Zeta Petroleum Limited

Report and Financial Statements

Year Ended 31 December 2007

ZETA PETROLEUM LIMITED

REPORT AND FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007

Page:

GENERAL INFORMATION

Directors

J A Rutland (Chairman)
C C G Lewis (Chief Executive)
S P West
T W Osborne

Company Secretary

S P West

Registered Office

1 Berkeley Street
London
W1J 8DJ
United Kingdom

Company Number

5560854

Auditor

Ernst & Young LLP
1 More London Place
London
SE1 2AF
United Kingdom

REPORT OF THE DIRECTORS FOR THE YEAR ENDED 31 DECEMBER 2007

The directors present their report together with the audited financial statements for the year ended 31 December 2007.

Results and Dividends

The consolidated income statement is set out on page 8 and shows a loss for the year amounting to £2,775,000 (2006 – loss of £1,562,000 for the period). The directors do not recommend the payment of a dividend.

Principal Activities and Review of Operations

The principal activities of the Group are oil and gas exploration, development and production.

On 15 January 2007 the Group acquired a 100% interest in the Bobocu licence in Romania. A concession agreement was signed with the Romanian National Agency for Minerals and Resources ("NAMR") on 27 March 2007 and was fully ratified on 19 December 2007.

On 31 March 2007 the Group entered into a farm-out agreement with a third party ("Farmee") whereby, subject to certain conditions, the Farmee is committed to invest up to US$4.5 million in the Bartin licences in Turkey and in return the Group agreed to transfer 50.5% of its 70% interest in the Bartin licences to the Farmee. In accordance with the terms of the farm-out agreement, the Group retained a 19.5% effective interest in the Bartin licences.

On 18 May 2007 the Bartin-2 exploration well commenced drilling and was completed on 15 July 2007. In accordance with the farm-out agreement signed on 31 March 2007 the Group was liable for 19.5% of any approved drilling costs above US$2 million. The final approved cost of the well was approximately US$3.4 million and therefore the cost to the Group of drilling the well was US$273,082.

On 8 June 2007 the Company was appointed Operator of the Duzce/Sakarya licences in Turkey and on 14 June 2007 the Company's 70% interest in the Duzce/Sakarya licences was formally approved by the General Directorate of Petroleum Affairs in Turkey.

On 27 August 2007 the Group signed concession agreements with NAMR for the Padureni licence and Jimbolia licence in Romania. These concession agreements are now passing through the ministerial approval process, which is expected to conclude in early 2008.

In September/October 2007 the Group drilled and tested the Baleni-1 appraisal well on the partitioned Zegujani licence in Romania. The total cost of the well was approximately US$1.95 million and under the terms of the Group's Zegujani farm-out agreement the Group's share of this cost was US$1,657,500. The Group now holds a 35% interest in the partitioned Zegujani licence and has an option to acquire an additional 15% interest.

In November 2007 the Company commenced a 2D seismic acquisition programme in the Duzce/Sakarya licences. Under the terms of the Company's Duzce/Sakarya farm-out agreement the Company will fund the total cost of this programme which is expected to be approximately US$2.14 million.

During 2007 the Company raised £2,098,968 (net of expenses) through the issue of new ordinary shares to fund the 2D seismic work programme in Turkey, an audit of the 2P reserves for the Bobocu gas field in Romania and ongoing working capital costs.

The subsidiary undertakings principally affecting the profits or net assets of the Group are listed in Note 12 to the consolidated financial statements.

REPORT OF THE DIRECTORS FOR THE YEAR ENDED 31 DECEMBER 2007

Principal Risks and Uncertainties

As an exploration, development and production company in the oil and gas industry the Company operates in an inherently risky sector and faces a large number of risks including:

Discovery Risk:	Risk that no economically producible oil or gas will be discovered or found to be present in the Group's licence areas.
Capital Intensive Business:	The drilling of wells to discover whether there is oil or gas is a highly capital intensive business and will require the Company to raise capital in the future.
Natural Gas Price:	The Company's asset value and economic viability of its exploration projects depend on the price of natural gas. The Company's ability to raise funds in the future is therefore likely to be sensitive to the price of natural gas.
Environmental Regulations:	The Group's operations are subject to the environmental risks inherent in the oil and gas industry.

Post Balance Sheet Events

Post balance sheet events are disclosed in Note 23 to the consolidated financial statements.

Share Capital

Details of the Company's authorised and issued share capital as at 31 December 2007 and of shares issued during the year are set out in Note 16 to the consolidated financial statements.

Policy and Practice on Payment of Creditors

It is the Company's policy that payments to suppliers are made in accordance with those terms and conditions agreed between the Company and its suppliers, providing that all trading terms and conditions have been complied with.

Directors and Directors' Interests

The directors who held office at 31 December 2007 had the following interests in the ordinary shares of the Company according to the register of directors' interests:

	Class of Share	Interest at start of year	Interest at end of year
C C G Lewis (appointed 12.09.05)	Ordinary	553,200	553,200
S P West (appointed 12.09.05)[1]	Ordinary	412,000	419,000
T W Osborne (appointed 31.03.06)	Ordinary	-	-
J A Rutland (appointed 25.05.06)	Ordinary	2,306	3,147

[1] S P West's interest is indirect as all the shares are owned by Cresthaven Investments Limited, a company in which S P West has an indirect beneficial interest.

