Petsec Energy

PETSEC ENERGY LTD

ANNUAL REPORT 2014

CAPITAL STRUCTURE

as at 20 March 2015

AUSTRALIA	
EXCHANGE	ASX
TICKER	PSA
SHARES ON ISSUE	231.2 MILLION
OPTIONS ON ISSUE	30,000
SHARE PRICE	$0.105
MARKET CAPITALISATION	$25.4 MILLION

USA	
EXCHANGE	OTC PINK SHEETS
TICKER	PSJEY

CONTENTS

PETSEC ENERGY LTD

ABN 92 000 602 700

The Company is listed on the Australian Stock Exchange (symbol: PSA) and traded over the counter in the USA as American Depositary Receipts (ADRs) (symbol: PSJEY). Its corporate office is in Sydney, Australia, and its USA operations offices are in Houston, Texas and Lafayette, Louisiana.

ANNUAL GENERAL MEETING

To be held at: 11am (AEST) on Thursday, 14 May 2015, at the Museum of Sydney, corner of Bridge and Phillip Streets, Sydney.

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

The Company's strategy is to maximise the value of its current reserves, pursue participation in high quality, high impact exploration drilling opportunities in the Gulf Coast onshore and bay areas of Texas and Louisiana, USA, and to acquire onshore leases, with undeveloped or producing oil and gas reserves, which hold significant development, low risk exploitation and exploration potential.

CORPORATE OBJECTIVE AND STRATEGY

The geographical focus is predominately in the USA in Texas and Louisiana, with one lease with undeveloped oil resources in the Republic of Yemen.

The aim is to build Petsec Energy into a significant mid-tier oil and gas exploration and production company, respected in the industry for its technical skills, timely and cost effective delivery of projects, and the integrity with which it conducts its business.

2014 YEAR IN REVIEW

CORPORATE

- Appointed Mr. Dick Smith as Chief Executive Officer of the U.S. operating subsidiary, Petsec Energy Inc., expanding the Company's exploration, development and production capabilities.
- Monetised mature and fully developed Marathon and Main Pass Block 270 fields at high point in oil and gas prices to provide funds for 2014/2015 onshore oil and gas exploration programme.
- Acquired a 29.75% participating interest in Block 7, Al Barqa Permit, in the Republic of Yemen, which contains the undeveloped Al Meashar oil discovery.

OPERATIONS

PRODUCTION

- The Marathon and Main Pass 270 production interests were divested in July 2014.
- Remaining producing fields are the Main Pass Block 19 Field in the shallow waters of the Gulf of Mexico, USA, and the Jeanerette Field, onshore Louisiana (brought into production on 30 June 2014).
- The Main Pass Block 18 Field ceased production in March 2014.
- The Chandeleur 31/32 Area Field was decommissioned August 2014.

EXPLORATION & DEVELOPMENT

- The Company returned to conventional exploration in 2014:
  - Exploration prospects were actively pursued.
  - Nine prospects have been acquired/generated for testing. Prospect target sizes range between 2.4 and 6.7 Bcfe per well net to the Company.
- Two wells drilled in 2014 for one discovery:
  - The Adeline Sugar Factory #4 well on the Jeanerette Field, which was brought into production on 30 June 2014.
  - The Herbert Abstract Co. #1 well on the SW Holmwood prospect which was plugged and abandoned after failing to encounter sufficient hydrocarbons to warrant completion (November/December 2014).
- The first well in an anticipated seven well exploration programme in 2015, the Ruth R. Bravanec, et al #1 well on the West Crab Lake prospect was plugged and abandoned after it failed to encounter commercial reserves (January 2015).
- In Block 7, Yemen, preparations were completed to undertake an extended production test on the Al Meashar oil discovery.

FINANCIAL

The divestiture of the Company's production interests in the Marathon and Main Pass 270 gas/condensate fields in July 2014 significantly reduced production and the financial results compared to the 2013 year.

