented in the currency of the primary economic environment in which it operates (its functional currency). For the purpose of the consolidated financial statements, the results and financial position of each group company are expressed in pound sterling, which is the functional currency of the Company, and the presentation currency for the consolidated financial statements.

In preparing the financial statements of the individual companies, transactions in currencies other than the functional currency of each Group company ('foreign currencies') are recorded in the functional currency at the rates of exchange prevailing on the dates of the transactions. At each balance sheet date, monetary assets and liabilities that are denominated in foreign currencies are retranslated into the functional currency at the rates prevailing on the balance sheet date. Non-monetary assets and liabilities carried at fair value that are denominated in foreign currencies are translated at the rates prevailing at the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Gains and losses arising on retranslation are included in net profit or loss for that period, except for exchange differences arising on non-monetary assets and liabilities carried at fair value where the changes in fair value are recognised directly in equity.

For the purpose of presenting consolidated financial statements, the assets and liabilities of the Group's foreign operations are translated at exchange rates prevailing on the balance sheet date. Income and expense items are translated at the average exchange rates for the period, unless exchange rates fluctuate significantly during that period, in which case the exchange rates at the date of transactions are used. Exchange differences arising, if any, are classified as equity and transferred to the Group's translation reserve. Such translation differences are recognised as income or as expenses in the period in which the operation is disposed of.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate.

(i) Taxation

The tax expense represents the sum of the tax currently payable and deferred tax.

The tax currently payable is based on taxable profit for the year. Taxable profit differs from net profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Company's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

3. Significant accounting policies (continued)

(i) Taxation (continued)

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the reporting package and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from the initial recognition of goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the tax profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries and associates, and interests in joint ventures, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

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

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised, using tax rates that have been enacted or substantively enacted at the balance sheet date. Deferred tax is charged or credited in the income statement, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

(j) Property, plant and equipment and other intangible assets

Property, plant and equipment and other intangible assets (software licences) are carried at cost less accumulated depreciation and any recognised impairment loss.

Depreciation is charged so as to write off the cost or valuation of assets, other than land and properties under construction, over their estimated useful lives, using the straight-line method, on the following bases:

Other

Buildings	4%
Fixtures and equipment	10%-30%

Other intangible assets

Software licences	2 to 5 years
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The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in income.

(k) Impairment of tangible and other intangible assets excluding goodwill

At each balance sheet date, the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where the asset does not generate cash flows that are independent from other assets, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Recoverable amount is the higher of fair value less costs to sell and value in use. 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 for which the estimates of future cash flows have not been adjusted.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

3. Significant accounting policies (continued)

(k) Impairment of tangible and other intangible assets excluding goodwill (continued)

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised as an expense immediately, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

The Group considers the whole of Ukraine to be one cash-generating unit and therefore aggregates all Ukraine assets for the purposes of determining whether impairment has occurred.

Where an impairment loss subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount, but so 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 (cash-generating unit) in prior years. A reversal of an impairment loss is recognised as income immediately, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

(l) Intangible exploration and evaluation assets

The Group applies the full cost method of accounting for Exploration and Evaluation ('E&E') costs, having regard to the requirements of IFRS 6 *Exploration for and Evaluation of Mineral Resources*. Under the full cost method of accounting, costs of exploring for and evaluating oil and gas properties are accumulated by reference to appropriate cost centres being the appropriate oil or gas property, but are tested for impairment on a cost pool basis as described below.

E&E assets comprise costs of (i) E&E activities that are ongoing at the balance sheet date, pending determination of whether or not commercial reserves exist and (ii) costs of E&E that, whilst representing part of the E&E activities associated with adding to the commercial reserves of an established cost pool, did not result in the discovery of commercial reserves.

Pre-licence costs

Costs incurred prior to having obtained the legal rights to explore an area are expensed directly to the income statement as they are incurred.

Exploration and Evaluation costs

All costs of E&E are initially capitalised as E&E assets. Payments to acquire the legal right to explore, costs of technical services and studies, seismic acquisition, exploratory drilling and testing are capitalised as intangible E&E assets.

Tangible assets used in E&E activities (such as the Group's vehicles, drilling rigs, seismic equipment and other property plant and equipment) are classified as property plant and equipment. However, to the extent that such a tangible asset is consumed in developing an intangible E&E asset, the amount reflecting that consumption is recorded as part of the cost of the intangible asset. Such intangible costs include directly attributable overhead, including the depreciation of property plant and equipment utilised in E&E activities, together with the cost of other materials consumed during the exploration and evaluation phases.

E&E costs are not amortised prior to the conclusion of appraisal activities.

Treatment of E&E assets at conclusion of appraisal activities

Intangible E&E assets related to each exploration licence/prospect are carried forward, until the existence (or otherwise) of commercial reserves has been determined. If commercial reserves have been discovered, the related E&E assets are assessed for impairment on a cost pool basis as set out below and any impairment loss is recognised in the income statement. The carrying value, after any impairment loss, of the relevant E&E assets is then reclassified as development and production assets.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

3. Significant accounting policies (continued)

(l) Intangible exploration and evaluation assets (continued)

Treatment of E&E assets at conclusion of appraisal activities (continued)

Intangible E&E assets that relate to E&E activities that are determined not to have resulted in the discovery of commercial reserves remain capitalised as intangible E&E assets at cost less accumulated amortisation, subject to meeting a pool-wide impairment test in accordance with the accounting policy for impairment of E&E assets set out below. Such E&E assets are amortised on a unit-of-production basis over the life of the commercial reserves of the pool to which they relate.

Impairment of E&E assets

E&E assets are assessed for impairment when facts and circumstances suggest that the carrying amount may exceed its recoverable amount. Such indicators include, but are not limited to, those situations outlined in paragraph 20 of IFRS 6 and include the point at which a determination is made as to whether or not commercial reserves exist.

Where there are indications of impairment, the E&E assets concerned are tested for impairment. Where the E&E assets concerned fall within the scope of an established full cost pool, the E&E assets are tested for impairment together with all development and production assets associated with that cost pool, as a single cash generating unit.

The aggregate carrying value is compared against the expected recoverable amount of the pool, generally by reference to the present value of the future net cash flows expected to be derived from production of commercial reserves. Where the E&E assets to be tested fall outside the scope of any established cost pool, there will generally be no commercial reserves and the E&E assets concerned will generally be written off in full.

Any impairment loss is recognised in the income statement as additional depreciation and amortisation, and separately disclosed. It is initially recorded against the carrying value of the related E&E asset. To the extent the impairment exceeds the carrying value of the E&E asset, a separate impairment test is conducted on the development and production assets.

(m) Development and production assets

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

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

Depreciation of producing assets

The net book value of producing assets are depreciated generally on a field-by-field basis on a unit of production method by reference to the ratio of production in the year and the related proved and probable reserves of the field, taking into account future development expenditures necessary to bring those reserves into production.

Producing assets are generally grouped with other assets that are dedicated to serving the same reserves for depreciation purposes, but are depreciated separately from producing assets that serve other reserves.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

3. Significant accounting policies (continued)

(m) Development and production assets (continued)

Impairment of development and production assets

An impairment test is performed whenever events and circumstances arising during both the development and production phase indicate that the carrying value of a development or production asset may exceed its recoverable amount.

The carrying value is compared against the expected recoverable amount of the asset, generally by reference to the present value of the future cash flows expected to be derived from production of commercial reserves. The cash-generating unit applied for impairment test purpose is generally the field, except that a number of the field interests may be grouped as a single cash generating unit where the cash flow of each field is interdependent.

(n) Inventories

Inventories are stated at the lower of cost and net realisable value. Costs comprise direct materials and, where applicable, direct labour costs and those overheads that have been incurred in bringing the inventories to their present location and condition. Cost is calculated using the weighted average method. Net realisable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution.

(o) Financial instruments

Recognition of financial assets and financial liabilities

Financial assets and financial liabilities are recognised on the Group's balance sheet when the Group becomes a party to the contractual provisions of the instrument.

Derecognition of financial assets and financial liabilities

The Group derecognises a financial asset only when the contractual rights to cash flows from the asset expire; or it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. If the Group neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Group recognises its retained interest in the asset and an associated liability for the amount it may have to pay. If the Group retains substantially all the risks and rewards of ownership of a transferred financial asset, the Group continues to recognise the financial asset and also recognises a collateralised borrowing for the proceeds received.