REPORT OF THE DIRECTORS FOR THE YEAR ENDED 31 DECEMBER 2007

According to the register of directors' interests, no rights to subscribe for shares in or debentures of Group companies were granted to any of the directors or their immediate families, or exercised by them, during the financial year except as indicated below:

Date of grant	Number of options at start of year	Options granted during the year	Number of options at the end of the year	Exercise price	Date from which exercisable	Expiry date
C C G Lewis						
29.03.06	50,000	-	50,000	£2.8736	29.03.07	29.03.16
29.03.06	50,000	-	50,000	£2.8736	29.09.07	29.03.16
	100,000	-	100,000			
S P West						
29.03.06	50,000	-	50,000	£2.8736	29.03.07	29.03.16
29.03.06	50,000	-	50,000	£2.8736	29.09.07	29.03.16
	100,000	-	100,000			
J A Rutland						
13.06.06	13,920	-	13,920	£2.8736	13.06.07	13.06.16
13.06.06	13,920	-	13,920	£2.8736	13.12.07	13.06.16
05.11.07	-	8,771	8,771	£2.8736	05.11.08	05.11.17
05.11.07	-	8,770	8,770	£2.8736	05.05.09	05.11.17
	27,840	17,541	45,381			

Substantial Shareholders

The following parties had interests of greater than 3% of the issued share capital of the Company at 31 December 2007:

	Number of shares	% of issued ordinary share capital
GM Investment & Co Limited	849,844	31.07
C C G Lewis	553,200	20.22
S Pagel	422,793	15.46
Cresthaven Investments Limited[2]	419,000	15.32
WCI Overseas Oil & Gas LLC	191,400	7.00
AM2 (Bermuda) Limited	104,400	3.82

[2] Cresthaven Investments Limited is a company in which S P West has an indirect beneficial interest.

Statement of Directors' Responsibilities

The directors are responsible for preparing the consolidated and company financial statements in accordance with applicable United Kingdom law and those International Financial Reporting Standards as adopted by the European Union.

The directors are required to prepare consolidated and company financial statements for each financial year which present fairly the financial position of the Group and Company, and the financial performance and cash flows of the Group and Company for the period. In preparing those financial statements the directors are required to:

- select suitable accounting policies in accordance with IAS 8: *Accounting Policies, Changes in Accounting Estimates and Errors* and then apply them consistently;

REPORT OF THE DIRECTORS FOR THE YEAR ENDED 31 DECEMBER 2007

- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements in IFRSs is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Group's and/or Company's financial position and performance; and
- state that the Group and Company have complied with IFRSs, subject to any material departures disclosed and explained in the financial statements.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Group and Company and enable them to ensure that the consolidated and company financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Statement as to Disclosure of Information to Auditors

The directors who were members of the board at the time of approving the directors' report are listed on page 1. Having made inquiries of fellow directors and of the Company's auditors, each of these directors confirm that:

- to the best of each director's knowledge and belief, there is no information relevant to the preparation of their report of which the Company's auditors are unaware; and
- each director has taken all the steps a director might reasonably be expected to have taken to be aware of relevant audit information and to establish that the Company's auditors are aware of that information.

Political and Charitable Contributions

The Group made no political contributions or donations to United Kingdom charities during the period.

Auditors

A resolution reappointing Ernst & Young LLP as auditors was passed at the Company's first annual general meeting on 22 March 2007.

By order of the Board

S P West
Director
7 March 2008

1 Berkeley Street
London W1J 8DJ
United Kingdom

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF ZETA PETROLEUM LIMITED

We have audited the Group and parent company financial statements of Zeta Petroleum Limited for the year ended 31 December 2007 which comprise the Consolidated Income Statement, the Consolidated and Company Balance Sheets, the Consolidated and Company Cash Flow Statements, the Consolidated and Company Statements of Changes in Equity and the related notes 1 to 23. These financial statements have been prepared under the accounting policies set out therein.

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

Respective responsibilities of directors and auditors

The directors’ responsibilities for preparing the consolidated and Company financial statements in accordance with applicable United Kingdom law and International Financial Reporting Standards (IFRSs) as adopted by the European Union are set out in the Statement of Directors’ Responsibilities on pages 4 and 5.

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

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

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

We read the directors’ report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies within it. Our responsibilities do not extend to any other information.

Basis of audit opinion

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

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

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF ZETA PETROLEUM LIMITED (CONTINUED)

Opinion

In our opinion:

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

Ernst & Young LLP

Ernst & Young LLP
Registered auditor
London
7 March 2008

CONSOLIDATED INCOME STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2007

	Note	**2007** **£'000**	2006 £'000
Continuing operations			
Revenue	2	**53**	1
Cost of goods sold		**(28)**	-
Gross profit		**25**	1
Exploration and evaluation expenses		**(1,498)**	(877)
Administrative expenses		**(1,392)**	(786)
Operating loss	4	**(2,865)**	(1,662)
Interest income		**90**	100
Loss before taxation		**(2,775)**	(1,562)
Taxation	8	-	-
Loss for the year attributable to the equity holders		**(2,775)**	(1,562)
Loss per ordinary share – basic	9	**112.54p**	93.15p

CONSOLIDATED BALANCE SHEET
AS AT 31 DECEMBER 2007

	Note	2007 £'000	2006 £'000
ASSETS			
Non-current assets			
Intangible assets	10	**711**	85
Property, plant & equipment	11	**28**	8
		739	93
Current assets			
Trade and other receivables	14	**541**	63
Prepayments and accrued income		**9**	81
Cash and cash equivalents	13	**1,735**	2,478
		2,285	2,622
Total assets		**3,024**	2,715
EQUITY AND LIABILITIES			
Equity attributable to equity holders			
Issued capital	16	**3**	2
Share premium	17	**6,008**	3,910
Share options reserve	18	**606**	337
Foreign currency translation reserve		**5**	-
Retained losses		**(4,337)**	(1,562)
Total equity		**2,285**	2,687
Current liabilities			
Trade and other payables	15	**739**	28
Total liabilities		**739**	28
Total equity and liabilities		**3,024**	2,715

Stephen West, Finance Director
7 March 2008

COMPANY BALANCE SHEET
AS AT 31 DECEMBER 2007

	Note	2007 £'000	2006 £'000
ASSETS			
Non-current assets			
Intangible assets	10	**2**	10
Property, plant & equipment	11	**23**	4
Investment in subsidiary	12	**1**	1
Other receivables		**2,160**	129
		2,186	144
Current assets			
Trade and other receivables	14	**73**	46
Prepayments and accrued income		**8**	80
Cash and cash equivalents	13	**1,722**	2,473
		1,803	2,599
Total assets		**3,989**	2,743
EQUITY AND LIABILITIES			
Equity attributable to equity holders			
Issued capital	16	**3**	2
Share premium	17	**6,008**	3,910
Share options reserve	18	**606**	337
Retained losses		**(3,254)**	(1,532)
Total equity		**3,363**	2,717
Current liabilities			
Trade and other payables	15	**626**	26
Total liabilities		**626**	26
Total equity and liabilities		**3,989**	2,743

