# FULL ANNUAL REPORT & ACCOUNTS

**Sefton Resources, Inc.**

**Consolidated Financial Statements**
**31 December 2013**

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## NON-EXECUTIVE DIRECTORS' STATEMENT

A considerable amount of change has occurred since the last annual report to shareholders. Since the departure of our CEO in 2013, the three non-executive directors, (the "NED"), have assumed leadership responsibility for the operations of the Group.

Mr Ellerton's departure left a vacuum within the organisation which required all remaining staff, management and NED to collaborate in maintaining the viability of the Group. We are happy to report that the teams in Kansas and California have sustained their business units while being significantly cash constrained.

## Going concern

The Bank of the West (the "Bank") chose not to extend the Group's borrowing facility which expired on 31 December 2013, but instead to require repayment. As the Group was unable to make the required payment, the Board has been actively exploring refinancing options.

The Group had already been looking at various ways in which to realise some of the value inherent in its assets. A number of proposals were received and evaluated. The Group settled on a proposal from Hawker Energy LLC ("Hawker") in which the Group's Californian business would be transferred to a new joint venture company, Tapia LLC, in which Hawker would hold an 80% and the Group the remaining 20% (the "Transaction"). The Transaction, as intended, would allow the Group to repay the Bank, participate in the development and expansion of the California assets and provide additional working capital to invest in other opportunities, including the existing Kansas assets, and general corporate purposes. However, as will be more fully discussed below, the Transaction could not be completed by June 30, 2014, the reporting date for this Annual Report and Accounts. Alternative arrangements have been made, see "Amended Transaction".

Further details of the Amended Transaction can be found in the notice of Extraordinary General Meeting ("EGM") which has been published concurrently with the Annual Report and Accounts and which has been called to approve the Transaction.

In the interim, Hawker has been of considerable assistance in dealing with liquidity issues, addressing the concerns of the Bank and providing capital for maintaining facilities in good working order. The Bank has been receptive to the Hawker initiatives while at the same time pursuing its rights under the credit agreement.

The NED have adopted the going concern basis in preparing the financial statements of the Group for the year ended 31 December 2013. In assessing whether the going concern basis is appropriate, the NED have considered all relevant available information concerning the future of the Group.

In carrying out their review and assessment, the NED have had budgets and forecasts prepared covering the period to July 1, 2015 which they have reviewed and approved. The budget for this period includes numerous assumptions, the majority of which are shown below. The NED consider the Transaction to reflect reasonable value given the difficult circumstances of the Group.

The assumptions used in preparing the budgets and forecasts include:

- Hawker, on its own or with other financial partners, will complete the Transaction detailed in the letter of intent between Hawker and the Group, dated 18 June 2014.

## NON-EXECUTIVE DIRECTORS' STATEMENT (continued)

- Shareholders of the Group will approve the Hawker Transaction at the EGM due to be held on 23 July 2014.
- The Bank will be repaid, in full, using proceeds from the Transaction and will not seek legal remedies to secure repayment of its loan to the Group. See Amended Transaction.
- The Group will receive quarterly instalments from Hawker of $250,000 in retirement of the note due from Hawker.
- Operating costs and overheads will be reduced compared to prior periods.
- The Kansas (TEG Midcontinent and TEG Transmission) operations will remain self-sufficient.
- New capital will be made available to TEG Midcontinent to increase production.
- Unsecured creditors will be paid as cash flow and instalments from Hawker permit.
- Hawker will invest new capital into TEG USA to increase production.

There are uncertainties in the assumptions which could be material.

The key risk is Hawker's ability to complete the Transaction in the appropriate timescale, which is in part, dependent on approval by the shareholders of the Group. Furthermore, the Bank may not grant additional time to repay the loan if the Transaction takes longer than expected to complete.

**Amended Transaction**

In the period just prior to the date of this Annual Report & Accounts, Hawker advised it would be unable to complete all of the provisions of the Transaction prior to the EGM. Discussions commenced with the Bank about extension of the time to repay to accommodate the EGM and short term funding issues. Other banks were also approached about replacing the Bank credit facility. On June 26, 2014, the Bank agreed to an extension of the final repayment date to December 28, 2014, subject to the following conditions:

- An immediate instalment payment of $360,000 to be applied, in order, to an extension fee, attorney's fees incurred by the Bank, default interest and penalties and principal
- A monthly payment of $100,000 plus interest at 8% beginning July 31, 2014
- Full repayment of balance owing on or before December 28, 2014
- Legal fees of $20,000 per month during the forbearance period

Hawker has made the payment of $360,000 on June 27, 2014. Instalment payments beginning July would be sourced first from TEG USA oil sale revenue with additional funding provided by Hawker if required.

The Group is confident that it can comply with these terms and conditions. The Group fully expects to refinance the credit facility from one or more of the alternatives being presented by competing financial institutions. Hawker will provide additional funds if required and intends to provide further working capital to TEG USA to increase oil production in California.

**Other issues**

In addition, the Group does not currently have a CEO, nor any executive directors, a matter which the NED intend to remedy after the Transaction has been completed. However, the NED have been active in the management of the business since the departure of the former CEO in 2013 and monitor the results of operations on a regular basis.

**NON-EXECUTIVE DIRECTORS' STATEMENT (continued)**

The uncertainties referred to above may cast significant doubt on the Group's ability to meet its financial obligations to the Bank and to continue as a going concern. Therefore, the Group may not be able to realise its assets and discharge its liabilities in the normal course of business. However, the NED consider that the assumptions made in the preparation of the budgets and forecasts are appropriate and are, therefore, of the opinion that the going concern basis is appropriate in preparing the financial statements of the Group.

If the Transaction does not complete then the going concern basis for the preparation of these accounts would be inappropriate as the Group does not have the funds available to repay the Bank loan.

## Value

The Transaction, outlined in the most recent letter of intent dated 18 June 2014, results in the following impact for TEG USA:

- TEG USA business activities along with related assets and liabilities (including the asset retirement obligation) are contributed to a JV entity, Tapia LLC
- The Bank debt is settled by Hawker
- TEG USA receives:
    - 20% interest in Tapia LLC valued at $1.375 Million
    - $3 million deferred consideration providing a quarterly cash inflow to the Group of $250,000

This reflects a lower value than book value of the investment, and the book value has been adjusted to reflect this valuation. However, this Transaction will provide for an investment in the property that the Group believes will greatly enhance the value of the TEG USA properties and therefore, the 20% retained by the Group.

This value also reflects substantially more value than might accrue to shareholders if the Bank enforces its rights under the loan agreement, appoints a receiver and sells all of the Group's assets at a fire sale price to clear the loan and accrued interest.

The retained 20% of TEG USA, held in Tapia LLC, will be a passive investment, with the intention of realising value within a three to five year time period.

## Strategic direction and next steps

Assuming shareholders approve the Transaction, the Group will initially focus on strengthening its financial position and resume modest growth in Kansas using proceeds from the Transaction and, at some point in the future when one or more appropriate partners can be found, third party joint venture arrangements. The EGM to approve the Transaction is set for 23 July 2014. It is the intention of the Board to call the Annual General Meeting of the Company ("AGM") for September.

The Board will seek to engage a CEO who can lead the Group in accordance with the mandate set by the Board.

**NON-EXECUTIVE DIRECTORS' STATEMENT (continued)**

The Board plans to adopt the Quoted Companies Alliance Corporate Governance Code for Small and Mid-Size Quoted Companies by the time of the AGM.

Former CEO and Chairman, Mr Ellerton, has requested arbitration in respect of his contract. The Board has chosen legal counsel and arbitrator for this process. The Group believes it has a strong position in the pending arbitration. The Group can make no further comments on this matter until arbitration is settled.

The Board of Directors currently consists of three independent members, none of whom are US residents. Additional Board member or members with "local" knowledge may be sought.

Longer term, it will be the responsibility of the new management team to source opportunities to participate in energy related business.

## Investor relations

To conserve cash and reduce overheads, we have closed the office in London and did not renew the contract with our investor relations consultant. While the UK capital markets are of key interest to Sefton, given the financial situation of the Group, cash conservation was of paramount importance. Travel and other expenses have been minimal as we move through 2014.

## Management

The departure of Mr Ellerton was a major event for the Group. The NED have not appointed another CEO as the circumstances have made it very difficult to attract a suitable candidate. The NED, working closely with our staff, are focused on getting the financial house in order to return the Group to a position of strength and viability. The NED expect the third quarter of 2014 to be the most likely time for such an appointment.

Financial consulting services are contracted from a reliable source familiar with IFRS reporting requirements. It is not expected that a CFO will be appointed until after a new CEO has an opportunity to assess the management team required going forward.

## Summary

The challenges have been numerous and daunting, the solutions inventive, and the stress plentiful. Shareholders have expressed their concerns strongly to the NED. We have not been able to respond as effectively as you would like, but we have responded to the issues. Shareholders are fortunate to have a strong operational team on the ground in Kansas and California.

We endorse the Transaction and encourage each shareholder to vote in favour of it.

## Independent Board of Non-Executive Directors

Keith Morris Mark Smith Tom Milne

**OPERATIONAL REVIEW**

## California

Production in California has declined during recent months as cash constraints affected the ability to pay for maintenance, chemicals, power and service rigs.

Enhanced oil recovery is an energy intensive process requiring consistent cyclic steaming. We have not been able to apply steam to the reservoirs consistently. Repair of mechanical problems has been delayed as service providers require advance payment due to outstanding invoices. Chemicals for in-tank oil/water separation must also be prepaid.

Hawker has advanced TEG USA in excess of $100,000 for maintenance work and reservoir steaming. Additional amounts of working capital will be available in the third quarter. Steaming re-commenced in June such that incrementally increased oil production is expected in July.