The Group derecognises financial liabilities when the Group's obligations are discharged, cancelled or expired.

Trade receivables

Trade receivables are measured at initial recognition at fair value, and are subsequently measured at amortised cost using the effective interest rate method. Appropriate allowances for estimated irrecoverable amounts are recognised in profit or loss when there is objective evidence that the asset is impaired. The allowance recognised is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the effective interest rate computed at initial recognition.

Cash and cash equivalents

Cash and cash equivalents comprise cash on hand and demand deposits, and other short-term highly liquid investments that are readily convertible to a known amount of cash with three months or less remaining to maturity and are subject to an insignificant risk of changes in value.

Trade payables

Trade payables are initially measured at fair value, and are subsequently measured at amortised cost, using the effective interest rate method.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

3. Significant accounting policies (continued)

(o) Financial instruments (continued)

Financial liabilities and equity instruments

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidences a residual interest in the assets of the group after deducting all of its liabilities. Equity instruments issued by the Group are recorded at the proceeds received, net of direct issue costs.

Bank borrowings

Interest-bearing bank loans and overdrafts are recorded at the proceeds received, net of direct issue costs.

Financial liabilities classified at fair value through profit and loss (FVTPL)

Financial liabilities are classified as at FVTPL where the financial liability is designated as at FVTPL. Financial liabilities at FVTPL are stated at fair value, with any resultant gain or loss recognised in profit or loss. The net gain or loss recognised in profit or loss incorporates any interest paid on the financial liability. Fair value is determined in the manner described in note 22.

(p) Provisions

Provisions are recognised when the Group has a present obligation as a result of a past event, and it is probable that the Group will be required to settle that obligation. Provisions are measured at the directors' best estimate of the present value of the expenditure required to settle the obligation at the balance sheet date and are discounted to present value where the effect is material.

(q) Decommissioning

Provision for decommissioning is recognised in full when the related facilities are installed. The decommissioning provision is calculated as the net present value of the Group's share of the expenditure expected to be incurred at the end of the producing life of each field in the removal and decommissioning of the production, storage and transportation facilities currently in place. The cost of recognising the decommissioning provision is included as part of the cost of the relevant asset and is thus charged to the income statement on a unit of production basis in accordance with the Group's policy for depletion and depreciation of tangible non-current assets. Period charges for changes in the net present value of the decommissioning provision arising from discounting are included in finance costs.

(r) Leases

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

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

(s) Share-based payments

The Group issues equity-settled share-based payments to certain parties in return for services or goods. The goods or services received and the corresponding increase in equity are measured directly at the fair value of the goods or services received. The fair value of the services or goods received is recognised as an expense except in so far as they relate to the cost of issuing or acquiring its own equity instruments. The costs of an equity transaction are accounted for as a deduction from equity to the extent they are incremental costs directly attributable to the equity transaction that would otherwise have been avoided.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

3. Significant accounting policies (continued)

(s) Share-based payments (continued)

The Group also issues equity-settled share-based payments to certain directors. Equity settled share-based payments are measured at fair value (excluding the effect of non market-based vesting conditions) at the date of grant. The fair value determined at the grant date for each tranche of the equity-settled share-based payments is expensed on a straight-line basis over the vesting period, based on the Group's estimate of shares that will eventually vest and adjusted for the effect of non market-based vesting conditions.

For those equity settled share-based payments with market-based performance conditions fair value is measured by use of the Stochastic model. For those which are not subject to any market based performance conditions fair value is measured by use of the Black-Scholes model. The expected life used in the models has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions, and behavioural considerations.

4. Critical accounting judgements and key sources of estimation uncertainty

In the application of the Group's accounting policies, which are described in note 3, the Directors are required to make judgements, estimates and assumptions about the carrying amounts of the assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both the current and future periods.

The following are the critical judgements and estimations that the Directors have made in the process of applying the Group's accounting policies and that have the most significant effect on the amounts recognised in the financial statements.

(a) Going concern

The Group is currently dependent upon the financial support received from its investors and other related parties until its revenues from primary business activities are sufficient to satisfy its obligations and fully finance its exploration and development programme for at least the next twelve months. In addition to the capital resources available at the date of the financial statements and income generated from future operations, additional funding will need to be raised which represents a material uncertainty over the Group's ability to continue as a going concern. The Group's management believe that sufficient additional funding expected to be raised from the proposed initial public offering on the London Stock Exchange expected to be completed in H1 2008 enable the Group to meet its obligations for the foreseeable future and continue as a going concern.

(b) Group reorganisation

The acquisition of Cadogan Petroleum Holdings Ltd and its subsidiary entities by the Company in 2006 has been accounted for on the basis that the transaction is a reorganisation of entities under common control. The shareholders remain the same and there has been no change in control. There is no change in the reporting group's substance and so the transaction does not meet the definition of a business combination as defined in IFRS 3 *Business Combinations*. Refer to Note 18 'Subsidiaries' for further details.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

4. Critical accounting judgements and key sources of estimation uncertainty (continued)

(c) Recoverability of exploration and evaluation assets and goodwill

Determining whether an exploration and evaluation asset is impaired requires an assessment of whether there are any indicators of impairment, including by reference to the specific impairment indicators prescribed in IFRS 6 *Exploration for and Evaluation of Mineral Resources*. If there is any indication of potential impairment, an impairment test is required based on value in use of the asset. The value in use calculation requires the entity to estimate the future cash flows expected to arise from the cash-generating unit and a suitable discount rate in order to calculate present value. The carrying amount of exploration and evaluation assets at the balance sheet date was £28,687,262 (2006: £5,771,074) and no impairment was identified or recognised in any of the years reported. A similar assessment is required in connection with the annual impairment test for goodwill.

(d) Acquisition of Radley Investments Limited

The acquisition of Radley Investments Limited together with its subsidiaries has not been treated as a business combination as defined in IFRS 3 *Business Combinations* as it was judged by management that this was an acquisition of business assets rather than that of a business as defined in IFRS 3.

(e) Recoverability of value added tax ('VAT')

The Group has significant receivables from the state budget of Ukraine relating to reimbursement of VAT arising on purchases of goods and services from external service and product providers. Management anticipates no significant cash settlements of receivables from the state budget. Consequently, the Group recognises recoverable VAT only to the extent that it is probable that VAT payable arising on the sales of gas production will be sufficient to offset the VAT due from the state within a reasonable period. Estimating the recoverability of VAT requires management to make an estimate of the future revenues in order to calculate amounts and timing of the VAT payable available for offset. The carrying amount of recoverable VAT at 31 December 2007 is shown in note 20.

(f) Fair values of exploration and evaluation assets acquired

The acquisition of subsidiaries is accounted for using the purchase method, which requires assets and liabilities acquired, including exploration and evaluation assets, to be included at their fair value. The actual value that will be realised, if any, from an exploration and evaluation asset is inherently uncertain and reflects a wide range of factors (including, but not limited to, geological and geophysical factors, future costs and commodity prices, the duration of the licence and its terms and the availability of the financial and other resources needed to progress exploration and development activities). The carrying amount of exploration and evaluation assets acquired is shown in note 26.

(g) Decommissioning

The Group recognises a provision for asset retirement obligation for expected decommissioning and site restoration costs expected to incur in approximately 14 to 19 years. At 31 December 2007, a provision has been made for costs of £374,291 (2006: £141,124) which are expected to be incurred within the next year due to the demobilisation of drilling equipment and respective site restoration. A further provision of £398,703 has been made for long term costs (2006: £383,239). The provision is estimated taking into consideration existing technology and current prices of site restoration after adjusting for expected future inflation as discounted using rates reflecting current market assessments of the time value of money and, where appropriate, the risks specific to the liability. The Group makes an estimate based on its experience and historical data (see note 23).

(h) Reserves

Commercial reserves are proven and probable oil and gas reserves, which are defined as the estimated quantities of crude oil, natural gas and natural gas liquids which geological, geophysical and engineering data demonstrate with a specified degree of certainty to be recoverable in future years from known reservoirs and which are considered commercially producible. There should be a 50 per cent statistical probability that the actual quantity of recoverable reserves will be more than the amount estimated as a proven and probable reserves and a 50 per cent statistical probability that it will be less.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

4. Critical accounting judgements and key sources of estimation uncertainty (continued)

(h) Reserves (continued)

Commercial reserves used in the calculation of depreciation and for impairment purposes test purposes are determined using estimates of oil and gas in place, recovery factors and future oil and gas prices. Management base their estimate of oil and gas reserves and resources upon competent persons reports (CPR) provided by independent advisors.