Stephen West, Finance Director
7 March 2008

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 DECEMBER 2007

	Issued Capital £'000	Share Premium £'000	Share Options Reserve £'000	Foreign Currency Translation Reserve £'000	Retained Losses £'000	Total £'000
As at 1 January 2007	2	3,910	337	-	(1,562)	2,687
Issue of share capital	1	2,236	-	-	-	2,237
Transaction costs of issue of shares	-	(138)	-	-	-	(138)
Issue of share options	-	-	269	-	-	269
Movement in reserve	-	-	-	5	-	5
Loss for the year	-	-	-	-	(2,775)	(2,775)
At 31 December 2007	**3**	**6,008**	**606**	**5**	**(4,337)**	**2,285**

COMPANY STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 DECEMBER 2007

	Issued Capital £'000	Share Premium £'000	Share Options Reserve £'000	Retained Losses £'000	Total £'000
As at 1 January 2007	2	3,910	337	(1,532)	2,717
Issue of share capital	1	2,236	-	-	2,237
Transaction costs of issue of shares	-	(138)	-	-	(138)
Issue of share options	-	-	269	-	269
Loss for the year	-	-	-	(1,722)	(1,722)
At 31 December 2007	**3**	**6,008**	**606**	**(3,254)**	**3,363**

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY FOR THE PERIOD ENDED 31 DECEMBER 2006

	Issued Capital £'000	Share Premium £'000	Share Options Reserve £'000	Foreign Currency Translation Reserve £'000	Retained Losses £'000	Total £'000
As at 12 September 2005	-	-	-	-	-	-
Issue of share capital	2	4,195	-	-	-	4,197
Transaction costs of issue of shares	-	(285)	-	-	-	(285)
Issue of share options	-	-	337	-	-	337
Loss for the period	-	-	-	-	(1,562)	(1,562)
At 31 December 2006	2	3,910	337	-	(1,562)	2,687

COMPANY STATEMENT OF CHANGES IN EQUITY FOR THE PERIOD ENDED 31 DECEMBER 2006

	Issued Capital £'000	Share Premium £'000	Share Options Reserve £'000	Retained Losses £'000	Total £'000
As at 12 September 2005	-	-	-	-	-
Issue of share capital	2	4,195	-	-	4,197
Transaction costs of issue of shares	-	(285)	-	-	(285)
Issue of share options	-	-	337	-	337
Loss for the period	-	-	-	(1,532)	(1,532)
At 31 December 2006	2	3,910	337	(1,532)	2,717

CONSOLIDATED CASH FLOW STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2007

	2007	2006
	£'000	£'000
Operating activities		
Loss before tax from continuing operations	**(2,775)**	(1,562)
Adjustments to reconcile loss to net cash outflow from operating activities		
Non-cash:		
Depreciation	**6**	5
Amortisation	**63**	15
Share based payments	**269**	337
Write-off of exploration and evaluation costs	**1,498**	877
Interest income	**(90)**	(100)
Working capital adjustments:		
Increase in trade and other receivables	**(477)**	(63)
Decrease/(increase) in prepayments and accrued income	**75**	(81)
Increase in trade and other payables	**711**	28
Net cash outflow from operating activities	**(720)**	(544)
Investing activities		
Purchase of property, plant and equipment	**(26)**	(13)
Purchase of intangible assets	**(687)**	(100)
Exploration and evaluation costs	**(1,498)**	(877)
Interest received	**90**	100
Net cash used in investing activities	**(2,121)**	(890)
Financing activities		
Proceeds from issue of shares	**2,236**	4,197
Transaction costs for issue of shares	**(138)**	(285)
Net cash inflow from financing activities	**2,098**	3,912
Net (decrease)/increase in cash and cash equivalents	**(743)**	2,478
Cash and cash equivalents at 1 January 2007	**2,478**	-
Cash and cash equivalents at 31 December 2007	**1,735**	2,478

COMPANY CASH FLOW STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2007

	2007 £'000	2006 £'000
Operating activities		
Loss before tax from continuing operations	**(1,722)**	(1,532)
Adjustments to reconcile loss to net cash outflow from operating activities		
Non-cash:		
Depreciation	**5**	5
Amortisation	**9**	13
Share based payments	**269**	337
Write-off of exploration and evaluation costs	**679**	864
Interest income	**(90)**	(100)
Working capital adjustments:		
Increase in trade and other receivables	**(27)**	(46)
Decrease/(increase) in prepayments and accrued income	**73**	(80)
Increase in trade and other payables	**600**	26
Net cash outflow from operating activities	**(204)**	(513)
Investing activities		
Purchase of property, plant and equipment	**(24)**	(9)
Purchase of intangible assets	**(1)**	(23)
Exploration and evaluation costs	**(679)**	(864)
Purchase of shares in subsidiary	**-**	(1)
Interest received	**90**	100
Loans to subsidiary	**(2,031)**	(129)
Net cash used in investing activities	**(2,645)**	(926)
Financing activities		
Proceeds from issue of shares	**2,236**	4,197
Transaction costs for issue of shares	**(138)**	(285)
Net cash inflow from financing activities	**2,098**	3,912
Net (decrease)/increase in cash and cash equivalents	**(751)**	2,473
Cash and cash equivalents at 1 January 2007	**2,473**	-
Cash and cash equivalents at 31 December 2007	**1,722**	2,473

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007

1. Accounting policies

1.1 Authorisation of financial statements and statement of compliance with IFRSs

Zeta Petroleum Limited ("Zeta" or the "Company"), the ultimate parent of the Group, is a private company incorporated in England. The registered office and principal place of business is 1 Berkeley Street, London, W1J 8DJ. The principal activities of Zeta and its subsidiary (the Group) are oil and gas exploration, development and production.

The Group's consolidated financial statements for the year ended 31 December 2007 were authorised for issue by the board of directors on 7 March 2008 and the balance sheets were signed on the Board's behalf by S P West.