## Kansas

Operationally, the subsidiaries are essentially self-sufficient from production but need additional capital to realise their potential.

Pipeline connections are delayed until additional capital can be made available. The Transaction should provide such capital.

**FINANCIAL REVIEW**

## Revenues

During the year ended 31 December 2013, revenue rose to $4.7 million, compared to $4.3 million in 2012. This was as a result of increased production in California and the commencement of production in Kansas.

The realised oil prices averaged $99 a barrel in California during 2013, which was a slight reduction on the $103 a barrel realised in 2012 – however, the Group still benefits from a favourable premium paid for heavy oil in California. Realised oil prices in Kansas averaged at $85 a barrel during 2013.

Oil volume sold in California was 45,377 barrels, compared to 39,158 barrels achieved in 2012. Production in 2013 in California was 45,199 barrels (2012: 42,498 barrels). Oil volume sold in Kansas was 3,187 barrels. Production in 2013 in Kansas was 4,038 barrels. Towards the end of 2012 a small amount of oil (yielding revenue of $12,000) was sold from tanks in Kansas. Although oil production was initiated in late 2012, sales of produced oil in Kansas didn't commence until early in 2013.

## Loss for the year

Cost of sales (lease operating expenses and royalties) was $1.9 million compared to $1.5 million in 2012. The increase in costs is due to fixed costs not decreasing, higher repairs and maintenance expenses and an increase in royalties payable resulting from the increased revenues.

After deducting the cost of sales from revenue, the gross profit from oil sales in 2013 is $2.8 million (2012: $2.8 million).

General and administrative expenses recognised in 2013 have increased significantly compared to 2012, largely due to significant legal expenses incurred during the year and accruals for anticipated legal expenses in relation to the legal arbitration with Mr Ellerton.

The most significant impact on the loss for the financial year, however, is in relation to the two impairments recognised, as disclosed in notes 7 and 8 to the financial statements. This resulted from detailed impairment reviews of both exploration and evaluation assets and production assets.

In Kansas, $1,923,000 of exploration and evaluation intangible assets have been impaired at 31 December 2013. Additionally, $405,000 of intangible assets in Kansas were transferred from intangible assets to production assets and plant and equipment assets.

In California, as a result of the constrained financial circumstances of the Group, the production assets were determined to be impaired down to the value indicated by the proposal from Hawker Energy. This resulted in an impairment of $10,963,000 being recognised at 31 December 2013.

Depreciation and depletion charges have increased in 2013 to $570,000 from $476,000 due to the combination of a higher asset base and increased production – the latter being the basis on which depletion charges are calculated.

**FINANCIAL REVIEW (continued)**

Net loss for the year after deducting finance costs was $13.77 million compared with $21,000 profit in 2012.

## Cash flow

It has been a very challenging year for the Group in terms of cash flow, however net cash provided by operating activities, as shown in the first section of the Group's cash flow statement, increased from $0.6 million in 2012 to $1.5 million in 2013.

Net cash provided by financing activities was significantly reduced, $140,000 in 2013 compared to $3.0 million in 2012.

This has consequently constrained the Group's ability to invest in its operations, with net cash flows used in investing activities down from $5.2 million in 2012 to $2.3 million in 2013.

As detailed in the non-executive directors' statement, the bank chose to demand repayment of total outstanding balances by January 02, 2014, and consequently the Group's non-executive directors have been actively working to identify alternative solutions to the Group's significant cash flow issues.

## Closing cash

The Group had $250,000 in cash on hand at 31 December 2013 as compared to $947,000 at the end of 2012.

## Equity fundraising

During 2013, the Group raised a net total of $0.93 million ($1.08 million before expenses) in equity funding compared with $3.73 million ($4.33 million before expenses) in 2012.

In March 2013, the Group raised approximately $1 million from a placing of 108,333,333 common shares at 0.6 pence per share.

In August 2013, a drawdown was made on the EFF (see note 14) raising $109,000 before costs from the issue of 16,000,000 common shares at 0.441 pence per share.

In December 2013, the Group issued $220,000 of convertible loan notes at a 10% original issue discount. Conversion of the loan notes is at the holder's option; the conversion price is 85% of the lowest VWAP of 5 trading days prior to conversion date. Interest accrues on the aggregate unconverted and outstanding principal on a monthly basis at 4% p.a. until either payment or conversion of the loan note. Additionally, 5,141,779 share warrants with a life of 3 years were issued alongside the loan notes, which have been valued in accordance with IFRS 2 and treated as a transaction cost of the loan notes.

A number of conversions have taken place in relation to these loan notes since the balance sheet date, these are detailed in note 17 to the financial statements.

**FINANCIAL REVIEW (continued)**

## Investments

The Group invested $2.3 million in cash in the development of its oil and gas and natural gas gathering and transportation projects during the year – compared to $5.2 million invested in cash in the previous year.

## Liquidity & risk management

The Group's objectives, policies and process for managing risks and the methods used to measure them are detailed in note 12 to the financial statements.

## Shareholders' equity

As at 31 December 2013, there were 704,089,741 common shares in issue of nil par value. At June 30, 2014, 787,810,441 common shares are issued and outstanding.

## Key Performance Indicators

The non-executive directors monitor financial information on a monthly basis, in particular production (barrels), sales volume (barrels) and revenue, cost of sales and general and administrative overheads, as set out above in the financial review.

Ms A Ovens FCCA
Financial Consultant

## STATEMENT OF DIRECTORS' RESPONSIBILITIES

The Directors are responsible for preparing the Annual Report and Accounts in accordance with applicable law and regulations. The Directors have elected to prepare the financial statements for the Group in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union.

International Accounting Standard 1 requires that financial statements present fairly for each financial year the Group'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 Preparation and Presentation of Financial Statements". In virtually all circumstances, a fair presentation will be achieved by compliance with all IFRS. The 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 IFRS is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Group'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 Group, for safeguarding the assets and for taking responsible steps for the prevention and detection of fraud and other irregularities.

## INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF SEFTON RESOURCES, INC.

Year ended 31 December 2013

We have audited the consolidated financial statements of Sefton Resources, Inc. (the "Group") for the year ended 31 December 2013 which comprise the consolidated statement of comprehensive income, consolidated balance sheet, consolidated statement of changes in equity, consolidated statement of cash flows, and accompanying notes.

The financial reporting framework that has been applied in their preparation is International Financial Reporting Standards (IFRS) as adopted by the European Union.

This report is made solely to the Group's members, as a body, in accordance with the terms of our engagement letter. Our audit work has been undertaken so that we might state to the Group's members those matters we are required to state to them in an auditor's 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 Group and the Group's members as a body, for our audit work, for this report, or for the opinions we have formed.

### Respective responsibilities of directors and auditor

As described in the statement of Directors' responsibilities set out on page 11, the Directors are responsible for the preparation of the consolidated financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the consolidated financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). These standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

### Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatements, whether caused by fraud or error. This includes an assessment of whether the accounting policies are appropriate to the Group's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Directors, and the overall presentation of the financial statements.

In addition, we read all the financial and non-financial information in the Full Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

### Opinion on consolidated financial statements

In our opinion:

- The consolidated financial statements give a true and fair view of the state of the Group's affairs as at 31 December 2013 and of the results of the Group for the year then ended;

- The consolidated financial statements have been properly prepared in accordance with IFRS as adopted by the European Union.

**Emphasis of matter – going concern**

In forming our opinion on the consolidated financial statements, which is not modified, we have considered the accuracy of the disclosures made in the strategic report and in note 1 to the consolidated financial statements concerning the uncertainty regarding the Group's ability to complete the proposed sale of its Californian operations in the appropriate timescale, repay its outstanding bank facilities and generate sufficient working capital to support the ongoing requirements of the Group. These conditions indicate the existence of material uncertainties which may affect the Group's ability to continue as a going concern. In view of the significance of these issues we consider that the disclosure should be brought to your attention.

However, the financial statements do include an impairment adjustment to the value of production assets based on the successful completion of this transaction, but do not include any other adjustments that would result if the Group was unsuccessful in completing the transaction.

**CHANTREY VELLACOTT DFK LLP**

**Chartered Accountants and Statutory Auditor**
**London**
**28 June 2014**

# Sefton Resources, Inc.

## Consolidated statement of comprehensive income
## for the year ended 31 December 2013

| | Notes | 2013 | 2012 |
|---|---|---|---|
| | | $000 | $000 |
| Revenue | | 4,727 | 4,289 |
| Cost of sales | | (1,894) | (1,478) |
| Gross profit | | 2,833 | 2,811 |
| General and administrative expense | | (2,594) | (1,792) |
| Retirement obligation expense | 6 | (72) | (56) |
| | | (2,666) | (1,848) |
| Profit before exceptional administrative expenses | | 167 | 963 |
| Exceptional expenses – impairment (Kansas) | 7 | (1,923) | - |
| Exceptional expenses – impairment (California) | 8 | (10,963) | - |
| (Loss) / profit before non-cash charges, interest and taxes | | (12,719) | 963 |
| Depletion, depreciation and amortisation | 8 | (570) | (476) |
| Share-based payments | 14 | (234) | (211) |
| Operating (loss) / profit | | (13,523) | 276 |
| Finance costs | 2 | (246) | (255) |
| Total comprehensive (expense) / income for the year attributable to equity holders of the parent | | (13,769) | 21 |

| | | Per share | Per share |
|---|---|---|---|
| | | $ | $ |
| Basic and diluted (loss) / earnings per share | 15 | (0.02047) | 0.00004 |

# Sefton Resources, Inc.

## Consolidated balance sheet
## at 31 December 2013

| | Notes | 2013 | 2012 |
|---|---|---|---|
| | | $000 | $000 |
| **Non-current assets** | | | |
| Intangible assets | 7 | 3,671 | 4,928 |
| Property, plant and equipment | 8 | 11,511 | 21,140 |
| | | 15,182 | 26,068 |
| **Current assets** | | | |
| Cash and cash equivalents | | 250 | 947 |
| Trade and other receivables | 9 | 690 | 859 |
| | | 940 | 1,806 |
| **Total assets** | | 16,122 | 27,874 |
| **Non-current liabilities** | | | |
| Long- term borrowings | 11 | - | 5,450 |
| Retirement obligation | 6 | 292 | 220 |
| Asset retirement obligation | 13 | 1,939 | 1,678 |
| | | 2,231 | 7,348 |
| **Current liabilities** | | | |
| Trade and other payables | 10 | 1,745 | 628 |
| Current portion of borrowings | 11 | 4,955 | 129 |
| | | 6,700 | 757 |
| **Total liabilities** | | 8,931 | 8,105 |
| **Net assets** | | 7,191 | 19,769 |
| **Shareholders' equity** | | | |
| Share capital | 14 | 24,692 | 23,750 |
| Retained deficit | | (17,501) | (3,981) |
| **Total equity attributable to equity holders of the parent** | | 7,191 | 19,769 |

The annual financial statements set out on pages 14 to 49 were approved and authorised for issue by the Board of Directors and signed on its behalf on 28 June 2014 by:

TG Milne, Non-Executive Director

The accompanying notes form part of these consolidated financial statements.