(i) Impairment of goodwill

Determining whether goodwill is impaired requires an estimation of the value in use of the cash-generating units to which goodwill has been allocated. The value in use calculation requires the entity to estimate the future cash flows expected to arise from the cash generating unit and a suitable discount rate in order to calculate present value. The carrying amount of goodwill at 31 December 2007 is shown in note 14.

(j) Share-based payments

The Group has an equity-settled share option scheme available to certain Directors. In accordance with IFRS 2 *Share-based payment*, in determining the fair value of options granted, the Group has applied the Black-Scholes and Stochastic models. As a result, the Group makes assumptions for expected volatility, expected life, risk free rate and expected dividend yield. The fair value of options granted at 31 December 2007 is shown in note 25.

5. Revenue

An analysis of the Group's revenue is as follows:

	2007 £	2006 £
Sale of hydrocarbon products	665,627	-
Investment revenue (note 10)	277,984	88,085
	<u>943,611</u>	<u>88,085</u>

6. Business and geographical segments

The Directors consider there to be only one business segment, the exploration and development of oil and gas revenues. The Directors consider there only to be one geographical segment, being Ukraine.

7. Other operating expenses

	2007 £	2006 £
Professional consultancy	1,071,284	1,224,996
Write-off of pre-licence expenditure	1,855,058	-
	<u>2,926,342</u>	<u>1,224,996</u>

Included within professional consultancy expenses above, £439,034 (2006: £285,145) relates to amounts paid to Executive Directors for services rendered.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

8. Loss for the year

The loss for the year has been arrived at after charging / (crediting):

	2007 £	2006 £
Depreciation of property, plant and equipment	598,118	66,747
Amortisation of other intangible assets	1,728	-
Loss / (gain) on disposal of property, plant and equipment	7,496	(714)
Staff costs (see note 9)	6,216,926	808,797
Net foreign exchange losses	538,973	487,136
	<u>538,973</u>	<u>487,136</u>

The analysis of the auditor's remuneration is as follows:

Fees payable to the Company's auditors for the audit of the Company's annual accounts	127,000	120,000
Total audit fees	<u>127,000</u>	<u>120,000</u>
Fees payable to the Company's auditors for the review of the Company's interim accounts	48,000	-
Corporate finance services	-	256,249
Tax services	93,200	11,500
Total non-audit fees	<u>141,200</u>	<u>267,749</u>
Total audit and non-audit fees	<u>268,200</u>	<u>387,749</u>

Corporate finance services represent the fee in respect of reporting accountants work performed in the year.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

9. Staff costs

The average monthly number of employees (including Executive Directors) was:

	Group		Company	
	2007 No.	2006 No.	2007 No.	2006 No.
Executive Directors	3	3	3	3
Other employees	285	60	-	-
	<u>288</u>	<u>63</u>	<u>3</u>	<u>3</u>
	£	£	£	£
Their aggregate remuneration comprised:				
Wages and salaries	1,592,452	690,845	-	-
Social security costs	379,179	14,327	-	-
Other pension costs	1,408	8,225	-	-
Other	-	95,400	-	-
Share-based payments (note 25)	4,243,887	-	4,243,887	-
	<u>6,216,926</u>	<u>808,797</u>	<u>4,243,887</u>	<u>-</u>

Other pension costs consist of payments to a former Director's personal pension plan.

Other staff costs relate to payments made to a former Director of the Group under a termination compromise agreement.

Within wages and salaries, £119,967 (2006: £1,003) relates to amounts paid to Executive Directors for services rendered. Refer to related party disclosure (note 29) for key management remuneration disclosure.

The Company did not have any employees in the period (2006: nil).

10. Investment revenue

	2007 £	2006 £
Interest on bank deposits	<u>277,984</u>	<u>88,085</u>

No additional investment revenue earned from loan and receivables (including cash and bank balances) have been recognised other than interest on bank deposits (above).

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

11. Finance costs

	2007 £	2006 £
Interest on shareholder loans	-	9,192
Unwinding of discount on decommissioning provision	28,154	9,375
	<u>28,154</u>	<u>18,567</u>

The transaction costs of equity transactions are accounted for as a deduction from equity to the extent that they are incremental costs directly attributable to the equity transaction that would otherwise have been avoided.

No additional gains or losses have been recognised on financial liabilities measured at amortised cost.

12. Tax - foreign

	2007 £	2006 £
Current tax	9,265	-
Deferred tax (note 21)	212,298	11,423
	<u>221,563</u>	<u>11,423</u>

The Group's operations are conducted primarily outside the UK. The most appropriate tax rate for the Group is therefore considered to be 25% (2006: 25%) the rate of profit tax in Ukraine which is the primary source of revenue for the Group. Taxation for other jurisdictions is calculated at the rates prevailing in the respective jurisdictions. The charge for the year can be reconciled to the loss per the income statement as follows:

	Group			
	2007 £	%	2006 £	%
Loss before tax				
Continuing operations	<u>(14,977,658)</u>	<u>100</u>	<u>(5,171,975)</u>	<u>100</u>
Tax at the Ukraine corporation tax rate of 25%	(3,744,415)	25	(1,292,994)	25
Tax effect of expenses that are not deductible in determining taxable profit	2,394,189	(16)	624,578	(12)
Tax effect of deferred tax assets not recognised	1,571,789	(10)	679,839	(13)
Tax expense and effective tax rate for the year	<u>221,563</u>	<u>(1)</u>	<u>11,423</u>	<u>-</u>

Cadogan Petroleum plc

Notes to the financial statements (continued)

Year ended 31 December 2007

13. Loss per ordinary share

Basic loss per ordinary share amounts are calculated by dividing the net loss for the year attributable to ordinary equity holders of the parent by the weighted average number of ordinary shares outstanding during the year. For the year ended 31 December 2006 the shares issued by Cadogan Petroleum Holdings Ltd have been multiplied by the share exchange ration of 725:1.

Diluted loss per ordinary share equals basic loss per ordinary share as, due to the losses incurred in 2007 and 2006, there is no dilutive effect from the subsisting share warrants, share options, shares to be issued and financial liabilities (see note 22).

The calculation of the basic and diluted loss per share is based on the following data:

Losses

	2007 £	2006 £
Loss for the purposes of basic loss per share being net loss attributable to equity holders of the parent	(15,197,276)	(5,183,398)

Number of shares

	No.	No.
Weighted average number of ordinary shares for the purposes of basic loss per share	318,493,850	185,019,747

14. Goodwill

At 1 January 2006 and 2007	£ -
Recognised on acquisition of subsidiaries (note 26)	2,837,579
Exchange differences	(33,380)
At 31 December 2007	<u>2,804,199</u>

Goodwill acquired in a business combination is allocated, at acquisition, to the cash generating units ('CGUs') that are expected to benefit from that business combination.

The recoverable amounts of CGUs are determined from value in use calculations. The value in use calculations are based upon the competent persons report (CPR) provided by independent advisors. The key assumptions used in the report are as follows:

- the Group's proved and proved plus probable reserve categories;
- discount rate of 12.5% (post tax rate which approximates the Group's adjusted tax-free rate of 15%);
- inclusion of relevant elements of Ukraine fiscal regime for petroleum operators (such as production and royalty tax relevant to each license and corporate income tax of 25%);
- expected future selling prices (based on current and anticipated market conditions for oil, condensate and gas); and
- costs escalated 2.5% annually (based on US\$ costs).

These assumptions reflect management's best estimates, and reflect current market assessments of the time value of money and the risks specific to the CGUs.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

14. Goodwill (continued)

The fair value of goodwill has been allocated to all Ukraine assets as Management believes that the anticipated future operating synergies gained on business acquisition can be used across the Group's entire asset base in Ukraine.

The Group tests goodwill annually for impairment or more frequently if there are indications that goodwill might be impaired.

At 31 December 2007, no impairment of goodwill has been recognised.