The Group's consolidated financial statements and the Company's financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. The principal accounting policies adopted by the Group are set out below.

1.2 Basis of preparation

The consolidated financial statements of Zeta have been prepared on a historical cost basis. The consolidated financial statements are presented in British pounds and all values are rounded to the nearest thousand (£000) except when otherwise indicated.

Zeta Petroleum Ltd was incorporated on 12 September 2005. The comparative 2006 figures shown in the consolidated financial statements cover the period from 12 September 2005 to 31 December 2006.

1.3 Basis of consolidation

The consolidated financial statements comprise the financial statements of Zeta and its subsidiary as at 31 December 2007. The financial statements of the subsidiary are prepared for the same reporting period as the parent company, using consistent accounting policies.

All intra-group balances, transactions, income and expenses and profits and losses resulting from intra-group transactions that are recognised in assets, are eliminated in full.

Subsidiary is fully consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases.

Zeta has used the exemption granted under s230(1)(b) of the Companies Act 1985 that allows for the non-disclosure of the Income Statement of the parent company. The loss attributable to Zeta for the year ended 31 December 2007 was £1,722,000 (2006: £1,532,000).

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007

1.4 Changes in accounting policy and disclosures

The accounting policies adopted are consistent with those of the previous financial year except as follows:

The Group has adopted the following new and amended IFRS and IFRIC interpretations during the year. Adoption of these revised standards and interpretations did not have any effect on the financial performance or position of the Group. They did however give rise to additional disclosures, including in some cases, revisions to accounting policies:

IFRS 7 – Financial Instruments: Disclosures
This standard requires disclosures that enable users of the financial statements to evaluate the significance of the Group's financial instruments and the nature and extent of risks arising from those financial instruments. The new disclosures are included throughout the financial statements. While there has been no effect on the financial position or results, comparative information has been revised where needed.

IAS 1 – Presentation of Financial Statements (amendment)
This amendment requires the Group to make new disclosures to enable users of the financial statements to evaluate the Group's objectives, policies and processes for managing capital. These new disclosures are shown in Note 22.

IFRIC 8 – Scope of IFRS 2
This interpretation requires IFRS 2 to be applied to any arrangements in which the entity cannot identify specifically some or all of the goods received, in particular where equity instruments are issued for consideration which appears to be less than fair value. As equity instruments are only issued to employees in accordance with the employee share scheme, the interpretation had no impact on the financial position or performance of the Group.

1.5 Joint ventures

The Group has a number of contractual arrangements with other parties which represent joint ventures.

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

Where a Group company undertakes its activities under joint venture arrangements, the Group's share of jointly and directly controlled assets and any liabilities incurred jointly with other ventures are recognised and classified according to their nature. The Group's share of joint venture expenses are recognised when it is probable that the economic benefits associated with the transactions will flow from the Group and their amounts can be measured reliably.

1.6 Foreign currencies

The consolidated financial statements are presented in British pounds, which is the Company's functional and presentational currency. Each entity in the Group translates foreign currency transactions into its functional currency at the rate of exchange prevailing at the transaction date. Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency at the rate of exchange prevailing at the Balance Sheet date. Exchange differences arising are taken to the Income Statement.

The functional currency of the foreign subsidiary Zeta Petroleum (Romania) SRL is Romanian New Lei (RON). Zeta translates the subsidiary accounts into the presentational currency using the closing rate method for assets and liabilities, which are translated into British pounds at the rate of exchange prevailing at the Balance Sheet date, and the weighted average exchange rate for the period for Income Statement accounts. Exchange differences arising on the translation of net assets of the subsidiary are taken to reserves.

1.7 Intangible Assets

Oil and gas exploration assets
Zeta follows the successful efforts based accounting policy for oil and gas assets. The successful efforts method means that only costs which relate directly to the discovery and development of specific oil and gas reserves are capitalised.

Costs incurred prior to obtaining the legal rights to explore an area are expensed immediately to the Income Statement.

Expenditure incurred on the acquisition of a licence interest is initially capitalised on a licence by licence basis and amortised on a straight-line basis over the estimated period of exploration and, in the event that no future activity is planned, the remaining balance of licence acquisition costs is written off. Should a discovery be made, the amortisation would be suspended and the remaining costs aggregated with exploration expenditure on a field by field basis as properties awaiting approval for development. When development is approved, the relevant expenditure is transferred to tangible assets.

Exploration expenditure incurred in the process of determining exploration targets is capitalised initially within exploration assets and subsequently allocated to drilling activities. Exploration drilling costs are initially capitalised on a well by well basis until the success or otherwise of the well has been established. The success or failure of each exploration effort is judged on a well by well basis. Drilling costs are written off on completion of a well unless the results indicate that hydrocarbon reserves exist and there is a reasonable prospect that these reserves are commercial.

Following appraisal of successful exploration wells, if commercial reserves are established and technical feasibility for extraction demonstrated, then the related capitalised exploration costs are transferred into a single field cost centre within development/producing assets after testing for impairment. Where results of exploration drilling indicate the presence of hydrocarbons which are ultimately not considered commercially viable, all related costs are written off to the Income Statement.

All costs incurred after the technical feasibility and commercial viability of producing hydrocarbons has been demonstrated are capitalised within development/producing assets on a field by field basis.

Subsequent expenditure is capitalised only where it either enhances the economic benefits of the development/producing assets or replaces part of the existing development/producing asset. Any costs remaining associated with the part replaced are expensed.

Software costs

Software costs are carried within intangible assets at cost, less any accumulated amortisation and accumulated impairment losses.

Amortisation is charged so as to write off the cost over the estimated useful lives (1 to 3 years) using the straight-line method.

1.8 Property, plant and equipment

Property, plant and equipment are carried at cost, less any accumulated depreciation and accumulated impairment losses. Cost includes purchase price and construction costs for qualifying assets and borrowing costs capitalised in accordance with the Group's accounting policy. Depreciation of these assets commences when the assets are ready for their intended use.