## Sefton Resources, Inc.

### Consolidated statement of changes in equity
### for the year ended 31 December 2013

| | Common shares, no par value | | | |
|---|---|---|---|---|
| | Shares | Amount | Retained deficit | Total |
| | | $000 | $000 | $000 |
| **At 1 January 2012** | 397,651,006 | 20,016 | (4,253) | 15,763 |
| Shares issued for cash | 179,930,714 | 4,326 | - | 4,326 |
| Share issuance costs | - | (592) | - | (592) |
| Compensation expense related to share options | - | - | 211 | 211 |
| Compensation expense related to share warrants | - | - | 40 | 40 |
| Total comprehensive income | - | - | 21 | 21 |
| **At 31 December 2012** | 577,581,720 | 23,750 | (3,981) | 19,769 |
| **At 1 January 2013** | 577,581,720 | 23,750 | (3,981) | 19,769 |
| Shares issued for cash | 124,333,333 | 1,082 | - | 1,082 |
| Share issuance costs | - | (150) | - | (150) |
| Stock issued on conversion of loan notes | 2,174,688 | 10 | - | 10 |
| Compensation expense related to share options | - | - | 234 | 234 |
| Compensation expense related to share warrants | - | - | 15 | 15 |
| Total comprehensive expense | - | - | (13,769) | (13,769) |
| **At 31 December 2013** | 704,089,741 | 24,692 | (17,501) | 7,191 |

## Sefton Resources, Inc.

### Consolidated statement of cash flows
### for the year ended 31 December 2013

| | 2013<br>$000 | 2012<br>$000 |
|---|---|---|
| **Cash flows from operating activities** | | |
| Total comprehensive (expense) / income | (13,769) | 21 |
| Finance costs | 246 | 255 |
| Share based payments | 234 | 211 |
| Retirement benefit expense | 72 | 56 |
| Depreciation | 570 | 476 |
| Impairments | 12,886 | - |
| | 239 | 1,019 |
| Changes in operating assets and liabilities: | | |
| Changes in trade and other receivables | 168 | (379) |
| Changes in trade and other payables | 1,102 | (82) |
| **Net cash provided by operating activities** | 1,509 | 558 |
| **Cash flows from investing activities** | | |
| Purchase of intangible assets | (1,071) | (1,390) |
| Purchase of property, plant and equipment | (1,275) | (3,814) |
| **Net cash used in investing activities** | (2,346) | (5,204) |
| **Cash flows from financing activities** | | |
| Proceeds of issue of new shares | 1,082 | 4,326 |
| Expenses of new share issue | (150) | (592) |
| Proceeds from notes payable | 193 | 129 |
| Payments on notes payable | (796) | (600) |
| Interest paid | (189) | (233) |
| **Net cash provided by financing activities** | 140 | 3,030 |
| Net decrease in cash and cash equivalents | (697) | (1,616) |
| Cash and cash equivalents at beginning of year | 947 | 2,563 |
| **Cash and cash equivalents at end of year** | 250 | 947 |

## 1. Accounting policies

**General information**

Sefton Resources, Inc. (the "Company" and together with its subsidiaries, the "Group") was incorporated on January 17, 1995, as a British Virgin Islands corporation and has been primarily engaged in the exploration, development, and production of oil and natural gas and gathering and transporting natural gas in the Continental United States. The Group's properties are located in California and Kansas, USA.

The Group's consolidated financial statements are presented in US Dollars, which is the Group's functional and presentation currency.

**Basis of preparation**

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU. All accounting standards and interpretations issued by the International Accounting Standards Board and the IFRS Interpretations Committee effective for the periods covered by these financial statements have been consistently applied to all years presented, unless otherwise stated. The consolidated financial statements have been prepared under the historical cost convention.

**Going concern**

The NED have adopted the going concern basis in preparing the financial statements of the Group for the year ended 31 December 2013. In assessing whether the going concern basis is appropriate, the NED have considered all relevant available information concerning the future of the Group.

In carrying out their review and assessment, the NED have had budgets and forecasts prepared covering the period to July 1, 2015 which they have reviewed and approved. The budget for this period includes numerous assumptions, the majority of which are shown below. The NED consider the Hawker Transaction to reflect reasonable value given the difficult circumstances of the Group.

The assumptions used in preparing the budgets and forecasts include;

- Hawker, on its own or with other financial partners, will complete the Transaction detailed in the letter of intent between Hawker and the Group, dated 18 June 2014.
- Shareholders of the Group will approve the Hawker Transaction at the EGM due to be held on 23 July 2014.
- The Bank will be repaid, in full, using proceeds from the Hawker Transaction and will not seek legal remedies to secure repayment of its loan to the Group.
- The Group will receive quarterly instalments from Hawker of $250,000 in retirement of the note due from Hawker.
- Operating costs and overheads will be considerably reduced.
- The Kansas (TEG Midcontinent and TEG Transmission) operations will remain self-sufficient.
- New capital will be made available to TEG Midcontinent to increase production.
- Unsecured creditors will be paid as cash flow and instalments from Hawker permit.
- Hawker will invest new capital into TEG USA to increase production.

There are uncertainties in the assumptions which could be material.

The key risk is Hawker's ability to complete the Transaction in the appropriate timescale, which is, in part, dependent on approval by the shareholders of the Group. Furthermore, the Bank may not grant additional time to repay the loan if the Hawker Transaction takes longer than expected to complete. See note 17 regarding events after the balance sheet date.

In addition, the Group does not currently have a CEO, nor any executive directors, a matter which the NED intend to change after the Hawker Transaction has been completed. However, the NED have been active in the management of the business since the departure of the former CEO in 2013 and monitor the results of operations on a regular basis.

The uncertainties referred to above may cast significant doubt on the Group's ability to meet its financial obligations to the Bank and to continue as a going concern. Therefore, the Group may not be able to realise its assets and discharge its liabilities in the normal course of business. However, the NED consider that the assumptions made in the preparation of the budgets and forecasts are appropriate and are, therefore, of the opinion that the going concern basis is appropriate in preparing the financial statements of the Group.

If the Transaction does not complete then the going concern basis for the preparation of these accounts would be inappropriate as the Group does not have the funds available to repay the Bank loan.

**Basis of consolidation**
The consolidated financial statements incorporate the results of the Company and entities controlled by the Company (its subsidiaries) as at 31 December 2013. 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.

Intercompany transactions, balances and unrealised gains on transactions between Group entities (the Company and its subsidiaries) are eliminated on consolidation.

At 31 December 2013, the Group's subsidiaries, all of which are registered and incorporated in the United States, and included in the consolidated Group financial statements, were:

| | |
|---|---|
| TEG Oil & Gas USA, Inc. | 100% |
| TEG MidContinent, Inc. | 100% |
| TEG Transmission, Co., LLC | 100% |

**New accounting standards and interpretations**
The Group has reviewed new and amended standards and interpretations currently in issue but not effective as of 31 December 2013 and determined that none of these new standards and interpretations will have significant impact on reported results.

Amendments to existing standards and new standards which may apply to the Group in future accounting periods are:

| | | Effective date (periods beginning on or after) | EU adopted | Impact on Sefton Resources Inc |
|---|---|---|---|---|
| IAS 32 | Financial Instruments: Presentation - Offsetting Financial Assets and Financial Liabilities | 1 January 2014 | Yes | Disclosure only |
| IAS 36 | Impairment of Assets – Recoverable amount disclosures for non-financial assets | 1 January 2014 | Yes | Disclosure only |
| IFRS 9 | Financial Instruments: Classification and Measurement | Currently no effective date | No | Classification and measurement of financial instruments |
| IFRS 10 | Consolidated Financial Statements | 1 January 2014 | Yes | No material impact |
| IFRS 11 | Joint Arrangements | 1 January 2014 | Yes | No material impact |
| IFRS 12 | Disclosure of Involvement with Other Entities | 1 January 2014 | Yes | Disclosure only |
| | Annual Improvements to IFRSs (2010-2012 & 2011-2013 Cycles) | 1 January 2014 | No | No material impact |

**Financial instruments**
Financial instruments are recognised when the Group becomes a party to contractual provisions of the instrument.

Financial assets are derecognised when the contractual rights to the cash flows from the financial asset expire, or when the financial asset and all substantial risks and rewards are transferred. A financial liability is derecognised when it is extinguished, discharged, cancelled or expires.