15. Intangible exploration and evaluation assets

	£
At 1 January 2006	1,374,348
Additions on acquisition of subsidiaries (note 26)	1,106,113
Additions	3,472,099
Exchange differences	(181,486)
	<hr/>
At 1 January 2007	5,771,074
Additions on acquisition of subsidiaries (note 26)	14,752,015
Additions	18,045,341
Transfer from other intangible assets (note 16)	13,926
Increase in estimate of decommissioning assets	91,811
Transfer to property, plant and equipment	(10,313,176)
Exchange differences	326,271
	<hr/>
At 31 December 2007	<u>28,687,262</u>

Total intangible exploration and evaluation assets at 31 December 2007 include £722,754 (2006: £517,797) in respect of decommissioning assets. Additions during the year includes £551,525 (2006: £165,993) of capitalised depreciation of Development and production assets used in exploration and evaluation activities.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

16. Other intangible assets

Cost	£
At 1 January 2006	-
Additions	24,666
	<hr/>
At 1 January 2007	24,666
Additions	8,924
Transfer to intangible exploration and evaluation assets	(13,926)
Transfer to property, plant and equipment	(4,480)
Exchange differences	(904)
	<hr/>
At 31 December 2007	14,280
	<hr/> <hr/>
Accumulated amortisation	
At 1 January 2006 and 2007	-
Charge for the year	1,728
Exchange differences	15
	<hr/>
At 31 December 2007	1,743
	<hr/> <hr/>
Carrying amount	
At 31 December 2007	12,537
	<hr/> <hr/>
At 31 December 2006	24,666
	<hr/> <hr/>

Other intangible assets principally comprise software licenses. The amortisation charge is presented as part of administration expense.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

17. Property, plant and equipment

	Other £	Development and production assets £	Total £
Cost			
At 1 January 2006	35,561	-	35,561
Additions on acquisition of subsidiaries (note 26)	4,589	36,919	41,508
Additions	617,394	4,510,514	5,127,908
Disposals	(19,182)	-	(19,182)
Exchange differences	(2,772)	(1,133)	(3,905)
At 1 January 2007	635,590	4,546,300	5,181,890
Additions on acquisition of subsidiaries (note 26)	901,792	3,729,164	4,630,956
Additions	438,547	4,162,284	4,600,831
Transfer from intangible exploration and evaluation assets and other intangible assets	4,480	10,313,176	10,317,656
Disposals	(148,092)	(132,067)	(280,159)
Exchange differences	(31,118)	(266,451)	(297,569)
At 31 December 2007	1,801,199	22,352,406	24,153,605
Accumulated depreciation			
At 1 January 2006	16,874	-	16,874
Additions on acquisition of subsidiaries (note 26)	4,172	-	4,172
Charge for the year	37,221	195,519	232,740
Disposals	(6,142)	-	(6,142)
Exchange differences	(3,468)	(1,827)	(5,295)
At 1 January 2007	48,657	193,692	242,349
Additions on acquisition of subsidiaries (note 26)	60	39,205	39,265
Charge for the year	178,581	971,062	1,149,643
Disposals	(10,619)	(1,255)	(11,874)
Exchange differences	(180)	1,423	1,243
At 31 December 2007	216,499	1,204,127	1,420,626
Carrying amount			
At 31 December 2007	1,584,700	21,148,279	22,732,979
At 31 December 2006	586,933	4,352,608	4,939,541

As at 31 December 2007, development and production assets totalling £10,313,176 (2006: £nil) were not depleted or depreciated pending commercial production.

Cadogan Petroleum plc

Notes to the financial statements (continued)

Year ended 31 December 2007

18. Subsidiaries

The Company had investments in the following subsidiary undertakings as at 31 December 2007, which principally affected the losses and net assets of the Group.

Name	Country of incorporation (or registration) and operation	Proportion of voting interest %	Activity
<i>Directly held</i>			
Cadogan Petroleum Holdings Ltd	Great Britain	100	Holding company
Ramet Holdings Ltd	Cyprus	100	Holding company
<i>Indirectly held</i>			
Colby Petroleum Ltd	British Virgin Islands	100	Holding company
Rentoul Ltd	Isle of Man	100	Holding company
LLC Industrial Company Gazvydobuvannya	Ukraine	100	Exploration
LLC AstroInvest -Ukraine	Ukraine	100	Exploration
LLC Astro Gas	Ukraine	90	Exploration
Tigar Oil & Gas Ltd	British Virgin Islands	100	Holding company
Tigar Oil SA	Panama	100	Inactive Exploration
Anglo Georgian Petroleum Ltd	British Virgin Islands	100	Holding company
LLC Anglo Georgian Petroleum	Georgia	100	Inactive Exploration
Stickle Ltd	Isle of Man	100	Holding company
Rochefort Ventures Ltd	Cyprus	100	Inactive exploration
USENCO International Inc.	USA	100	Holding company
USENCO Ukraine	Ukraine	100	Exploration
LLC USENCO Nadra	Ukraine	90	Exploration
Momentum Energy International Inc	Canada	100	Holding company
Momentum Enterprise Inc	Canada	100	Holding company
Momentum Enterprise (Europe) Ltd	Cyprus	100	Holding company
LLC JV Delta	Ukraine	100	Exploration
Radley Investments Ltd	Great Britain	100	Holding company
LLC Astro-Energy	Ukraine	100	Exploration
LLC Astroinvest-Energy	Ukraine	90	Exploration
OJSC 'AgroNaftoGasTechService	Ukraine	79.9	Construction services

Cadogan Petroleum plc was incorporated on 22 February 2006 with an authorised share capital of 600,000,000 ordinary shares of £0.01 each. On 21 April 2006, the Company acquired the whole of the share capital of Cadogan Petroleum Holdings Limited in a share for share exchange transaction where each share in Cadogan Petroleum Holdings Limited was exchanged for 725 ordinary shares in Cadogan Petroleum plc. The number of shares in issue at 21 April 2006 was 220,416 (nominal value £22,042), which resulted in the issue of 159,801,600 shares in Cadogan Petroleum plc.

As detailed in note 26, the Group acquired Momentum Energy International Inc, Radley Investment Limited and Ramet Holdings Limited together with all associated subsidiaries during the year ended 31 December 2007.

The investments in subsidiaries are all stated at cost on the Company's balance sheet.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

19. Inventories

	2007 £	2006 £
Material and supplies	1,654,464	835,552

20. Other financial assets

Other non-current receivables

	2007 £	2006 £
VAT recoverable	3,059,654	-

Trade and other receivables

	Group		Company	
	2007 £	2006 £	2007 £	2006 £
Other receivables	310,338	1,468,426	52,000	31,929
VAT recoverable	526,283	1,504,552	12,251	13,340
Prepayments	849,856	900,923	-	-
	<u>1,686,477</u>	<u>3,873,901</u>	<u>64,251</u>	<u>45,269</u>

The Group's principal financial assets are bank balances and cash and other receivables none of which are past due. The Directors consider that the carrying amount of other receivables approximates their fair value.

Included in other receivables there is no unpaid share capital (2006: £50).

VAT balances recoverable from Ukraine authorities will only be recoverable once significant production commences. The Directors consider amounts in the balance sheet to be fully recoverable. An allowance for impairment is made where there is an identified event which, based on previous experience, is evidence of a reduction in the recoverability of the cash flows. No such events occurred in 2007 and 2006. VAT will be recovered by netting off the VAT liabilities arising from future revenues and therefore have been adjusted for the time value of money. As a result, a charge of £856,987 was in 2007 (2006: £165,199). The portion that is not expected to be recovered within the next twelve months has been presented as non-current.

Cash and cash equivalents

Cash and cash equivalents comprise cash held by the Group and the Company. The Directors consider that the carrying amount of these assets approximates their fair value.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

21. Deferred tax

The following are the major deferred tax liabilities recognised by the Group and movements thereon during the current and prior period.

	Accelerated tax depreciation and other temporary differences £
At 1 January 2006	296,928
Charge to income	11,423
Exchange differences	(32,484)
	<hr/>
At 1 January 2007	275,867
Acquisition of subsidiaries	497,422
Charge to income	212,298
Exchange differences	(18,218)
	<hr/>
At 31 December 2007	<u>967,369</u>

At 31 December 2007, the Group had unused tax losses of £10.1 million (2006: £4.2 million) available for offset against future taxable profits. Tax losses have not been recognised as deferred tax assets due to the uncertainty that profits will be available in future periods against which they can be utilised.

Of the Group's total unused tax losses, £5.2 million (2006: £2.6 million) relate to losses incurred in the UK. These tax losses are available to shelter future non-trading profits arising within Cadogan Petroleum Holdings Ltd and Cadogan Petroleum plc, subject to restrictions which may apply if there is a change of ownership. These losses are not subject to a time restriction on expiry.