Depreciation is charged so as to write off the cost, less estimated residual value, over their estimated useful lives using the straight-line method, for the following classes of assets: computer equipment (3 years) and other equipment (1 to 5 years).

The estimated useful lives of property, plant and equipment and their residual values are reviewed on an annual basis and, if necessary, changes in useful lives are accounted for prospectively.

The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in the Income Statement for the relevant period.

1.9 Impairment of intangible assets and property, plant and equipment

At each balance sheet date, the Group reviews the carrying amounts of its intangible assets and property, plant and equipment to determine whether there is any indication that those assets have suffered an impairment loss. Individual assets are grouped together as a cash-generating unit for impairment assessment purposes at the lowest level of their identifiable cash flows, where these are largely independent of the cash flows of the other Group assets. In the case of exploration assets this will normally be at a field by field level.

If any such indication of impairment exists the Group makes an estimate of the recoverable amount of the asset or cash generating unit. The recoverable amount is the higher of its fair value less costs to sell and its value in use. Where the carrying amount of an individual asset or a cash-generating unit exceeds its recoverable amount, the asset/cash-generating unit is considered impaired and is written down to its recoverable amount. In accessing the value in use, the estimated future cash flows are adjusted for the risks specific to the asset/cash-generating unit and are discounted to their present value at a rate that reflects the current market indicators.

Where an impairment loss subsequently reverses, the carrying amount of the asset/cash-generating unit is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset/cash-generating unit in prior years. A reversal of an impairment loss is recognised as income immediately.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007

1.10 Impairment of financial assets

The Group assesses at each balance sheet date whether a financial asset is impaired and will recognise the impairment loss immediately through the income statement.

1.11 Cash and cash equivalents

Cash and cash equivalents comprise cash in hand and current balances with banks and similar institutions, which are readily convertible to known amounts of cash. Cash equivalents are short-term with an original maturity of less than 3 months, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

1.12 Trade and other receivables

Trade receivables are recognised and carried at the lower of their original invoiced value and recoverable amount. Other debtors are recognised and measured at nominal value.

1.13 Share-based payments

Share options

The Group issues equity-settled share-based payments to the directors and senior management ("Employee Share Options") and to its corporate finance advisers for assistance in raising private equity ("Non-employee Share Options"). Equity-settled share-based payments are measured at fair value at the date of grant for Employee Share Options and the date of service for Non-employee Share Options. The fair value determined at the grant date or service date, as applicable, of the equity-settled share-based payments is expensed, with a corresponding credit to equity, on a straight-line basis over the vesting period, based on the Group's estimate of shares that will eventually vest. At each subsequent balance sheet date the Group calculates the estimated cumulative charge for each award having regard to any change in the number of options that are expected to vest and the expired portion of the vesting period. The change in this cumulative charge since the last balance sheet date is expensed with a corresponding credit being made to equity. Once an option vests, no further adjustment is made to the aggregate amount expensed. The fair value is calculated using the Black Scholes method. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of non-transferability exercise restrictions and behavioural considerations. The market price used in the model is the issue price of Company shares at the last placement of shares immediately preceding the calculation date. The fair values calculated are inherently subjective and uncertain due to the assumptions made and the limitation of the calculations used.

1.14 Taxation

Income tax expense represents the sum of the current tax payable and deferred tax.

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

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

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

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

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset realised based on tax rates and laws substantively enacted by the balance sheet date.

Deferred tax is charged or credited in the income statement, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

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

1.15 Investments and other financial assets

Financial assets within the scope of IAS 39 are classified as either financial assets at fair value through profit or loss, loans and receivables, held to maturity investments, and available for sale financial assets, as appropriate. When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs. The Group considers whether a contract contains an embedded derivative when the entity first becomes a party to it. The embedded derivatives are separated from the host contract which is not measured at fair value through profit or loss when the analysis shows that the economic characteristics and risks of embedded derivatives are not closely related to those of the host contract.

The Group determines the classification of its financial assets after initial recognition and, where allowed and appropriate, re-evaluates this designation at each financial year end.

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss includes financial assets held for trading and financial assets designated upon initial recognition as at fair value through profit and loss.

Financial assets are classified as held for trading if they are acquired for the purpose of selling in the near term. Derivatives, including separated embedded derivatives are also classified as held for trading unless they are designated as effective hedging instruments or a financial guarantee contract. Gains or losses on investments held for trading are recognised in profit and loss.

Financial assets may be designated at initial recognition as at fair value through profit or loss if the following criteria are met: (i) the designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the assets or recognising gains or losses on them on a different basis; or (ii) the assets are part of a group of financial assets which are managed and their performance evaluated on a fair value basis, in accordance with a documented risk management strategy; or (iii) the financial asset contains an embedded derivative that would need to be separately recorded. As at 31 December 2007, no financial assets have been designated as at fair value through profit and loss.

Held-to-maturity investments

Held-to-maturity investments are non-derivative financial assets which carry fixed or determinable payments and fixed maturities and which the Group has the positive intention and ability to hold to maturity. After initial measurement held to maturity investments are measured at amortised cost. This cost is computed as the amount initially recognised minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initially recognised amount and the maturity amount, less allowance for impairment. This calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums and discounts. Gains and losses are recognised in the income statement when the investments are derecognised or impaired, as well as through the amortisation process. As at 31 December 2007, the Company had no held-to-maturity investments.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement loans and receivables are subsequently carried at amortised cost using the effective interest method less any allowance for impairment. Amortised cost is calculated taking into account any discount or premium on acquisition and includes fees that are an integral part of the effective interest rate and transaction costs. Gains and losses are recognised in the income statement when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

Available-for-sale financial investments

Available-for-sale financial assets are those non-derivative financial assets that are designated as available-for-sale or are not classified in any of the three preceding categories. After initial measurement, available for sale financial assets are measured at fair value with unrealised gains or losses being recognised directly in equity in the net unrealised gains reserve. When the investment is disposed of, the cumulative gain or loss previously recorded in equity is recognised in the income statement. Interest earned or paid on the investments is reported as interest income or expense using the effective interest rate. Dividends earned on investments are recognised in the income statement as 'Dividends received' when the right of payment has been established. As at 31 December 2007, the Company had no available-for-sale financial investments.