**Financial assets**
The Group's financial assets are all classified as loans and receivables. The Group's loans and receivables comprise trade and other receivables and cash and cash equivalents.

**Cash and cash equivalents**
Cash and cash equivalents include cash on hand, deposits held at call with banks and other short-term highly liquid investments which are subject to insignificant risk of changes in value. Bank overdrafts are shown within loans and borrowings in current liabilities on the consolidated balance sheet.

**Trade and other receivables**
These arise principally through the provision of supplies of oil and gas (e.g. trade receivables), but also incorporate other types of contractual monetary assets.

They are initially recognised at fair value plus transaction costs that are directly attributable to their acquisition or issue and are subsequently carried at amortised cost using the effective interest rate method, less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables and is recognised in the statement of comprehensive income.

**Financial liabilities**
Trade payables and other short-term monetary liabilities are classified as financial liabilities and are initially recognised at fair value and subsequently carried at amortised cost using the effective interest method.

Bank borrowings and loan notes, including convertible loan notes which do not qualify as compound financial instruments, are initially recognised at fair value net of any transaction costs directly attributable to the issue of the instrument. Such interest bearing liabilities are subsequently measured at amortised cost using the effective interest rate method, which ensures that any interest expense over the period to repayment is at a constant rate on the balance of the liability carried in the statement of financial position. Interest expense in this context includes initial transaction costs and premium payable on redemption, as well as any interest or coupon payable while the liability is outstanding.

There is no material difference between the book value and fair value of financial instruments.

**Equity instruments**
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.

**Exploration and evaluation costs**
Exploration and evaluation expenditure, in respect of each area of interest, is accounted for under the successful efforts method.

Costs incurred prior to obtaining the legal rights to explore an area are expensed immediately to the statement of comprehensive income.

Exploration acquisition costs relating to established oil and gas exploration areas are capitalised as exploration and evaluation assets within intangible assets.

The costs of drilling exploration wells are initially capitalised within exploration and evaluation assets pending the results of the well.

Costs are expensed where the well does not result in the successful discovery of potentially economically recoverable reserves.

All other exploration and evaluation expenditure, including general administration costs, geological and geophysical costs, and new venture expenditure is expensed as incurred, except where the expenditure relates to an exploration discovery for which, at balance sheet date, an assessment of the existence or otherwise of economically recoverable reserves is not yet complete; or the expenditure relates to an area of interest under which it is expected that the expenditure will be recouped through successful development and exploitation or by sale.

When an oil or gas field has been approved for commercial development, the accumulated exploration and evaluation costs are transferred to production assets within property, plant and equipment.

Net proceeds from any disposal of an exploration asset are initially credited against the previously capitalised costs. Any surplus proceeds are credited to the statement of comprehensive income.

Development expenditure includes past exploration and evaluation costs, pre-production development costs, development drilling, development studies and other subsurface expenditure pertaining to that area of interest.

The definition of an area of interest for development expenditure is narrowed from the exploration permit for exploration and evaluation expenditure to the individual geological area where the presence of an oil or natural gas field exists, and in most cases will comprise an individual oil or gas field. Development expenditure is reviewed for impairment at each reporting date where there is an indication that the individual geological area may be impaired.

Amortisation is not charged on costs carried forward in respect of areas of interest in the development phase until production commences. When production commences, carried forward development costs are transferred into production assets within property, plant and equipment, and depreciated on the units of production basis over the life of economically recoverable reserves.

**Other intangible assets**
Other intangible assets include expenditure relating to the development of gas gathering and transportation assets.

Amortisation is not charged on costs carried forward in respect of gas gathering and transportation development assets. When such assets are certified as ready for use, carried forward development costs are transferred into gas transportation assets within property, plant and equipment and depreciated.

**Property, plant and equipment**
Costs related to surface plant and equipment and any associated land and buildings are accounted for as property, plant and equipment.

Property, plant and equipment is stated at historical cost less depreciation and any impairment losses. Cost includes expenditure that is directly attributable to the acquisition or construction of these items. Subsequent costs are included in the asset’s carrying amount only when it is probable that future economic benefits associated with the item will flow to the Group and the costs can be measured reliably.

All other costs, including repairs and maintenance costs, are charged to the statement of comprehensive income in the period in which they are incurred.

Depreciation is provided on all property, plant and equipment and is calculated as follows:

| | |
|---|---|
| Equipment and vehicle costs | 2-3 years straight-line |
| Production assets | % of estimated reserves (units of production) |

Depreciation is provided on cost less residual value. The residual value, depreciation methods and useful lives are annually reassessed.

**Impairment of assets**

At each balance sheet date the Directors review the carrying amounts of the Group's 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.

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.

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 periods. A reversal of an impairment loss is recognised in the statement of comprehensive income immediately.

**Provisions**

A provision is recognised on the balance sheet when the Group has a present legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation.

Provisions are measured at the present value of management's best estimate of expenditure required to settle the present obligation at the balance sheet date. The discount rate used to determine the present value reflects current market assessments of the time value of money and the risks specific to the liability.

*Asset retirement obligation*
The Group recognises the present value of the future estimated costs of plugging oil and gas wells and removing surface facilities associated with those oil and gas wells in the financial statements in the period in which the obligation arises.

Upon initial recognition of the liability, an asset retirement cost is capitalised by increasing the carrying amount, included in oil and gas properties, by the same amount as the liability. In periods subsequent to initial measurement, the capitalised asset retirement cost is allocated to depreciation and amortisation expense at the unit of production rate associated with the corresponding asset.

The unwinding of the discount is recognised as an accretion expense in the statement of comprehensive income.

For additional detail regarding provisions see note 13.

**Revenue recognition**
Revenue from the sale of oil and gas is recognised when significant risks and rewards of ownership are transferred to the buyer.

The Group follows the gross method of accounting for royalties where the royalty owners' share of sales is accounted for as an operating expense of the Group, and calculated as a percentage of revenue.

**Income taxes**
Current income tax is based on taxable profit for the year.

The Group's current tax assets and liabilities are calculated using tax rates that have been enacted or substantively enacted by the balance sheet date. The Group's ultimate parent is incorporated in the British Virgin Islands and is not subject to US income tax; however, the parent's subsidiaries are incorporated and operate in the US and are subject to US income taxes.

Deferred income tax is provided in full, using the balance sheet method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income tax is determined using tax rates and laws that are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred tax assets are recognised for deductible temporary differences and unused tax losses only if it is probable that future taxable amounts will be available to utilise those temporary differences and losses.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets and liabilities and when the deferred tax balances relate to the same taxation authority on either the same taxable entity or different taxable entities which intend to settle or realise the amounts simultaneously.

**Foreign currency**

The presentational currency for the Group's consolidated financial statements is US dollars and it is this currency in which the Group reports.

The Group's assets at this time are all in the United States and the majority of transactions are made in US dollars.

Foreign currency transactions by Group companies are recorded in their functional currency (being US dollars) at the exchange rate at the date of the transaction. Monetary assets and liabilities have been translated at rates in effect at the balance sheet date, with any exchange adjustments being charged or credited in the statement of comprehensive income.

**Employment benefits**

Provision is made in the financial statements for all employee benefits.

The Group's contributions to defined contribution pension plans are charged to profit or loss in the period to which the contributions relate.

The Group provides for long-term retirement obligations for certain employees. These provisions are measured at the present value of management's best estimate of expenditure required to settle the present obligation at the balance sheet date. The discount rate used to determine the present value reflects current market assessments of the time value of money and the risks specific to the liability.

**Share-based payments**

Where share options and warrants have been granted to employees, consultants, Directors and suppliers, IFRS 2 has been applied whereby the fair value of the options is measured at the grant date and spread over the period during which the counterparties become entitled to the options. A Black Scholes options valuation model is used to assess the fair value, taking into account the terms and conditions attached to the options. The fair value of goods and services received are measured by reference to the fair value of options.

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

The cumulative expense recognised for equity-settled transactions at each reporting date until the vesting date reflects the extent to which the vesting period has expired and the Group's best estimate of the number of equity instruments that will ultimately vest.

At the end of each period, the Group revises its estimates of the number of options that are expected to vest based on the non-market vesting conditions. It recognises the impact of the revision to original estimates, if any, in the statement of comprehensive income, with a corresponding adjustment to equity.

The charge or credit to the statement of comprehensive income for a period represents the movement in cumulative expense recognised as at the beginning and end of that period.

No expense is recognised for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition, which are treated as vesting irrespective of whether or not the market condition is satisfied, provided that all other performance and/or service conditions are satisfied.

For additional detail regarding share-based compensation see note 14.

**Risk management objectives and policies**

The overall objective of the Board is to set policies that seek to reduce risk as far as possible without unduly affecting the Group's competitiveness and flexibility.

The Group uses various financial instruments including cash, loans, and items such as debtors and creditors that arise directly from its operations. The existence of these financial instruments exposes the Group to a number of financial risks, which are described in note 12 of these financial statements.

**Critical accounting estimates and judgements**

In the process of applying the Group's accounting policies, management makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

*Exploration and evaluation costs*

The Group's accounting policy leads to the capitalisation of intangible exploration and evaluation assets, where it is considered likely that the amount will be recoverable by future exploitation or sale or alternatively where the activities have not reached a stage which permits a reasonable assessment of the existence of reserves. This requires management to make estimates and assumptions as to the future events and circumstances, especially in relation to whether an economically viable extraction operation can be established. Such estimates are subject to change and following initial capitalisation, should it become apparent that recovery of the expenditure is unlikely, the relevant capitalised amount will be written off to the statement of comprehensive income.

*Estimation of oil and gas reserves*

Proved oil and gas reserves are the estimated quantities of oil and gas which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic and operating conditions.