Total unused tax losses of £1.3 million (2006: £nil) relate to losses incurred by USENCO International Inc in the USA. Net operating losses ('NOL') can be carried forward and utilised to offset taxable income arising in the succeeding 20 years. However, if there is a change in ownership the losses would be subject to an annual limitation, being broadly the NOL, at the date of change in ownership, multiplied by the federal interest rate at that time.

Unused tax losses incurred by Ukraine subsidiaries, amount to £3.6 million (2006: £1.6 million). Under general provisions, these losses may be carried forward indefinitely to be offset against any type of taxable income arising from the same company of origination. Tax losses may not be surrendered from one Ukraine subsidiary to another. Under Ukraine tax law, losses can be carried forward indefinitely. However, in the last few years, Ukrainian legislation has been established imposing restrictions regarding the carry forward of tax losses. Should similar restrictions be introduced in future periods and before the Ukraine companies become profitable, the accumulated tax losses at 31 December 2007 may not be used.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

22. Other financial liabilities

Trade and other payables

	Group		Company	
	2007 £	2006 £	2007 £	2006 £
Trade creditors	1,493,679	2,018,298	-	-
Other taxes and social security	99,090	9,485	-	-
Other creditors and payables	596,236	103,722	149,142	-
Accruals	866,124	317,494	175,000	120,000
	<u>3,055,129</u>	<u>2,448,999</u>	<u>324,142</u>	<u>120,000</u>

Trade creditors and accruals principally comprise amounts outstanding for trade purchases and ongoing costs. The Group has financial risk management policies to ensure that all payables are paid within the credit timeframe.

The Directors consider that the carrying amount of trade and other payables approximates to their fair value. No interest is charged on balances outstanding.

Financial liability

	Group		Company	
	2007 £	2006 £	2007 £	2006 £
Financial liability	<u>1,583,333</u>	<u>-</u>	<u>1,583,333</u>	<u>-</u>

In December 2007, 8,333,333 ordinary shares of £0.01 each were issued for a consideration of £0.60 per share raising a total cash consideration of £5,000,000. As a condition of this placing, it was agreed that in the event that the Company did not complete any additional placings at the increased price per share of £0.60 prior to 15 March 2008, the weighted average price per share for this tranche of shares would revert back to £0.41. Additional shares would then fall due to be issued with no additional cash consideration being due.

As the number of shares issued in the second tranche is dependent on a future placing, the value of the shares has been determined at the fair market value at 31 December 2007 of £0.41 per share, this being the price at which the Company's shares were being issued in private equity fundraising, with the difference between this and the cash received recorded as a financial liability.

Refer to note 31 for a discussion of events that occurred after the balance sheet date.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

23. Provisions

	Decommissioning £	Other £	Total £
At 1 January 2006	26,161	-	26,161
Additions on acquisitions of subsidiaries (note 26)	491,636	29,114	520,750
Unwinding of discount on decommissioning provision	9,375	-	9,375
Exchange differences	(2,809)	-	(2,809)
	<hr/>	<hr/>	<hr/>
At 1 January 2007	524,363	29,114	553,477
Additions on acquisition of subsidiaries (note 26)	113,146	19,943	133,089
Additions	225,069	-	225,069
Change in estimate	(133,258)	-	(133,258)
Utilisation of provision	-	(11,332)	(67,398)
Unwinding of the discount on decommissioning provision	28,154	-	28,154
Exchange differences	(22,205)	-	(22,205)
	<hr/>	<hr/>	<hr/>
At 31 December 2007	735,269	37,725	772,994
			<hr/>
Included in current provisions			374,291
Included in long-term provisions			398,703
			<hr/>
			772,994
			<hr/>

In accordance with the Group's environmental policy and applicable legal requirements, the Group intends to restore the site of geological exploration upon the completion of the exploration phase. A short-term provision of £374,291 (2006: £141,124) has been made for decommissioning costs, which are expected to be incurred within the next year as a result of the demobilisation of drilling equipment and respective site restoration.

The long-term provision recognised in respect of decommissioning reflects management's estimate of the net present value of the Group's share of the expenditure expected to be incurred in this respect with regard to expected expenditure on similar site restorations. This amount has been recognised as a provision at its net present value, using a discount rate that reflected the market assessment of time value of money at that date, and the unwinding of the discount on the provision has been charged to the income statement. Key assumptions underlying the calculation are a pre-tax, risk free discount rate, estimated to be 15% and inflation estimated to be 12%. These expenditures are expected to be incurred at the end of the producing life of each field in the removal and decommissioning of the facilities currently in place (currently estimated to be between 14 and 19 years).

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

24. Share capital

	Group		Company	
	2007 £	2006 £	2007 £	2006 £
Authorised:				
600,000,000 ordinary shares of £0.01 each (2006: 600,000,000)	6,000,000	6,000,000	6,000,000	6,000,000
Issued and partly paid:				
416,940,862 ordinary shares of £0.01 each (2006: 257,078,867)	4,169,409	2,570,789	4,169,409	2,570,789

At 31 December 2007, no ordinary shares of £0.01 each remained unpaid (2006: 242).

Cadogan Petroleum Holdings Ltd issued shares for cash at various prices as follows:

	Number Issued
At 1 January 2006	205,391
Share issues	15,025
At 21 April 2006	220,416

Cadogan Petroleum plc was incorporated on 22 February 2006 with an authorised share capital of 600,000,000 ordinary shares of £0.01 each. On 21 April 2006, the Company acquired the whole of the share capital of Cadogan Petroleum Holdings Limited in a share for share exchange transaction where each share in Cadogan Petroleum Holdings Limited was exchanged for 725 ordinary shares in Cadogan Petroleum plc. The number of shares in issue at 21 April 2006 was 220,416 (nominal value £22,042), which resulted in the issue of 159,801,600 shares in Cadogan Petroleum plc.

The Company issued further shares for cash at various prices as follows:

	Number Issued
At 22 February 2006	-
Share exchange	159,801,600
Share issues	97,277,267
At 1 January 2007	257,078,867
Share issues	157,121,995
On acquisition of subsidiary (note 26)	2,740,000
At 31 December 2007	416,940,862

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

24. Share capital (continued)

In December 2007, 8,333,333 ordinary shares of £0.01 each were issued for a consideration of £0.60 per share raising a total cash consideration of £5,000,000. As a condition of this placing, it was agreed that in the event that the Company did not complete any additional placings at the increased price per share of £0.60 prior to 15 March 2008, the weighted average price per share for this tranche of shares would revert back to £0.41. Additional shares would then fall due to be issued with no additional cash consideration being due.

As the number of shares issued in the second tranche is dependent on future placing, the value of the shares has been determined at the fair market value of £0.41 per share, this being the price at which the Company's shares were being issued in private equity fundraising.

Refer to note 22 for discussion of financial liability and note 31 for a discussion of events that occurred after the balance sheet date.

At 31 December 2007, a placing agreement was in place for the issue of 2,440,731 shares of £0.41 each, where cash had been received, but the shares were not yet issued. The total consideration received amounted to £1,000,700. As the shares were not in issue at year end, the value has been presented as shares to be issued. Refer to note 31 for a discussion of events that occurred after the balance sheet date.

25. Share-based payments

Under the terms of an agreement dated 17 February 2006, which was subsequently updated on 20 September 2006 and 8 May 2007, the Company's broker and financial adviser Fox-Davies Capital ('Fox Davies') were granted certain warrant rights. Under the terms of this agreement as amended on 8 May 2007, Fox-Davies became entitled, on completion of any share placing to be granted warrants to subscribe for 4.5% (which was changed from 5% at 17 February 2006 and subsequently to 6% at 20 September 2006) of the total number of shares allotted by the Company on funds raised by Fox-Davies, such warrants to be exercisable at a price per share equal to the placing price (average price of £0.273 and £0.41) and to be exercisable at any time within the five-year period following completion of the placing.

At 31 December 2007, 13,170,933 (2006: 5,147,883) warrants had accrued to Fox-Davies and these were deemed to hold a value equivalent to one half of one percent cash commission on gross funds raised. This valuation has been made with reference to the additional commission which would have been due to Fox-Davies had the warrants not been granted. The monetary value of the warrants was calculated as £430,606 (2006: £129,434).

In accordance with the Group's accounting policy, the costs of an equity transaction are accounted for as a deduction from equity to the extent they are incremental costs directly attributable to the equity transaction that would otherwise have been avoided. The effect on the income statement during the year is, therefore, nil.