Fair value

The fair value of investments that are actively traded in organised financial markets is determined by reference to quoted market bid prices at the close of business on the balance sheet date. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm's length market transactions; reference to the current market value of another instrument, which is substantially the same; discounted cash flow analysis or other valuation models.

1.16 Revenue recognition

Sales of oil and gas products are recognised when the significant risks and rewards of ownership have passed to the buyer and it can be reliably measured. Other services are recognised when the services have been performed. Revenue is measured at the fair value of the consideration received, excluding discounts, rebates, VAT and other sales taxes or duty.

Interest income is recognised as the interest accrues, by reference to the net carrying amount at the effective interest rate applicable.

1.17 Trade payables

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

1.18 Share issue expenses and share premium account

Costs of share issues are written off against the premium arising on the issue of share capital.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007

2. Revenue

Revenue received is entirely attributable to other services provided by the Company to the joint venture operations in Turkey and Romania.

3. Segment information

For the purposes of segmental information the primary segment reporting format is determined to be the business segment. The Group has one class of business, the exploration, development and production of oil and gas. No further disclosure is required in relation to primary segment reporting in this note as all the relevant disclosure is already detailed throughout the Group financial statements.

Secondary segment information is reported geographically. The Group's geographical segments are United Kingdom, Turkey and Romania.

Group revenue for the year ended 31 December 2007 is entirely attributable to the United Kingdom and Romanian geographical segments.

The following tables present expenditure and certain asset information regarding the Group's geographical segments for the year ended 31 December 2007:

Segment assets	**2007 £'000**	2006 £'000
United Kingdom	**1,798**	2,586
Turkey	**32**	27
Romania	**1,194**	102
	3,024	2,715

Capital expenditure	**2007 £'000**	2006 £'000
United Kingdom	**24**	32
Turkey	**679**	864
Romania	**1,509**	94
	2,212	990

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007

4. Operating loss

Operating loss is stated after charging/(crediting):

	GROUP		COMPANY	
	2007	2006	**2007**	2006
	£'000	£'000	**£'000**	£'000
Amortisation (note 10)	**63**	15	**9**	13
Depreciation (note 11)	**6**	5	**5**	5
Net foreign exchange differences	**(80)**	10	**(11)**	9
Interest Income	**(90)**	(100)	**(90)**	(100)

5. Auditors' remuneration

	GROUP		COMPANY	
	2007	2006	**2007**	2006
	£'000	£'000	**£'000**	£'000
Audit of the financial statements	**20**	15	**20**	15
Other fees to auditors:				
- Taxation services	-	1	-	-
	20	16	**20**	15

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007

6. Employment costs

	GROUP		COMPANY	
	2007	2006	**2007**	2006
	£'000	£'000	**£'000**	£'000
Wages and salaries	**313**	127	**305**	127
Social security costs	**36**	14	**36**	14
Share based payments arising from equity-settled share based payment transactions	**227**	272	**227**	272
	576	413	**568**	413

The weighted average number of employees (including executive directors) during the year was:

	GROUP		COMPANY	
	2007	2006	**2007**	2006
Management	**3**	2	**2**	2
Administration	**1**	-	**1**	-
	4	2	**3**	2

7. Remuneration of Directors

Group and Company:	**2007** **£'000**	2006 £'000
Basic salary and fees	**172**	127
Share based payments	**175**	255
	347	382

Details of interests in share options for each director are set out in the Directors Report on page 4.

8. Taxation

The tax charge for the year is £nil. The tax charge is calculated as follows:

	2007	2006
	£'000	£'000
Accounting loss before tax	**(2,775)**	(1,562)
Tax at domestic rate of corporation tax of 30%	**(832)**	(469)
Disallowed expenses and non-taxable income	**77**	6
Share options issued	**81**	101
Non-qualifying depreciation and amortisation	**257**	7
Effect of lower tax rates in Romania	**18**	2
Unrecognised tax losses	**399**	353
	-	-

The Directors do not consider it appropriate to provide for any deferred tax asset to reflect the potential benefit arising from temporary differences at 31 December 2007. At 31 December 2007 there were unprovided deferred tax assets in respect of tax losses carried forward of approximately £751,739 (2006: £352,532).

9. Loss per share

Basic loss per share is calculated on the loss for the year attributable to equity holders of the parent of £2,775,000 (2006: £1,562,000) and divided by the weighted average of 2,465,743 (2006: 1,677,102) ordinary shares.

As the exercise of options would be anti-dilutive no diluted earnings per share figure has been provided.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007

10. Intangible assets

GROUP	Licence Acquisition Costs £'000	Exploration and Evaluation £'000	Software Costs £'000	Total £'000
Cost:				
As at 12 September 2005	-	-	-	-
Additions	77	877	23	977
Unsuccessful exploration and evaluation	-	(877)	-	(877)
At 31 December 2006	77	-	23	100
Amortisation:				
As at 12 September 2005	-	-	-	-
Provided in the period (see note 4)	(2)	-	(13)	(15)
At 31 December 2006	(2)	-	(13)	(15)
Net book value at 31 December 2006	75	-	10	85
Cost:				
As at 1 January 2007	**77**	**-**	**23**	**100**
Additions	**687**	**1,498**	**2**	**2,187**
Unsuccessful exploration and evaluation	**-**	**(1,498)**	**-**	**(1,498)**
At 31 December 2007	**764**	**-**	**25**	**789**
Amortisation:				
As at 1 January 2007	**(2)**	-	**(13)**	**(15)**
Provided in the period (see note 4)	**(53)**	-	**(10)**	**(63)**
At 31 December 2007	**(55)**	**-**	**(23)**	**(78)**
Net book value at 31 December 2007	**709**	**-**	**2**	**711**

Acquisition of the Bobocu licence, Romania

On 15 January 2007 Zeta Petroleum (Romania) SRL acquired the Bobocu licence in Romania. This licence was ratified by the Romanian government on 19 December 2007. The carrying amount of this licence as at 31 December 2007 is £586,576. Amortisation will commence once the work programme enters the production phase and will be calculated on the basis of estimated remaining reserves.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007