Estimates of oil and gas reserves are inherently imprecise, require the application of judgement and are subject to future revision. Accordingly, financial and accounting measures (such as the standardised measure of discounted cash flows, depreciation, depletion and amortisation charges, and decommissioning provisions) that are based on proved reserves are also subject to change.

*Impairment of non-financial assets*
Management review all non-financial assets at each balance sheet date to determine whether there are any indications of impairment. If any such indication exists, an estimate of the recoverable amount is performed, and an impairment loss is recognised to the extent that carrying amount exceeds recoverable amount.

*Share-based payments*
In determining the fair value of equity-settled share-based payments and the related charge to the statement of comprehensive income, the Group makes assumptions about future events and market conditions; in particular, judgement must be made as to the likely number of shares that will vest, and the fair value of each award granted. The fair value is determined using a valuation model which is dependent on further estimates, including the Company's future dividend policy, the timing with which options will be exercised and the future volatility in the price of the Company's shares.

Such assumptions are based on publicly available information. Different assumptions about these factors to those made by the Company could materially affect the reported value of share-based payments.

*Asset retirement obligation (provision for abandonment)*
Estimates of the amounts of provision for abandonment recognised are based on current legal and constructive requirements, technology and price levels. As actual outflows may be different from estimates due to changes in laws, regulations, technology, prices and conditions, and can take place in the future, the carrying amounts of provisions are regularly reviewed and adjusted to take account of such changes. For additional detail regarding provision for abandonment see note 13.

**Segmental reporting**
The Directors have determined that the Group has two principal business activities — oil and gas exploration and production, and natural gas gathering and transportation — both of which are conducted solely within the United States at this time.

As of 31 December 2013, the Group's revenues derived solely from the production of oil.

Assets relating to natural gas gathering and transportation at 31 December 2013 (and 31 December 2012) are recognised within intangible assets and disclosed within note 7.

Assets relating to oil and gas exploration and production are included within both intangible assets and property, plant and equipment, and are disclosed accordingly in notes 7 and 8.

All costs associated with natural gas gathering and transportation have been capitalised within intangible assets (note 7), as commercial activity has not yet commenced in this segment.

## 2. Finance costs

The Group's finance costs during the years ended 31 December 2013 and 2012 were as follows:

| | **2013** | **2012** |
|---|---|---|
| | $000 | $000 |
| Interest on bank credit agreement | 181 | 203 |
| Interest on notes payable | 15 | 11 |
| Share warrant expense recognised as a finance charge (note 14) | 10 | 6 |
| Accretion of asset retirement obligation | 37 | 35 |
| Other interest charges | 3 | - |
| | 246 | 255 |

## 3. Income tax expense

Sefton Resources, Inc., the parent company, is a British Virgin Islands company and is not subject to taxes based on its jurisdiction. The operating subsidiaries, TEG Oil & Gas USA, TEG MidContinent and TEG Transmission are taxed as US entities.

United States Tax Provision

A reconciliation of the provision (benefit) for income taxes computed at the United States statutory rate to the provision for income taxes as shown in the financial statements of operations for the years ended 31 December 2013 and 2012 is summarised below:

| | **2013** | **2012** |
|---|---|---|
| | % | % |
| Tax provision (benefit) at federal statutory rate | (34.00)% | (34.00)% |
| State taxes, net of federal tax effects | (5.39)% | (6.13)% |
| Other adjustments | (0.39)% | (1.15)% |
| Valuation allowance | 39.78% | 41.28% |
| Net income tax provision (benefit) | –% | –% |

The components of the US deferred tax assets and liabilities as of 31 December 2013 and 2012 are as follows:

| | 2013 | 2012 |
|---|---|---|
| | $000 | $000 |
| Deferred tax assets: | | |
| Federal and state net operating loss and depletion carry forwards | 7,561 | 7,609 |
| Accrued retirement obligation | 766 | 667 |
| Deferred tax liabilities: | | |
| Oil and gas properties | (3,770) | (8,216) |
| Net deferred tax asset | 4,557 | 60 |
| Less: valuation allowance | (4,557) | (60) |
| Net deferred tax asset | - | - |

The Group has a $16,650,344 operating loss carryover (2012: $16,738,273) and $2,593,302 percentage depletion carry forward for US federal income tax purposes as of 31 December 2013 (2012: $2,588,857). The net operating losses may offset taxable income through the year ending 31 December 2033 and begin expiring in the year ending 31 December 2021.

The Group provided a valuation allowance against its deferred tax assets as of 31 December 2013 and 2012 since it is uncertain whether net deferred tax assets will be fully utilised on future income tax returns.

## 4. Staff costs

The average number of employees, Directors and consultants employed or contracted by the Group during the years ended 31 December 2013 and 2012, by category was:

| | 2013 | 2012 |
|---|---|---|
| Management | 3 | 3 |
| Exploration and production | 7 | 7 |
| Administration | 3 | 3 |
| Total | 13 | 13 |

The aggregate compensation expense incurred by the Group for these employees, Directors and consultants during the years ended 31 December 2013 and 2012, by category was as follows:

| | **2013** | **2012** |
|---|---|---|
| | $000 | $000 |
| Salaries and fees | 1,828 | 1,745 |
| Social security and other taxes | 79 | 64 |
| Pension costs | 27 | 22 |
| Retirement obligation | 72 | 56 |
| Share-based compensation | 234 | 211 |
| Total compensation expense | 2,240 | 2,098 |

A portion of the compensation expense of the employees, Directors and consultants included in the table above has been capitalised into the cost of oil and gas properties where those costs are directly attributable costs associated with these assets.

**5. Directors' remuneration**

Total remuneration comprises emoluments, which include salaries or fees accrued, bonuses accrued and health and life insurance benefits received.

Total remuneration also includes pension and retirement benefits accrued, and share-based awards. Ad hoc bonuses may be paid to reward exceptional performance. Such bonuses are decided by the Board on the recommendation of the compensation committee. Share options are also awarded to Directors, employees and consultants from time to time.

The granting of share options to individuals is determined taking into account seniority, commitment to the business and recent performance. Such share option awards are also decided by the Board on the recommendation of the compensation committee. For additional information on share awards and share-based compensation see note 14.

The key management of the Group consists of the Board of Directors. The total remuneration for each Director for the years ended 31 December 2013 and 2012 is shown below.

**Year ended 31 December**

| | 2013 Emoluments & compensation $000 | 2013 Pension contributions & retirement benefits $000 | 2013 Share-based compensation $000 | 2013 Total $000 | 2012 Total $000 |
|---|---|---|---|---|---|
| J Ellerton * | 268 | 61 | 46 | 375 | 520 |
| M Smith ** | 22 | - | 35 | 57 | 46 |
| T Milne ** | 22 | - | 3 | 25 | 10 |
| K Morris *** | 22 | - | 3 | 25 | - |
| K Arleth **** | 10 | - | 24 | 34 | 244 |
| Total | 344 | 61 | 111 | 516 | 820 |

* Includes fees paid under a consultancy agreement with C & J Resources Inc., which is owned by Mr Ellerton and his wife. Resigned as a director 29 August 2013. Fees shown represent compensation whilst in office as a director.
** Non-Executive Director.
*** Non-Executive Director appointed 23 January 2013.
**** Resigned 19 June 2013. Fees shown represent compensation whilst in office as a director.

## 6. Retirement obligation

The Group provides a retirement benefit to certain employees with employment or service contracts as described below.

The following outlines the Group's retirement obligation in relation to these employees:

| | 2013 $000 | 2012 $000 |
|---|---|---|
| Balance 1 January | **220** | 164 |
| Retirement obligation expense | **72** | 56 |
| Balance 31 December | **292** | 220 |

The retirement obligation is based on the individual's ending monthly salary or fee arrangement at the date of retirement times a multiple for years of service. This multiple ranges from one month of base salary or fee for two years of service or less, to two and a half times monthly salary or fee for ten or more years of service.

Four employees are covered by this arrangement at 31 December 2013 (2012: three employees), with their retirement dates under the plan being 2016, 2020 and 2022 (for 2 employees).

## 7. Intangible assets

Intangible exploration assets for all years presented consist of the Group's investment in oil and gas properties and pipeline interests in Kansas.

| | **Total** | | **Exploration & evaluation assets** | | **Gas gathering & transportation assets** | |
|---|---|---|---|---|---|---|
| | **2013** | **2012** | **2013** | **2012** | **2013** | **2012** |
| | $000 | $000 | $000 | $000 | $000 | $000 |
| Balance at 1 January | 4,928 | 3,538 | 3,453 | 2,547 | 1,475 | 991 |
| Additions | 1,071 | 1,390 | 982 | 906 | 89 | 484 |
| Transfers to production assets | (294) | - | (294) | - | - | - |
| Transfers to plant & equipment | (111) | - | (111) | - | - | - |
| Reclassification of assets | - | - | (1,320) | - | 1,320 | - |
| Impairment | (1,923) | - | (1,923) | - | - | - |
| Balance at 31 December | 3,671 | 4,928 | 787 | 3,453 | 2,884 | 1,475 |

As of 31 December 2013, some commercial activity has commenced on the acreage, and those exploration and evaluation assets have been transferred to property, plant and equipment (see note 8) as a result. The remaining exploration and evaluation assets continue to be evaluated for future development potential.

A detailed review of historic costs capitalised as intangible assets was carried out as at the balance sheet date on a lease-by-lease basis. This review identified historic exploration assets which are more appropriately classified as gas gathering and transportation assets – accordingly a reclassification is shown in the table above.

This detailed review also identified $1,923,000 of exploration and evaluation assets in Kansas which qualify for impairment due to obsolescence and / or the discontinuation of investment in the associated leases. This impairment has been recognised in the statement of comprehensive income in the year.