Equity-settled share option scheme

The Company has a share option scheme for certain Directors of the Group. Options are exercisable at a price of £0.273 and vest on achieving certain performance criteria. If the options remain unexercised after a period of five years from the date of grant, the options expire. Options are forfeited if the Director leaves the Group before the options vest. The options are split into the following tranches and each tranche is subject to the following performance conditions:

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

25. Share-based payments (continued)

Option tranche 1

Of the total options granted, 40% vest on the grant date.

Option tranche 2

- 20% of the options granted will vest and become exercisable when the Group has sales over a continuous period of 90 days of at least 5,000 barrels of oil equivalent per day.
- 20% of the options granted will vest and become exercisable when the Group has sales over a continuous period of 90 days of at least 10,000 barrels of oil equivalent per day.

Barrels of oil equivalent means the aggregate of

- barrels of oil; and
- barrels of condensate; and
- gas converted to equivalent barrels on the basis of 6,000 standard cubic feet per barrel at a standard temperature and pressure.

Sales shall not include sales to any subsidiary or sales which are not on an arm's length basis.

Option tranche 3

Of the total options granted 20% vest upon the earlier of:

- Admission, being the date in which the shares are first admitted on any stock exchange, at an initial price per share of £1.092 and, maintaining a daily average price per share of at least £1.092 for any period of 45 consecutive days after admission; and
- a trade sale at a price per share of at least £1.092.

Details of the share options outstanding during the year were as follows.

	No. Tranche 1	No. Tranche 2	No. Tranche 3
Outstanding at 1 January 2006 and 2007	-	-	-
Granted during the year	17,138,315	17,138,315	8,569,158
Outstanding at 31 December 2007	<u>17,138,315</u>	<u>17,138,315</u>	<u>8,569,158</u>
Exercisable at 31 December 2007	<u>17,138,315</u>	<u>-</u>	<u>-</u>

No share options were forfeited, exercised or expired during the year (2006: nil).

The options outstanding at 31 December 2007 had a weighted average exercise price of £0.273, and a weighted average remaining contractual life of 57 months. Options were granted on 11 September 2007.

The fair values of the options have been calculated using the following models:

- Option tranche 1 and 2 – not subject to any market-based performance conditions and therefore the Black- Scholes model has been used.
- Option tranche 3 – market-based performance conditions must be included in the calculation of fair value and therefore the Stochastic model has been considered the most appropriate.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

25. Share-based payments (continued)

The inputs into the models were as follows:

	Black- Scholes	Stochastic
Weighted average share price	41p	41p
Weighted average exercise price	27.3p	27.3p
Expected volatility	55%	55%
Expected term	2.5 years	5 years
Risk free rate	4.99%	4.98%
Expected dividend yield	0%	0%

As the Company is unlisted, expected volatility was determined by considering the historical volatility of other similar entities. Similar entities have been chosen as the FTSE AIM Oil & Exploration constituents (with a market capitalisation of greater than £100m). Volatility for each of these companies has been calculated over both 5 years and 2.5 years resulting in median volatility for the Group of 56% and 55%. These numbers have been rounded to 55% respectively and taken as a proxy for the Company's volatility in valuing the options. The aggregate of the estimated fair values of the options granted on that date is £8,966,938 (option tranche 1: £3,634,180; option tranche 2: £3,634,180; option tranche 3: £1,698,578).

The Group recognised total expenses of £4,243,887 related to equity-settled share based payment transactions in 2007 (2006: £nil). Of this expense, £3,634,180 relates to tranche 1 and £609,707 relates to option tranche 2. No expense has been recognised for option tranche 3 as this is considered to be a discrete event and therefore it will be recognised when the conditions are met.

For option tranche 1 and 2, an expected term of two and a half years has been assumed, being half way between the grant date and the lapse date. For option tranche 3, an expected term of five years was derived from the Stochastic valuation model being the expected term of the market-based performance condition.

The exercise price was established in accordance with the terms included within the share option scheme.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

26. Acquisition of subsidiaries

Momentum Energy International Inc.

On 24 May 2007, the Company completed the acquisition of 100% of the issued share capital of Momentum Energy International Inc. ('Momentum') for cash consideration of US\$7.3 million via its wholly-owned subsidiary Cadogan Petroleum Holdings Limited. Momentum, through its subsidiaries, holds interests in several oil and gas fields in western Ukraine.

The transaction has been accounted for as a business combination using an effective date of 24 May 2007, being the date that the Company gained control of Momentum. For reasons of materiality and practicality, the Company has consolidated Momentum's results from 31 May 2007.

	Book value £	Fair value £
Net assets acquired:		
Property, plant and equipment	2,092,206	3,407,610
Inventories	79,974	79,974
Trade and other receivables	197,926	157,004
Cash and cash equivalents	254,001	254,001
Trade and other payables	(561,324)	(747,672)
Non-current provisions	-	(113,243)
Deferred tax	-	(319,657)
	<u>2,062,783</u>	<u>2,718,017</u>
Goodwill		<u>1,071,124</u>
		<u>3,789,141</u>
Satisfied by:		
Cash		3,736,944
Directly attributable costs		52,197
Total consideration		<u>3,789,141</u>
Net cash outflow arising on acquisition		
Cash consideration		3,789,141
Cash and cash equivalents acquired		(254,001)
		<u>3,535,140</u>

In presenting the Group's interim accounts for the period ending 30 June 2007, the fair values of the identifiable assets and liability acquired as part of the Momentum acquisition had been done on a preliminary basis in accordance with IFRS 3 *Business Combinations*, as valuations on certain property, plant and equipment acquired were not then complete. This resulted in a purchase price consideration equal to the aggregate of the identifiable assets and liabilities of Momentum and therefore no goodwill resulted at that time.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

26. Acquisition of subsidiaries (continued)

Momentum Energy International Inc (continued)

Subsequent to receipt of these valuations, it was determined that the purchase price consideration exceeded the aggregate of the identifiable assets and liabilities acquired, resulting in goodwill of £1,071,124.

The goodwill arising on the acquisition of Momentum and its subsidiary undertaking is attributable to future operating synergies from the combination.

Momentum contributed £488,075 to revenue and £204,268 to the Group's loss before tax for the period between the date of acquisition and the balance sheet date.

Ramet Holdings Limited

On 26 December 2007, the Company entered into an agreement to purchase 100% of the issued share capital of Ramet Holdings Limited, a company which was owned by Mark Tolley, an Executive Director of Cadogan Petroleum plc, for consideration consisting of:

- the allotment of 3,048,780 ordinary shares of £0.01 in the Company;
- cash consideration of US\$2.5 million; and
- deferred consideration equal to the number of recoverable proven and probable barrels of oil equivalent from the first two wells drilled and tested in the Malynovestske Field (the Malynovestske license area in the Bogorodchansky Administration District of the Ivano-Frankivska Administration Region in Western Ukraine). For the purpose of ascertaining the quantity of oil equivalent recoverable, the parties should instruct a suitably qualified and insured independent expert of at least 10 years' standing. Payment shall be paid within 30 days of the expert's report and, notwithstanding that report, shall not exceed US\$5 million. No consideration for this has been included in the purchase consideration as these costs were not considered probable at the date of acquisition.

It was subsequently agreed that the cash consideration of US\$2.5m would be settled by the issue of 2,763,194 ordinary shares of £0.01 in the Company and a cash payment of £149,142. The fair value of the shares was deemed to be £0.41 this being the price at which the Company's shares were being issued in private equity fundraising.

Of the total consideration to be settled by the issue of ordinary shares, 2,740,000 had been issued at 31 December 2007 and 3,071,974 were issued in January 2008. The value of the shares issued and to be issued has been determined at the fair market value of £0.41 per share, this being the price at which the Company's shares were being issued in private equity fundraising.

Ramet Holdings Limited is the beneficial owner of 79.9% shares in the Ukrainian company OJSC 'AgroNaftGasTechService' which holds interests in two licences and provides construction services to the oil and gas sector. Prior to being held by Ramet Holdings Limited, the shares in OJSC 'AgroNaftGasTechService' were originally held by Mark Tolley and Vasyl Vivcharyk both of whom are Executive Directors of Cadogan Petroleum plc.