10. Intangible assets *continued*

COMPANY	Exploration and Evaluation £'000	Software Costs £'000	Total £'000
Cost:			
As at 12 September 2005	-	-	-
Additions	864	23	887
Unsuccessful exploration and evaluation	(864)	-	(864)
At 31 December 2006	-	23	23
Amortisation:			
As at 12 September 2005	-	-	-
Provided in the period (see note 4)	-	(13)	(13)
At 31 December 2006	-	(13)	(13)
Net book value at 31 December 2006	-	10	10
Cost:			
As at 1 January 2007	**-**	**23**	**23**
Additions	**679**	**1**	**680**
Unsuccessful exploration and evaluation	**(679)**	**-**	**(679)**
At 31 December 2007	**-**	**24**	**24**
Amortisation:			
As at 1 January 2007	-	**(13)**	**(13)**
Provided in the period (see note 4)	-	**(9)**	**(9)**
At 31 December 2007	**-**	**(22)**	**(22)**
Net book value at 31 December 2007	**-**	**2**	**2**

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007

11. Property, plant and equipment

	GROUP		COMPANY	
	2007	2006	**2007**	2006
	£'000	£'000	**£'000**	£'000
Cost:				
As at start of period	**13**	-	**9**	-
Additions	**26**	13	**24**	9
As at end of year	**39**	13	**33**	9
Depreciation:				
As at start of period	**(5)**	-	**(5)**	-
Provided in the period (see note 4)	**(6)**	(5)	**(5)**	(5)
As at end of year	**(11)**	(5)	**(10)**	(5)
Net book value at start of period	**8**	-	**4**	-
Net book value at end of year	**28**	8	**23**	4

12. Investment in subsidiary

	COMPANY	
	2007	2006
	£'000	£'000
Cost:		
As at start of period	**1**	-
Additions	-	1
As at end of year	**1**	1

The Company's only subsidiary is Zeta Petroleum (Romania) SRL, a Romanian incorporated company in which the Company holds 100% of the entire issued capital. The principal activity of Zeta Petroleum (Romania) SRL is exploration and production and the company operates in Romania.

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007

13. Cash and cash equivalents

	GROUP		COMPANY	
	2007	2006	**2007**	2006
	£'000	£'000	**£'000**	£'000
Cash at bank and in hand	**244**	18	**231**	13
Short-term deposits	**1,491**	2,460	**1,491**	2,460
As at end of year	**1,735**	2,478	**1,722**	2,473

Cash at bank earns interest at floating rates based on a discount to US$ / GBP LIBOR. Short-term deposits are made for varying periods of between one day and one month depending on the future cash requirements of the Group, and earn interest at the respective short-term deposit rates. The fair value of the Group's and Company's cash and cash equivalents is £1,735,401 (2006: £2,478,377) and £1,722,229 (2006: £2,472,703) respectively.

14. Trade and other receivables

	GROUP		COMPANY	
	2007	2006	**2007**	2006
	£'000	£'000	**£'000**	£'000
Trade receivables	**519**	1	**51**	1
Other receivables	**22**	62	**22**	45
As at end of year	**541**	63	**73**	46

Provision for Doubtful Debts
Included in other receivables is an amount of £179,805 paid by the Company into a bank account controlled by another party to the Bartin joint venture. In October 2007 the other party to the Bartin joint venture claimed that the Company was in default in respect of its payment of certain funding obligations for the Bartin-2 exploration well under the Joint Operating Agreement. The Company denies that it is a defaulting party, or that it owes the sums claimed. Nevertheless, in order to safeguard the Company's rights under the Joint Operating Agreement, the Company paid the amount and intends to claim the amount back. The Company has provided the full amount of £179,805 as a doubtful debt as at 31 December 2007.

15. Trade and other payables

	GROUP		COMPANY	
	2007	2006	**2007**	2006
	£'000	£'000	**£'000**	£'000
Trade payables	**128**	5	**129**	3
Other taxes and social security costs	**21**	8	**21**	8
Accruals	**590**	15	**476**	15
As at end of year	**739**	28	**626**	26

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007

16. Share capital

Group and Company:	**2007 Number**	**2007 £'000**	2006 Number	2006 £'000
Authorised:				
Ordinary shares of £0.001 each	**3,000,000**	**3**	3,000,000	3
Allotted, issued and fully paid:				
As at start of period	**2,425,398**	**2**	-	-
Issue of new shares for cash	**309,901**	**1**	2,425,398	2
As at end of year	**2,735,299**	**3**	2,425,398	2

The following shares were allotted during the year:

(i) 247,231 £0.001 ordinary shares on 7 November 2007 at a price of £7.22 per share; and

(ii) 62,670 £0.001 ordinary shares on 14 December 2007 at a price of £7.22 per share.

17. Share premium

Group and Company:	**2007 £'000**	2006 £'000
As at start of period	**3,910**	-
Arising on shares issued for cash	**2,236**	4,195
Transaction costs for issue of shares	**(138)**	(285)
As at end of year	**6,008**	3,910

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007

18. Share options reserve

Group and Company:	2007 £'000	2006 £'000
As at start of period	**337**	-
Charge for the period	**269**	337
As at end of year	**606**	337

The balance in the share options reserve relates to the fair value of the share options that have been expensed through the income statement in accordance with IFRS 2. During the year, 47,541 (2006: 242,840) share options were granted to directors and senior management (none of which were exercisable as at 31 December 2007) and 17,391 (2006: 73,429) share options were granted to the Company's corporate finance advisers (all of which were exercisable as at 31 December 2007).

19. Share Based Payments

The expense recognised for employee and non-employee services during the year is shown in the following table:

Group and Company:	2007 £'000	2006 £'000
Expense arising from equity-settled share-based payment transactions	**269**	337
Expense arising from cash-settled share-based payment transactions	**-**	-
Total expense arising from share-based payment transactions	**269**	337

The share-based payment plans are described below. There have been no cancellations or modifications to any of the plans during 2007 or 2006.