There is no further indication of impairment at the balance sheet date.

## 8. Property, plant and equipment

Production assets consist of the Group's investment in producing oil properties in California and Kansas.

| | Production assets | Other plant & equipment | Total |
|---|---|---|---|
| | $000 | $000 | $000 |
| **Cost** | | | |
| At 1 January 2012 | 22,111 | 188 | 22,299 |
| Additions | 2,140 | 27 | 2,167 |
| At 31 December 2012 | 24,251 | 215 | 24,466 |
| Transfers from exploration & evaluation assets | 294 | 111 | 405 |
| Additions | 1,331 | 168 | 1,499 |
| At 31 December 2013 | 25,876 | 494 | 26,370 |
| **Accumulated depreciation** | | | |
| At 1 January 2012 | 2,677 | 173 | 2,850 |
| Charge | 455 | 21 | 476 |
| At 31 December 2012 | 3,132 | 194 | 3,326 |
| Charge | 492 | 78 | 570 |
| Impairment | 10,963 | - | 10,963 |
| At 31 December 2013 | 14,587 | 272 | 14,859 |
| **Net book value** | | | |
| **At 31 December 2013** | 11,289 | 222 | 11,511 |
| At 31 December 2012 | 21,119 | 21 | 21,140 |

Other plant and equipment assets include office and computer equipment and vehicles.

The Group was in discussions with various third parties during late 2013 regarding the potential sale, or partial sale, of some production assets to alleviate the Group's cash flow issues. These discussions gave a preliminary indication that the carrying value of these assets was higher than their sale value.

A detailed review for impairment indicators was then carried out in relation to property plant and equipment as at the balance sheet date.

Whilst the pre-impairment balance sheet value of production assets is supported by the third party reserves valuation report, a key impairment indicator was identified as at 31 December 2013 in the Group's lack of available financial resources required to develop the production assets to realise the full balance sheet value from those assets.

As a result of this, an impairment review calculation has been performed to compare the carrying value of the production assets in California at 31 December 2013 with the expected fair value (less costs to sell) indicated by the expected compensation to be received from the planned disposal of an 80% interest in the assets and business of the California operations to Hawker Energy.

As the latter value is substantially lower than the balance sheet value, an impairment charge has been recognised, in accordance with the requirements of IAS 36, to decrease the value of production assets held in California to this lower value.

There is no further indication of impairment at the balance sheet date.

## 9. Trade and other receivables

| | **2013** | **2012** |
|---|---|---|
| | $000 | $000 |
| Trade receivables | 324 | 421 |
| Prepayments | 83 | 155 |
| Related party receivables | 283 | 283 |
| | 690 | 859 |

Trade receivables represent accruals of the prior month's unpaid oil revenues, which are received one month in arrears.

Related party receivables at 31 December 2013 and 2012 consist of:

| | **2013** | **2012** |
|---|---|---|
| | $000 | $000 |
| J Ellerton | 283 | 283 |

The receivable from Mr. Ellerton as of 31 December 2013 and 2012 consists of amounts due for cash advances.

See note 10 as Mr. Ellerton, through C&J Resources and C&J Pension Plan is due amounts that the Group owes to the referenced entities controlled by Mr. Ellerton.

The carrying value of trade and other receivables approximates their fair value.

## 10. Trade and other payables

| | 2013<br>$000 | 2012<br>$000 |
|---|---|---|
| Trade payables | 832 | 205 |
| Accruals | 413 | 188 |
| Related party payables | 500 | 235 |
| | 1,745 | 628 |

Related party payables at 31 December 2013 and 2012 consist of:

| **Related party** | **2013**<br>$000 | **2012**<br>$000 |
|---|---|---|
| K Arleth | - | 6 |
| Summit Energy Consultants LLC | 4 | - |
| M Smith | 25 | 6 |
| K Morris | 24 | - |
| C & J Resources Inc. | 262 | 137 |
| C & J Resources Inc. Pension Plan | 157 | 80 |
| T Milne | 28 | 6 |
| Total | 500 | 235 |

Summit Energy Consultants LLC is owned by Mr. Arleth and provided his services under a consultancy agreement.

Amounts due to C&J Resources, Inc. at 31 December 2013 and 2012 represent accrued bonus and fees. C&J Resources Inc. is owned by Mr. Ellerton and his wife and provided his services under a consultancy agreement.

The obligation to the C&J Resources, Inc. Pension Plan at 31 December 2013 and 2012 represents the full outstanding retirement obligation due for Mr. Ellerton's services at that time.

The net amounts due (to) / from organisations under the control of Mr. Ellerton are:

| | **2013**<br>$000 | **2012**<br>$000 |
|---|---|---|
| Mr. Ellerton, C&J Resources, Inc, C&J Resources Inc. Pension plan | (136) | 66 |

The carrying amounts of trade and other payables approximate their fair value.

Included within trade payables above are amounts owed on credit cards in Mr J. Ellerton's name which are Group liabilities, and not included within the related party balance above.

## 11. Borrowings

| | 2013 Within one year $000 | 2013 After one year $000 | 2012 Within one year $000 | 2012 After one year $000 |
|---|---|---|---|---|
| Bank loan | 4,654 | - | - | 5,450 |
| Convertible loan note | 172 | - | - | - |
| Notes payable | 129 | - | 129 | - |
| Total | 4,955 | - | 129 | 5,450 |

### Convertible loan notes

On 17 December 2013, the Group issued $220,000 of convertible loan notes with a one year term, at a 10% original issue discount. Conversion of the loan notes is at the holder's option; the conversion price is 85% of the lowest VWAP of 5 trading days prior to conversion date.

Interest accrues on the aggregate unconverted and outstanding principal on a monthly basis at 4% p.a. until either payment or conversion of the loan notes. The principal plus accrued interest on unconverted notes must be repaid on or before 17 December 2014.

Additionally, 5,141,779 share warrants with a life of 3 years were issued alongside the loan notes, which have been valued in accordance with IFRS 2 (as disclosed in note 14) and treated as a transaction cost of the loan notes.

The following table summarises the initial recognition of these loan notes and the associated original issue discount and transaction costs:

| | $000 |
|---|---|
| Loan notes principal | 220 |
| Original issue discount | (20) |
| Issue costs deducted from consideration | (7) |
| Cash received | 193 |
| Warrants issued | (14) |
| Initial value of loan notes financial liability | 179 |
| Accrued interest | 1 |
| Conversion of loan notes | (8) |
| Value at 31 December 2013 | 172 |

Because the conversion option does not specify a fixed price for a fixed number of shares, these loan notes do not qualify as compound instruments in accordance with IAS 32. The value of the loan notes, less discounts and transaction fees is therefore accounted as a single financial instrument using the effective interest method.

As announced on 8 January 2014, the loan notes holder elected to convert $10,000 of these loan notes into common shares during December 2013. 2,174,688 common shares were issued at £0.00195 per share, which shares are included in the amounts disclosed in note 14. A loss on conversion of $2,000 has been recognised in comprehensive income for the year.

**Bank loan**

On 14 August 2007, the Group entered into a Credit Agreement with its primary bank lender for a credit facility with a maximum commitment amount of $10 million.

The Credit Agreement has been amended and restated on several occasions. The most recent amendment to the agreement was made on 10 May 2013, where a further extension to January 2014 was agreed, with a number of smaller principal payments being made each month from July 2013.

The interest rate under the Credit Agreement is the prime rate plus 0.5% or a LIBOR based rate, at the Group's election.

Advances under this agreement totalled $4.65 million and $5.45 million at 31 December 2013 and 2012, respectively.

The Credit Agreement contains various covenants that include restrictions on additional debt, sale of collateralised assets, as the Notes are secured by a mortgage on the Group's oil and gas properties (see notes 7 and 8), and maintenance of minimum working capital and debt service ratios.

The Bank currently holds a charge over all the assets of TEG USA, plus a parent company guarantee from Sefton and further guarantees from TEG Midcontinent and TEG Transmission. Upon payment in full of the Old Loan Facility, these guarantees from Sefton and subsidiaries will be cancelled. Hawker holds a second charge on the assets of TEG USA under the Subordinated Loan.

Subsequent to the balance sheet date, the Bank gave formal notice to the Company that its current facility will not be renewed in its current form and that the outstanding loan balance became due in full in January 2014.

## 12. Financial instruments, risk exposure and management

The principal financial instruments used by the Group from which the financial risk arises are as follows:

| | 2013 | 2012 |
|---|---|---|
| | $000 | $000 |
| **Financial assets** | | |
| Cash and cash equivalents | 250 | 947 |
| Trade receivables | 324 | 421 |
| Related party receivables | 283 | 283 |
| | 857 | 1,651 |

| | 2013 | 2012 |
|---|---|---|
| | $000 | $000 |
| **Financial liabilities** | | |
| Trade payables | 832 | 205 |
| Accruals | 413 | 188 |
| Related party payables | 500 | 235 |
| Borrowings | 4,955 | 5,579 |
| | 6,700 | 6,207 |

The Group's activities expose it to a variety of financial risks that arise as a result of its exploration, development, production, and financing activities. The Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance.

The Group's objectives, policies and process for managing risks and the methods used to measure them are as follows.

***Commodity price risk***
The Group is exposed to commodity price risk as it sells its oil and gas production on a floating price basis, and may consider partially mitigating this risk in the future through hedging instruments.

***Interest rate risk***
The Group has a $10 million credit facility (2012: $10 million) with a $4.65 million borrowing base (2012: $5.45 million) with its primary bank lender at a variable interest rate. The Group does not currently hedge its interest rate exposure and consequently, its net income or loss is directly affected by changes in interest rates.