The transaction has been accounted for as a business combination using an effective date of 28 December 2007, being the date that the Company gained control of Ramet Holdings Limited and consolidated at 31 December 2007 for reasons of materiality and practicality.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

26. Acquisition of subsidiaries (continued) Ramet Holdings Limited (continued)

	Book value £	Fair value £
Net assets acquired:		
Property, plant and equipment	491,854	1,184,081
Inventories	80,748	80,748
Trade and other receivables	121,437	121,437
Cash and cash equivalents	20,258	20,258
Trade and other payables	(152,219)	(152,219)
Non-current provisions	(9,148)	(19,846)
Deferred tax	(7,383)	(177,765)
Minority interest	(94,262)	(197,002)
	<u>451,285</u>	<u>859,692</u>
Goodwill		<u>1,766,455</u>
		<u>2,626,147</u>
Satisfied by:		
Cash to be paid		149,142
Directly attributable costs		14,614
Issue of equity instruments – shares issued		1,123,400
Issue of equity instruments – shares to be issued		1,259,510
Forgiven intercompany loans		79,481
Total consideration		<u>2,626,147</u>
Net cash outflow arising on acquisition		
Total consideration		2,626,147
Consideration not yet paid		(149,142)
Cash and cash equivalents acquired		(20,258)
Issue of equity instruments – shares issued		(1,123,400)
Issue of equity instruments – shares to be issued		(1,259,510)
		<u>73,837</u>

The goodwill arising on the acquisition of Ramet Holdings Limited and its subsidiary undertaking is attributable to future operating synergies from the combination.

As the company was acquired on 28 December 2007, it has made no contribution to the Group revenues or losses.

If the acquisition of Momentum and Ramet Holdings Limited, together with their subsidiaries, had been completed on the first day of the financial year, Group revenues for the year would have been £2,160,773 and Group loss attributable to equity holders of the parent would have been £15,256,766.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

26. Acquisition of subsidiaries (continued)

Radley Investments Limited

On 30 November 2007, the Company acquired 100% of the issued share capital of Radley Investments Limited for cash consideration of US\$32.6 million, via its wholly-owned subsidiary Cadogan Petroleum Holdings Limited. The Company has a beneficial interest, through its wholly-owned subsidiary LLC Astro-Energy, of 90% in LLC Astroinvest-Energy which holds together with NAK Nadra Ukraine the Zagoryanske license. The acquisition of Radley Investments Limited has not been treated as a business combination as defined in IFRS 3 *Business Combinations* as it was judged by management that it was an acquisition of business assets rather than that of a business as defined in IFRS 3.

The cost of the transaction was allocated between the assets and the liabilities acquired as follows:

	£
Net assets acquired:	
Intangible exploration and evaluation assets	14,752,015
Trade and other receivables	2
Cash and cash equivalents	1,254,230
Trade and other payables	(4,230)
	<u>16,002,017</u>
Satisfied by:	
Cash	15,913,660
Directly attributable costs	88,357
	<u>16,002,017</u>
Total consideration	<u>16,002,017</u>
Net cash outflow arising on the transaction	
Cash consideration	16,002,017
Cash and cash equivalents acquired	(1,254,230)
	<u>14,747,787</u>

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

27. Notes to the cash flow statement

	Group		Company	
	2007 £	2006 £	2007 £	2006 £
Net loss	(15,199,221)	(5,183,398)	(4,311,223)	(136,183)
Adjustments for:				
Depreciation of property, plant and equipment	598,118	66,747	-	-
Depreciation of other intangible assets	1,728	-	-	-
Loss / (gain) on disposal of property, plant and equipment	7,496	(714)	-	-
Share-based payments	4,243,887	-	4,243,887	-
Investment revenue	(277,984)	(88,085)	(191,375)	(69,505)
Interest on shareholder loans	-	9,192	-	-
Tax – foreign	221,563	11,423	-	-
Minority interest	1,945	-	-	-
Effect of foreign exchange rate changes	(154,829)	341,690	-	-
Operating cash flows before movements in working capital	(10,557,297)	(4,843,145)	(258,711)	(205,688)
Increase in inventories	(658,190)	(833,174)	-	-
Increase in receivables	(603,144)	(3,956,348)	(8,782)	(45,269)
(Decrease) / increase in payables	(458,465)	2,137,562	55,000	120,000
Cash used in operations	(12,277,096)	(7,495,105)	(212,493)	(130,957)
Income taxes paid	(9,265)	(3,318)	-	-
Net cash outflows from continuing operations	(12,286,361)	(7,498,423)	(212,493)	(130,957)

Cash and cash equivalents comprise cash at bank.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

28. Financial instruments

Categories of financial instruments

	Group		Company	
	2007 £	2006 £	2007 £	2006 £
Financial assets				
Cash and cash equivalents	13,956,712	8,688,261	84,629	1,405,388
Other receivables	281,210	1,417,138	41,800	31,929
Amounts due from subsidiaries	-	-	82,298,170	23,378,531
	<u>14,237,922</u>	<u>10,105,399</u>	<u>8,424,599</u>	<u>24,815,848</u>
	2007 £	2006 £	2007 £	2006 £
Financial liabilities				
Trade creditors	(1,493,679)	(2,018,298)	-	-
Other creditors and payables	(596,236)	(103,722)	(149,142)	-
Financial liabilities	(1,583,333)	-	(1,583,333)	-
	<u>(3,673,248)</u>	<u>(2,122,020)</u>	<u>(1,732,475)</u>	<u>-</u>

Fair value of financial liabilities

As discussed in note 22, a financial liability has been recognised in relation to the issuance of ordinary shares during the year as the number of shares issued is dependent on future placing. The fair value has been determined as being the fair market value of the Company's ordinary shares of £0.41 per share as at 31 December 2007.

Capital risk management

The Group manages its capital to ensure that entities in the Group will be able to continue as going concerns (see note 3(a) and 4(a)) while maximising the return to stakeholders. The Group is not subject to externally imposed capital requirements.

The capital structure of the Group consists of cash and cash equivalents and equity attributable to equity holders of the parent, comprising issued capital, reserves and retained earnings as disclosed in the consolidated statement of changes in equity.

Significant accounting policies

Details of the significant accounting policies and methods adopted, including the criteria for recognition, the basis of measurement, the basis on which income and expenses are recognised, in respect of each class of financial asset, financial liability and equity instrument are disclosed in note 3 to the financial statements.

Financial risk management objectives

Management provides services to the business, co-ordinates access to domestic and international financial markets and monitors and manages the financial risks relating to the Group's operations in Ukraine. These risks include market risks, credit risk, liquidity risk and cash flow interest rate risk.

The Group does not enter into or trade financial instruments, including derivative financial instruments, for speculative purposes.

As the Group has no committed borrowings, the Group is not exposed to any risks associated with fluctuations in interest rates. Fluctuations in interest rates on cash balances held are immaterial.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

28. Financial instruments (continued)

Commodity price risk

The commodity price risk related to Ukrainian gas and condensate prices and, to a lesser extent, prices for crude oil are the Group's most significant market risk exposures. World prices for gas and crude oil are characterised by significant fluctuations that are determined by the global balance of supply and demand and worldwide political developments, including actions taken by the Organisation of Petroleum Exporting Countries. These fluctuations may have a significant effect on the Group's revenues and operating profits going forward. The Ukrainian gas price has historically been, and currently remains, at a discount to gas prices prevailing in the European Union. The principal factor in the current Ukrainian gas price is bi-lateral negotiations with Gazprom to establish the price of gas imports from Russia. The price for Ukrainian gas is based on the current price of these gas imports from Russia, which are nonetheless influenced by world prices, and it is expected that the trend of Ukrainian prices becoming more in alignment with prevailing European and world prices will continue. Ukrainian gas prices are also influenced in some degree by local supply and demand. The Group continues to expect that its principal market for gas will be the Ukrainian domestic market.

The Group does not hedge market risk resulting from fluctuations in gas, condensate and oil prices.

Inflation risk

Inflation, in Ukraine and in the international market for oil and gas, may affect the Group's cost for equipment and supplies. The Directors expect that the Group's practices of raising funds in sterling and keeping deposits in sterling accounts until funds are needed and selling its production in the spot market, coupled with the linkage of the currency in Ukraine and to the US dollar, will enable the Group to manage the risk of inflation.

Foreign exchange risk and foreign currency risk management

The Group does not hold large quantities of foreign currency and therefore is not exposed to significant foreign currency risk.

The Group to date has elected not to hedge its exposure to the risk of changes in foreign currency exchange rates.