Employee Plan
Under the Employee Plan ("EMP") share options are granted to directors and employees at the complete discretion of the Company. The exercise price of the options is determined by the Company at the date of the grant. Fifty percent (50%) of the options vest after twelve months and fifty percent (50%) vest after eighteen months.

The fair value of the options is determined using the Black Scholes method as stated in Note 1.13. The contractual life of each option granted is ten years. There are no cash settlement alternatives.

Options are settled when the Company receives a notice of exercise and cash proceeds from the option holder equal to the aggregate exercise price of the options being exercised.

19. Share Based Payments *continued*

Non-Employee Plan

Under the Non-Employee Plan ("NEMP") share options are granted to non-employees at the complete discretion of the Company. The exercise price of the options is determined by the Company at the date of the grant. The options vest at the date of the grant.

The fair value of the options is determined using the Black Scholes method as stated in Note 1.13. The contractual life of each option granted is three years. There are no cash settlement alternatives.

Options are settled when the Company receives a notice of exercise and cash proceeds from the option holder equal to the aggregate exercise price of the options being exercised.

Group and Company:	**2007 Number**	**2007 WAEP[1]**	2006 Number	2006 WAEP[1]
Outstanding at the beginning of the year	**316,269**	**1.61**	-	-
Granted during the year	**64,932**	**5.56**	316,269	1.61
Outstanding at the end of the year	**381,201**	**2.01**	316,269	1.61
Exercisable at the end of the year	**333,600**	**1.61**	73,429	0.88

[1]weighted average exercise price

The weighted average remaining contractual life for the share options outstanding as at 31 December 2007 is 7.67 years (2006: 7.89 years). The weighted average fair value of options granted during the year was £5.56 (2006: £1.62). The range of exercise prices for options outstanding at the end of the year was £2.87 - £7.22 (2006: £2.87 - £3.32).

The following table lists the inputs to the models used for the two plans for the year ended 31 December 2007 and the period ended 31 December 2006:

	2007 (EMP)	**2007 (NEMP)**	2006 (EMP)	2006 (NEMP)
Expected volatility %	**42.45**	**42.45**	46.65	46.65
Risk-free interest rate %	**4.99**	**4.78**	4.46	4.54
Expected life of options (years)	**10**	**3**	10	3
Weighted average share price £	**7.22**	**7.22**	2.87	2.87
Model used	**Black Scholes**	**Black Scholes**	Black Scholes	Black Scholes

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007

20. Financial instruments

The Group's and Company's principal financial instruments comprise cash and cash equivalents, and short-term deposits. The main purpose of these financial instruments is to finance the Group's operations. The Group has other financial instruments which mainly comprise trade payables which arise directly from its operations.

Exposure to currency and interest rate risks arise in the normal course of the Group's business.

Interest rate risk
The Group and Company earn interest from bank deposits at floating rates.

The interest rate profile of the financial assets of the Group and Company as at the end of the year is as follows (excluding short-term assets and liabilities, non-interest bearing):

	GROUP		**COMPANY**	
	2007	2006	**2007**	2006
	£'000	£'000	**£'000**	£'000
Floating rate – within one year:				
Cash and cash equivalents	**1,735**	2,478	**1,722**	2,473

Floating rate financial assets comprise cash deposits placed on money markets at call and cash at bank.

A one per cent increase/decrease in interest rates on the floating rate would decrease/increase the Group loss by £16,185 (2006: £23,954) and Company loss for the year by £15,925 (2006: £23,948). There is no impact on the Group's and Company's equity.

Foreign currency risk
The Group operates internationally and has monetary assets and liabilities in currencies other than the functional currency of the operating company involved. These exposures, which are immaterial as at 31 December 2007, give rise to the net currency gains and losses recognised in the profit and loss account.

A one per cent strengthening of the British Pound against the Romanian New Lei would not have a material impact on the Group and Company loss. There is no impact on the Group and Company's equity.

The Group does not use foreign exchange contracts to hedge its currency risk.

20. Financial instruments *continued*

Fair values of financial assets and financial liabilities

All financial assets and liabilities are shown in the balance sheet at their nominal amount, which approximates to the underlying fair value.

The following methods and assumptions are used in estimating the fair values of financial instruments reflected in this note:

(a) Financial assets – the fair value of a financial asset is the amount at which the financial asset could be exchanged in an arm's length transaction. Where available, market values have been used. The fair value of the Group's and Company's financial assets, cash and cash equivalents is disclosed in note 13; and

(b) Trade receivables/trade and other payables – all trade and other receivables and payables have a remaining life of less than one year. The nominal amount is deemed to reflect the fair value.

Liquidity Risk

The Group and Company monitor liquidity risk on a monthly basis by maintaining cashflow summaries and forecasts extending out for a twelve month period. The Group and Company have no debt or overdraft facilities at the balance sheet date and no long term cash investments. In order to meet both overhead and operational cashflow obligations the Company issues additional equity for cash, and divests interests in asset licenses in order to fund other areas of the business. Group and Company liabilities are payable on demand.

21. Capital commitments

In accordance with an agreement between the Group and a third party in Turkey, the Group is committed to drilling an exploration well in Turkey in 2008. The Group estimates that the minimum cost of drilling this well will be £1,500,000.

22. Capital management

The primary objective of the Group's capital management is to fund oil and gas exploration with a focus on central and eastern Europe and the Black Sea region. The Group aims to establish and maintain a balanced portfolio that includes development, appraisal and exploration stage assets.

The Group manages its capital commitments by raising funds through the issuance of ordinary shares in the parent company Zeta Petroleum Limited and divestment of licence interests.

Capital commitments involve the initial acquisition of licence interests that the Group believes has the potential to contain commercially viable oil and gas reserves and then the exploration and/or appraisal of these licences by following a work programme that achieves internally stated timelines as well as licence commitments imposed by local governments.

No changes were made in the objectives, policies or processes during the year ended 31 December 2007.

23. Post balance sheet events

On 27 February 2008 the Company signed a sale and purchase agreement ("SPA") for the sale of its entire 19.5% interest in the Bartin licences. The Company is bound by a confidentiality clause in the SPA and is unable to disclose the consideration amount payable by the Purchaser.