1,612MMcfe

PRODUCTION:
1,612 MMcfe, DOWN 56%

US$5.08/Mcfe

GAS EQUIVALENT SALES PRICE REALISED:
US$5.08/Mcfe, UP 13%

US$8.2MM

NET REVENUES (AFTER ROYALTIES AND HEDGING):
US$8.2 MILLION, DOWN 50%

US$3.4MM

EBITDAX:
US$3.4 MILLION, DOWN 56%
EBITDAX MARGIN STEADY AT US$2.10/MCFE

US$3.0MM

IMPAIRMENT, ABANDONMENT, EXPLORATION AND WORK-OVER EXPENSE:
US$3.0 MILLION, DOWN 79%

US$1.8MM

DEPRECIATION, DEPLETION AND AMORTISATION (DD&A) EXPENSE:
US$1.8 MILLION (US$1.13/Mcfe), DOWN 74%

US$4.23/Mcfe

UNIT OPERATING COSTS:
US$4.23/Mcfe, UP 76%

US$1.1MM

NET LOSS AFTER TAX:
US$1.1 MILLION (AFTER US$2.2 MILLION GAIN ON SALE OF ASSETS), DOWN 93%

US$5.7MM

ACQUISITION, EXPLORATION AND DEVELOPMENT EXPENDITURES:
US$5.7 MILLION, IN LINE WITH PREVIOUS YEAR

US$32.6MM

CASH AT 31 DECEMBER 2014:
US$32.6 MILLION, UP 28%

1.9Bcfe

NET 2P OIL AND GAS RESERVES AS OF 1 JANUARY 2015:
1.9 Bcfe (RYDER SCOTT)

CHAIRMAN'S REPORT

DEAR SHAREHOLDER,

2014 was a particularly active year for Petsec Energy as we suspended our shale oil strategy and returned to exploration of conventional prospects, mainly onshore Louisiana and Texas Gulf, USA, and the acquisition of reserves, producing or to be developed, with associated exploitation and exploration potential.

In the year, a new leader of the US operations was appointed, nine exploration prospects were generated/acquired, two wells were drilled for one success and an undeveloped oil discovery with associated high potential exploration potential was acquired in Block 7, Republic of Yemen.

The objective of the Company from 2015 onwards will be to drill between five and ten wells on conventional prospects each year exposing the Company to in excess of 21 Bcfe per year, which if all five wells were successful could generate a PV10 value in excess of US$50 million per annum.

The Company has a strong record of conventional exploration success, which has substantially increased the value of the Company particularly in periods of low but stable oil and gas prices. In the USA, in the period from 1991 to 2014 Petsec Energy drilled 101 wells with a 78% success rate, and generated net production of approximately 214 Bcfe and EBITDAX of US$568 million.

The Company currently has a highly experienced management team and is confident that it can achieve a significant level of success from the prosecution of our 2015 Exploration and Development Programme.

Dick Smith was appointed to the position of Chief Executive Officer of our U.S. operating subsidiary, Petsec Energy Inc., in March 2014 to provide impetus to our return to conventional exploration, development and production. Dick Smith brings strong technical and commercial expertise in exploration in Texas and Louisiana.

Two exploration prospects were drilled in the 2014 year for one discovery of gas and condensate in the Adeline Sugar Factory # 4 well, which was brought into production in June 2014 and has since flowed at a steady rate of some 10 million cubic feet of gas and 62 barrels of oil a day.

In 2015, it is anticipated that some seven exploration wells will be drilled exposing the Company to in excess of 21 Bcfe net to the Company. The prospects are economically robust at current oil prices of US$50/bbl and US$3/Mcf gas.

STRONG RECORD OF CONVENTIONAL EXPLORATION SUCCESS

The Company has a strong record of conventional exploration success, which has substantially increased the value of the Company particularly in periods of low but stable oil and gas prices. In the USA, in the period from 1991 to 2014 Petsec Energy drilled 101 wells with a 78% success rate, and generated net production of approximately 214 Bcfe and EBITDAX of US$568 million.

The fall in oil and natural gas prices in the December 2014 quarter from US$110/bbl of oil to less than US$50/bbl, and US$4/Mcf of natural gas to just below US$3/Mcf, has caused a 25–30% reduction in drilling and development costs, and made available a larger population of farm-in and acquisition opportunities.

To generate additional funds for the potential development of expected discoveries, we disposed of our production interests in the mature and fully developed Marathon and Main Pass Block 270 gas/condensate fields in July 2014 for US$17 million plus interests in four exploration prospects, one of which was the successful Adeline Sugar Factory # 4 well. This disposition took our cash holdings up to US$32.6 million at year-end.

The recent dramatic fall in oil and gas prices is expected to provide a fruitful environment for the acquisition of reserves with significant exploitation and exploration potential. Our focus is mainly onshore Texas and Louisiana, USA, however in the year an opportunity arose to acquire interests subject to Yemen government approval, from AWE (21.25%) and Mitsui E&P Middle East (8.5%) at low cost, in Block 7, Al Barqa Permit, in the Republic of Yemen, which includes the undeveloped Al Meashar oil discovery.

The Australian listed company Oil Search Limited is the operator of Block 7 and the Joint Venture ("JV") has spent over US$110 million on the Block drilling three exploration wells (all intersected oil) discovering the Al Meashar oil field and defining a number of prospects and leads with exploration potential ranging from 2 to 900 million bbls. The immediate objective of the JV is to conduct a production test in 2015 on the Al Meashar oil discovery to establish flow rates and indications of reserve size, leading to development. The oil discovery is geologically similar and 14 kilometres east of the Habban oil field in the Al Uqlah Block S2, which is currently producing in excess of 23,000 bopd, operated by OMV Exploration GmbH.