Credit risk management

Credit risk refers to the risk that a counterparty will default on its contractual obligations resulting in financial loss to the Group. The Group does not have any significant credit risk exposure as the normal terms for sales of gas and condensate to the Group's customers require payment before delivery. In the future, the Group could face issues with customers if curtailments of throughput in the gas transportation system delay deliveries to customers, but the Group has yet to experience such issues and transportation remains the responsibility of the customer once the Group has delivered product to the transportation system.

The Group makes allowances for impairment of receivables where there is an identified event which, based on previous experience, is evidence of a reduction in the recoverability of cash flows.

The credit risk on liquid funds (cash) is considered to be limited because the counterparties are financial institutions with high and good credit ratings assigned by international credit-rating agencies in the UK and Ukraine, respectively.

The carrying amount of financial assets recorded in the financial statements represents the Group's maximum exposure to credit risk.

Liquidity risk management

Ultimate responsibility for liquidity risk management rests with the board of Directors, which has built an appropriate liquidity risk management framework for the management of the Group's short, medium and long-term funding and liquidity management requirements. The Group manages liquidity risk by maintaining adequate cash reserves and by monitoring forecast and actual cash flows. The maturities of financial liabilities have been disclosed in note 22.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

28. Financial instruments (continued)

Sensitivity analysis

Interest rate sensitivity

Management's estimate of a reasonable possible change in interest rates is +/- 1%. This change would not have a material impact on interest received in the period.

Exchange rate sensitivity

Management estimates the impact of a reasonable possible movement in foreign exchange rates at around +/- 10%, to be immaterial.

29. Related party transactions

Transactions between the Company and its subsidiaries, which are related parties, have been eliminated on consolidation and are not disclosed in this note.

Amounts due from subsidiaries

The Company has entered into a number of unsecured related party transactions with its subsidiary undertakings. The most significant transactions carried out between the Company and its subsidiary undertakings are mainly for short and long-term financing. Amounts owed from these entities are detailed below:

	Outstanding	
	2007 £	2006 £
Cadogan Petroleum Holdings Limited	82,295,032	23,378,531
Ramet Holdings Limited	3,138	-
	<u>82,298,170</u>	<u>23,378,531</u>

The loans are interest free and are denominated in pounds sterling.

Trading transactions

During the year, the Group companies entered into the following transactions with related parties who were not members of the Group:

	Purchase of services		Amounts owed to related parties	
	2007 £	2006 £	2007 £	2006 £
OJSC 'AgroNafloGasTechService'	<u>1,128,206</u>	<u>1,404,067</u>	<u>-</u>	<u>11,000</u>

Purchase of services from related parties were made at the market price on standard terms equivalent to those that prevail in an arm's length transaction. Prior to being held by Ramet Holdings Limited, the shares in OJSC 'AgroNafloGasTechService' were originally held by Mark Tolley and Vasyl Vivcharyk both of whom are Executive Directors of the Company.

Cadogan Petroleum plc

Notes to the financial statements (continued)

Year ended 31 December 2007

29. Related party transactions (continued)

Acquisition of subsidiary

On 26 December 2007, the Company acquired Ramet Holdings Ltd, a company which was owned by Mark Tolley, an Executive Director of the Company. Ramet Holdings Limited is the beneficial owner of 79.9% shares in the Ukrainian company OJSC 'AgroNaftGasTechService' which holds interests in two licences and provides construction services to the oil and gas sector. Prior to being held by Ramet Holdings Limited, the shares in OJSC 'AgroNaftGasTechService' were originally held by Mark Tolley and Vasyl Vivcharyk both of whom are executive Directors of the Group. Refer to note 26 for further details of the transaction.

An outstanding balance of £149,142, being a portion of the total consideration for the acquisition, had not yet been paid to Mark Tolley and Vasyl Vivcharyk at 31 December 2007.

Remuneration of key management personnel

The remuneration of the Directors, who are the key management personnel of the Group, is set out below in aggregate for each of the categories specified in IAS 24 *Related Party Disclosures*.

	Purchase of services		Amounts owed to related parties	
	2007 £	2006 £	2007 £	2006 £
Short-term employee benefits	974,066	559,988	86,177	143,229
Termination benefits	-	95,400	-	-
Share-based payments	4,243,887	-	-	-
	<u>5,173,947</u>	<u>655,388</u>	<u>86,177</u>	<u>143,229</u>

No Directors belong to pension schemes operated by the Group although, as discussed in note 9, the Group made contributions of £1,408 (2006: £8,225) to a former director's' personal pension plan which are not included in the above table.

The total remuneration of the highest paid Director was £278,420 in the year (2006: £180,000).

30. Commitments and contingencies

Joint activity agreements

The Group has interests in eleven licenses for the conduct of its exploration and development activities within Ukraine. Each licence is held with the obligation to fulfil a minimum set of exploration activities within its term and is summarised on an annual basis, including the agreed minimum amount forecasted expenditure to fulfil those activities. The activities and proposed expenditure levels are agreed with the government licensing authority NAK Nadra Ukraine.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

30. Commitments and contingencies (continued)

Joint activity agreements (continued)

The minimum required future financing of exploration and development work on fields under the licence obligations are as follows:

	2007 £'000	2006 £'000
Within one year	26,895	12,665
Between one and five years	18,821	18,660
Total	<u>45,716</u>	<u>31,325</u>

A greater level of capital expenditure is however budgeted over the above period to achieve corporate targets.

Ramet Holdings Limited

Under the terms of acquisition of Ramet Holdings Limited, the Group has a contingent liability in relation to the deferred consideration equal to the number of recoverable proven and probable barrels of oil equivalent from the first two wells drilled and tested in the Malynovestske Field (the Malynovestske license area in the Bogorodchansky Administration District of the Ivano-Frankiviska Administration Region in Western Ukraine). For the purpose of ascertaining the quantity of oil equivalent recoverable, the parties should instruct a suitably qualified and insured independent expert of at least 10 years' standing. Payment shall be paid within 30 days of the expert's report and, notwithstanding that report, shall not exceed US\$5 million (see note 26).

31. Events after the balance sheet date

Acquisition of subsidiary

On 16 January 2008, Astro-Energy LLC signed an agreement to acquire a 99.991% interest in Mercor LLC for a cash consideration of US\$4.35 million. On the same date, Astroinvest-Ukraine LLC signed an agreement to acquire the remaining 0.009% interest in Mercor LLC for US\$490. Under the terms of the agreements, the vendor was obliged to execute certain obligations related to technical documentation on land plots and resolution of certain contractual obligations with other third parties. It was stipulated that the full control would pass to Astro-Energy LLC only after fulfilment of these obligations and after the final 50% payment were made. The final payment was made on 8 April 2008 and management considers that the Group gained control of Mercor LLC as of this date.

Mercor LLC holds an interest in JAA# 17 on the Zagoryanske Licence which was previously acquired by the Group through the purchase of Radley Investments Limited. As a result of the acquisition of Mercor LLC, Astro-Energy LLC and Astroinvest-Ukraine LLC together hold a 100% interest in JAA#17.

Approval of this acquisition was received from the Anti-Monopoly Committee of Ukraine on 28 February 2008.

On 18 January 2008, Astro-Energy LLC acquired a 99.91% stake in the Zagoryanska JAA#1 from Profit LLC for a cash consideration of US\$1 million. The other participant in this joint activity agreement, holding a 0.09% interest is Poltavanaftogasgeologia, a subsidiary of NAK Nadra Ukraine. Approval of this acquisition was received from the Anti-Monopoly Committee of Ukraine on 25 April 2008.

This acquisition has not been treated as a business combination as defined in IFRS 3 *Business Combinations* as it was judged by management that this was an acquisition of business assets rather than that of a business as defined in IFRS 3.

Cadogan Petroleum plc

Notes to the financial statements (continued) Year ended 31 December 2007

31. Events after the balance sheet date (continued)

Share capital issues

Cadogan Petroleum plc issued a further 27,493,066 ordinary shares subsequent to 31 December 2007 as follows, raising gross proceeds of £11,272,157.

Date issued	Number issued	Price per share
January 2008	731	£0.41
February 2008	13,992,335	£0.41
April 2008	13,500,000	£0.41

In January 2008, 3,071,974 shares were issued as part of the consideration for the acquisition of Ramet Holdings Limited (see note 26).

Associated with the financial liability in note 22, as the Company did not complete any additional placing of shares at the increased price per share of £0.60, in accordance with the terms of the share agreement, the price per share for the second tranche was reduced to £0.41 per share. This resulted in 3,861,788 additional ordinary shares of £0.01 each being issued on 9 April 2008.