The Group's bank deposits bear interest at nominal rates, and changes in these rates do not have any significant impact on its financial results.

The Group additionally issued $220,000 of convertible loan notes in December 2013. Interest accrues on the aggregate unconverted and outstanding principal on a monthly basis at a fixed rate 4% p.a. until either payment or conversion of the loan note.

***Credit risk***
Although the Group markets its crude oil to two counterparties, the Group has not historically experienced any bad debts or delays in payment with respect to its trade receivables.

***Market risk***
Due to the nature of the Group's operations during 2013 and 2012, it is mainly exposed to risk arising from fluctuations in the price of oil.

During the periods under review, the following oil prices (per barrel) applied to the oil sales across the Group:

| Year ended 31 December | High | Low | Average |
|---|---|---|---|
| 2013 | $106.15 | $74.66 | $98.07 |
| 2012 | $114.63 | $90.07 | $102.76 |
| 2011 | $114.80 | $83.36 | $102.62 |

***Liquidity risk***
Liquidity risk is the risk that the Group will not have sufficient funds to meet liabilities. The Group manages its liquidity needs through forecasts which are reviewed regularly by the Board to ensure sufficient funds exist to finance the Group's current operational and investment cash flow requirements.

At 31 December 2013 the Group held approximately $250,000 in cash (2012: $947,000).

There have been no substantive changes in the Group's exposure to financial instrument risks, as objectives, policies and processes for managing those risks or the methods used to measure them from previous periods have not changed.

In managing liquidity risk, the main objective of the Group is to ensure that it has the ability to pay all of its liabilities as they fall due. The Group monitors its levels of working capital to ensure that it can meet its liabilities as they fall due.

The table below shows the undiscounted cash flows on the Group's financial liabilities as at 31 December 2013 and 2012 on the basis of their earliest possible contractual maturity.

| | Total $000 | Within 2 months $000 | Within 2 -6 months $000 | 6 – 12 months $000 | Greater than 12 months $000 |
|---|---|---|---|---|---|
| At 31 December 2013 | | | | | |
| Trade payables | 832 | 832 | - | - | - |
| Accruals | 413 | - | 413 | - | - |
| Bank loan | 4,654 | 4,654 | - | - | - |
| Other loan notes | 301 | - | - | 301 | - |
| | 6,200 | 5,486 | 413 | 301 | - |
| At 31 December 2012 | | | | | |
| Trade payables | 205 | 205 | - | - | - |
| Accruals | 188 | - | 188 | - | - |
| Bank loan | 5,450 | - | - | - | 5,450 |
| Other loan notes | 129 | - | 129 | - | - |
| | 5,972 | 205 | 317 | - | 5,450 |

## 13. Asset retirement obligation

The undiscounted liability for asset retirement obligations as of 31 December 2013 is estimated at $3,278,000 (2012: $2,908,000), which is expected to be incurred in the period between 2016 and 2036, and does not include any potential salvage values. The present value of the obligation is estimated using a discount rate of 3.5%.

A reconciliation of the asset retirement obligation is as follows:

| | **2013** $000 | **2012** $000 |
|---|---|---|
| Liabilities, beginning of year | 1,678 | 1,604 |
| Accretion expense | 37 | 35 |
| Revision to estimate | 224 | 39 |
| Liabilities, end of year | 1,939 | 1,678 |

## 14. Share capital, share options and share-based payments

The Group's share capital for the years ended 31 December 2013 and 2012 is as follows:

| | 2013 | 2012 |
|---|---|---|
| **Authorised** | | |
| Three billion common shares at nil par value | - | - |
| Number of common shares in issue | 704,089,741 | 577,581,720 |
| | $000 | $000 |
| **Issued and fully paid** | | |
| Share capital | 24,692 | 23,750 |

**Allotments during the year**

| Date | Price per share ($) | Number of shares issued | Total consideration received $000 |
|---|---|---|---|
| 6 March – placing | 0.0090 | 108,333,333 | 972,240 |
| 23 August – EFF drawdown | 0.0068 | 16,000,000 | 109,317 |
| 23 December – loan notes conversion | 0.0046 | 2,174,688 | 10,000 |

During the year ended 31 December 2013 the Group issued 126,508,021 common shares (2012: 179,930,714 shares) and received proceeds of $1,091,557 (2012: $4,326,000) before expenses of $150,000 (2012: $592,000).

**Equity financing facility**

During the prior year, the Group entered into an equity financing facility with Darwin Strategic Ltd.

The facility allows drawdowns of up to £15m in total over the course of 3 years. Drawdowns, which are at the Group's discretion, comprise the issue of common shares in Sefton Resources Inc to Darwin for cash, with the issue price being based on recent trading prices, less a 5% discount. The common shares issued under these drawdowns are equity instruments.

As part of the arrangement, Darwin also has the right to subscribe for up to 10% of any placings of common shares by the Company. Darwin also received warrants over 3,500,000 of the Company's common shares: these warrants had a fair value at issue date of $40,048.

The Group has received £70,500 during the year (2012: £616,412) as part of this arrangement, in exchange for 16,000,000 common shares (2012: 58,750,000).

**Share options and share-based payments**

The Group maintains an incentive share option plan whereby from time to time at the discretion of the Board, options to purchase common shares may be granted to the Directors, consultants and employees of the Group.

The plan specifies that the subscription exercise price of such options shall not be less than the applicable market price of the common shares at the date of grant of the relevant option. The number of common shares for which options may be granted is limited so that at any time the total number of common shares subject to option under the plan will not exceed 10% of the total number of common shares issued and outstanding.

The options vest over a three year period and have a ten year life. The Group records a share-based payment expense based on an estimate of the fair value of the option awarded. The fair value is estimated using a Black-Scholes option pricing model.

The fair value of the various options is determined using a Black-Scholes option pricing model and based on the inputs below.

| **Grant date** | **18-Mar-08** | **25-Jun-08** | **1-Jan-11** |
|---|---|---|---|
| Number of options | 3,850,000 | 2,750,000 | 13,000,000 |
| Share price at grant - pounds | 0.0578 | 0.0675 | 0.0150 |
| Exercise price – pounds | 0.0600 | 0.0650 | 0.0175 |
| Volatility | 62.78% | 67.17% | 161.51% |
| Dividend yield | nil | nil | nil |
| Risk free investment rate | 0.014 | 0.0248 | 0.0325 |
| Option life – years | 6.5 | 6.5 | 10.0 |
| Fair value per share option - pounds | 0.034 | 0.044 | 0.0149 |

| **Grant date** | **7-Feb-11** | **24-Jul-11** | **27-Sep-11** |
|---|---|---|---|
| Number of options | 1,000,000 | 3,500,000 | 5,500,000 |
| Share price at grant - pounds | 0.0180 | 0.0305 | 0.0224 |
| Exercise price – pounds | 0.0200 | 0.0350 | 0.0350 |
| Volatility | 122.40% | 163.06% | 69.01% |
| Dividend yield | nil | nil | nil |
| Risk free investment rate | 0.0325 | 0.0325 | 0.0325 |
| Option life – years | 10.0 | 10.0 | 10.0 |
| Fair value per share option - pounds | 0.0171 | 0.302 | 0.0158 |

| **Grant date** | **05-Jul-13** |
|---|---|
| Number of options | 27,000,000 |
| Share price at grant - pounds | 0.0047 |
| Exercise price – pounds | 0.0063 |
| Volatility | 70.43% |
| Dividend yield | nil |
| Risk free investment rate | 0.014 |
| Option life – years | 5 |
| Fair value per share option - pounds | 0.0018 |

**Warrants**

Warrants issued in December 2013 alongside convertible loan notes were fair valued using a Black-Scholes option pricing model.

Warrants issued in June 2012 as part of the arrangement of the equity financing facility were also fair valued using a Black-Scholes option pricing model.

Inputs to the Black-Scholes pricing model for all warrants issued are detailed below:

| **Grant date** | **Jun-12** | **Dec-13** |
|---|---|---|
| Number of warrants | 3,500,000 | 5,141,779 |
| Share price at grant - pounds | 0.0163 | 0.0036 |
| Exercise price – pounds | 0.0325 | 0.0036 |
| Volatility | 95.50% | 73.09% |
| Dividend yield | nil | nil |
| Risk free investment rate | 0.0079 | 0.0175 |
| Warrant life – years | 3 | 3 |
| Fair value per warrant - pounds | 0.0074 | 0.00175 |

The fair value of share warrants has been recognised in the retained earnings reserve.

The expense for warrants issued alongside convertible loan notes has been treated as a transaction cost and deducted from the loan liability accordingly (see note 11).

The expense recognised in finance costs for the year in relation to the share warrants issued in 2013 is $10,012 (2012: $5,562).

The following is a summary of share options and warrants for the years ended 31 December 2012 and 2013, share-based payment expense for the years ended 31 December 2013 and 2012, and employees, consultants and Director option holdings as of 31 December 2013.

**Awards, expirations and relinquishments**

| | Number of options | Exercise price | Number of warrants | Exercise price |
|---|---|---|---|---|
| Outstanding at 31 December 2011 | 30,916,666 | $0.0217-$0.1164 | - | - |
| Granted | - | - | 3,500,000 | $0.0506 |
| Outstanding at 31 December 2012 | 30,916,666 | $0.0217-$0.1164 | 3,500,000 | $0.0506 |
| Granted | 27,000,000 | $0.0093 | 5,141,779 | $0.0059 |
| Outstanding at 31 December 2013 | 57,916,666 | $0.0093-$0.1164 | 8,641,779 | $0.0059-$0.0506 |
| Weighted average exercise price | | $0.0208 | $0.02084 | $0.0240 |
| Options / warrants vested and exercisable at 31 December 2013 | 7,916,667 | | 8,641,779 | |
| Weighted average fair value of options / warrants granted: | | | | |
| 2013 | | $0.0215 | | $0.0063 |
| 2012 | | $0.0380 | | $0.0114 |

**Share-based payment expense**

The following outlines share-based payment expense in relation to share options for the years ended 31 December 2013 and 2012:

| | 2013 | 2012 |
|---|---|---|
| | $000 | $000 |
| Directors | 111 | 138 |
| Employees | 123 | 73 |
| Total | 234 | 211 |

Share option exercise prices are set in sterling and have been converted to US dollars at the respective year-end exchange rates.

| Year of award | 2013<br>$000 | 2012<br>$000 |
|---|---|---|
| 2011 | 211 | 211 |
| 2013 | 23 | - |
| Total share-based compensation expense | 234 | 211 |

At 31 December 2013 the Group's Officers and Directors held the following options:

| Officer or Director | Number of options held | Expiration dates | Exercise prices £ | Average exercise price £ |
|---|---|---|---|---|
| Keith Morris | 4,000,000 | 7/5/18 | 0.00625 | 0.00625 |
| Tom Milne | 4,000,000 | 7/5/18 | 0.00625 | 0.00625 |
| Mark Smith | 8,000,000 | 9/26/2021– 11/11/2021 | 0.00625 – 0.035 | 0.01406 |
| Total | 16,000,000 | | | |

At 31 December 2012 the Group's Officers and Directors held the following options:

| Officer or Director | Number of options held | Expiration dates | Exercise prices £ | Average exercise price £ |
|---|---|---|---|---|
| Jim Ellerton | 12,116,667 | 9/2/2014 – 11/11/2021 | 0.0175 – 0.065 | 0.0371 |
| Karl Arleth | 6,000,000 | 9/26/2021– 11/11/2021 | 0.0175 – 0.035 | 0.0233 |
| Mark Smith | 4,000,000 | 9/26/2021– 11/11/2021 | 0.0175 – 0.035 | 0.0219 |
| Total | 22,116,667 | | | |

**Shares reserved for employee benefit pool**

During 2005, the Board approved the establishment of an employee benefit and incentive plan. This plan may include cash, a net profits interest from production, stock and other items which the Board may elect to contribute. Distributions to employees will be accumulated and issued at the sole discretion of the Board of Directors of the Group.

## 15. Earnings per share

Basic (loss) / earnings per share is calculated by dividing the (loss) / earnings attributable to common shareholders by the weighted average number of common shares outstanding during the reporting period.

Given the Group's reported loss for the year, share options and warrants are not taken into account when determining the weighted average number of Ordinary Shares in issue during the year and therefore the basic and diluted earnings per share are the same.

**Basic (loss) / earnings per share**

| | 2013 | 2012 |
|---|---|---|
| | $'s | $'s |
| (Loss) / earnings per share | (0.02047) | 0.00004 |

The (loss) / earnings and weighted average number of common shares used in the calculation of basic (loss) / earnings per share are as follows:

| | 2013 | 2012 |
|---|---|---|
| | $000 | $000 |
| (Loss) / earnings used in the calculation of total basic and diluted earnings per share | (13,769) | 21 |

| | 2013 | 2012 |
|---|---|---|
| **Number of common shares** | | |
| Weighted average number of common shares for the purposes of basic (loss) / earnings per share | 672,715,707 | 474,738,877 |

If the Company's share options and warrants were taken into consideration in respect of the Company's weighted average number of common shares for the purposes of diluted earnings per share, it would be as follows:

| | | |
|---|---|---|
| **Number of common shares** | | |
| Dilutive effect of share options and warrants | 47,795,096 | 32,682,988 |
| Weighted average number of common shares for the purposes of diluted (loss) / earnings per share | 720,510,803 | 507,682,865 |

Basic and diluted (loss) / earnings per share have been computed to be substantially the same for the year ended 31 December 2012.

## 16. Leases

The Group has the following minimum future payments on non-cancellable operating leases:

| | 2013 | 2012 |
|---|---|---|
| | $000 | $000 |
| **Buildings** | | |
| Expiring within one year | 10 | 10 |
| **Equipment** | | |
| Expiring within one year | 2 | 2 |

## 17. Events after the balance sheet date

On 17 January 2014, 7,154,724 common shares were issued in settlement of future contractual payments totalling £20,000, equivalent to 0.28 pence per share.

The following conversions of the convertible loan notes (as described in note 11) have taken place since the balance sheet date:

| Date | Principal converted | Price per common share | Number of shares issued |
|---|---|---|---|
| 21 January 2014 | $10,000 | 0.195 pence | 3,128,206 |
| 31 January 2014 | $10,000 | 0.195 pence | 3,128,206 |
| 10 February 2014 | $25,000 | 0.195 pence | 7,820,513 |
| 17 April 2014 | $10,000 | 0.153 pence | 3,986,929 |
| 6 May 2014 | $20,000 | 0.1397 pence | 8,446,671 |
| 9 June 2014 | $15,000 | 0.0995 pence | 9,045,226 |
| 18 June 2014 | $15,000 | 0.0862 pence | 10,259,917 |
| 25 June 2014 | $50,000 | 0.0956 pence | 30,750,308 |

Following the above share issues, the Company has a total of 787,810,441 common shares in issue, and the convertible loan notes principal is reduced to $55,000.

As per announcements made since the balance sheet date, the Directors have been attempting to refinance the Group following the decision by the Bank of the West not to extend the Group's borrowing facilities. The Board evaluated several proposals for refinancing and/or recapitalising the Group, addressing both the demand for repayment by the Bank and seeking additional working capital to support the Group's existing operations in California and Kansas.

The Group settled on a proposal from Hawker Energy in which Hawker would acquire 80% of the Group’s assets in California, thus providing a means to repay the Bank, develop the California assets and provide additional working capital to invest in other opportunities, including the existing Kansas assets, and repay unsecured creditors in an orderly manner.

The Investment will require the approval of Sefton's shareholders ("Shareholders") at a general meeting in accordance with the AIM Rules for Companies.

In the interim, Hawker has been of considerable assistance in dealing with liquidity issues, addressing the concerns of the Bank and providing capital for maintaining facilities in good working order. The Bank has been receptive to the Hawker initiatives while at the same time pursuing its rights under the credit agreement.

The Group has entered into an Inter-creditor Agreement, dated 2 June 2014, with the Bank and Hawker to extend the time available to the Group to repay the Bank in full.

The Inter-creditor Agreement provides for Hawker to advance additional subordinated loans to the Group in two instalments which will fund up to two 30 day extensions of the existing borrowing facilities with the Bank, bringing the aggregate amount of subordinated debt balance up to $1,000,000 (including operational advances and extension payments for June and July). These extension payments advanced to the Group by Hawker will be paid to the Bank in settlement first of accrued interest and then to reduce principal amount of the existing borrowing facilities.

Advances for the first and second 30 day extensions are repayable by the Group to Hawker on 31 July 2014 or will be capitalised on successful conclusion of the Investment.

On June 26, 2014, the subordinated note terms were amended to increase the amount available to be drawn down on the note to $1,500,000 and extend repayment to December 28, 2014 to match the extension of the bank credit facility to that date.

The transaction with Hawker outlined in the most recent letter of intent dated 18 June 2014, (the “Hawker Transaction”) results in the following impact for the Group:

- TEG USA business activities along with related assets and liabilities (including asset retirement obligations) are contributed to a joint venture entity, Tapia LLC
- The Bank debt is settled by Hawker
- The Group receives:
    - 20% interest in Tapia LLC valued at $1.375 Million
    - $3 million deferred consideration providing a quarterly cash inflow to the Group of $250,000

This reflects a lower value than book value of the investment, and the book value at 31 December 2013 has been adjusted to reflect this valuation. However, this transaction will provide for an investment in the property that the Group believes will greatly enhance the value of the TEG USA properties and therefore, the 20% retained by the Group. This value also reflects substantially more value than might accrue to shareholders if the Bank enforces its rights under the loan agreement, appoints a receiver and sells all of the Group’s assets at a fire sale price to clear the loan and accrued interest.

The retained 20% of TEG USA, held in Tapia LLC, will be a passive investment, held for sale within a three to five year window.

**Amended Transaction**

In the period just prior to the date of this Annual Report & Accounts, Hawker advised it would be unable to complete all of the provisions of the Transaction prior to the EGM. Discussions commenced with the Bank about extension of the time to repay to accommodate the EGM and short term funding issues. Other banks were also approached about replacing the Bank credit facility. On June 26, 2014, the Bank agreed to an extension of the final repayment date to December 28, 2014, subject to the following conditions:

- An immediate instalment payment of $360,000 to be applied, in order, to an extension fee, attorney's fees incurred by the Bank, default interest and penalties and principal
- A monthly payment of $100,000 plus interest at 8% beginning July 31, 2014
- Full repayment of balance owing on or before December 28, 2014
- Legal fees of $20,000 per month during the forbearance period

Hawker has made the payment of $360,000 on June 27, 2014. Instalment payments beginning July would be sourced first from TEG USA oil sale revenue with additional funding provided by Hawker if required.

The Group is confident that it can comply with these terms and conditions. The Group fully expects to refinance the credit facility from one or more of the alternatives being presented by competing financial institutions. Hawker will provide additional funds if required and intends to provide further working capital to TEG USA to increase oil production in California.

## 18. Contingent liabilities

The Group and its former CEO and Chairman, Mr. Ellerton, have commenced arbitration proceedings in respect of the termination of his consultancy agreement. The Board has chosen legal counsel and arbitrator for this process. In particular, we confirm that, in the opinion of the Board, no provision is required as we are confident that the arbitrator will find in the Group's favour. Adequate provision has been made in relation to potential legal costs regarding this matter.