Petsec Energy has no debt and held US$32.6 million in cash at year-end. We expect to drill seven exploration wells in the USA in 2015 exposing the Company to in excess of 21 Bcfe, and to bring the Al Meashar oil discovery in Yemen into production. We are confident of a significant level of success in 2015 and a consequent increase in shareholder value.

The Board and I would like to thank you, our shareholders, for your support which we expect to reward this year with success in the 2015 exploration and development programme. I look forward to providing further details on our progress at the AGM.

TN Fern
Chairman and Managing Director

NEW DISCOVERIES – THE ENGINE OF GROWTH

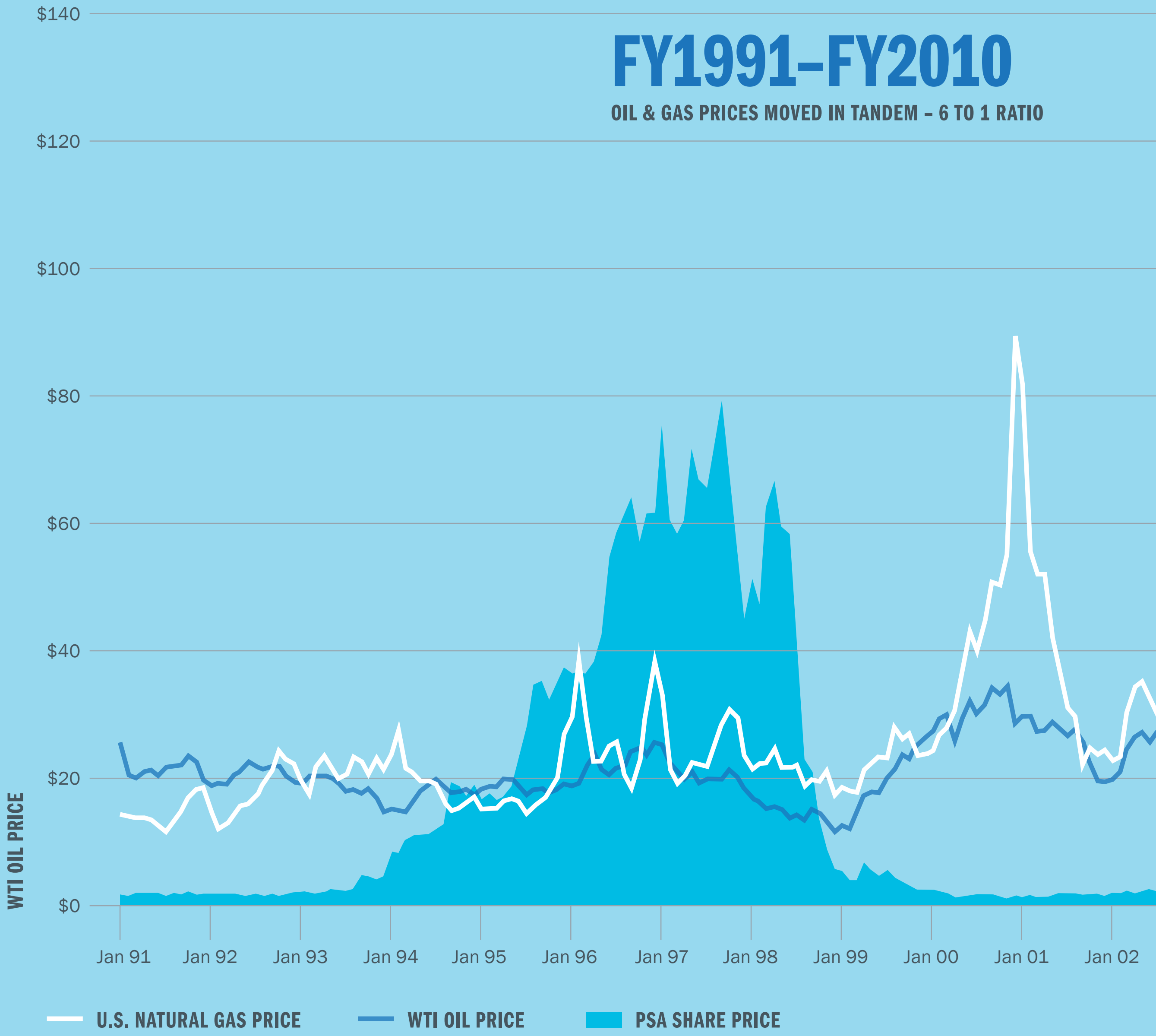
PETSEC ENERGY SHARE PRICE / WTI OIL PRICE / U.S. NATURAL GAS PRICE

FY1991–FY1999

58 WELLS DRILLED IN USA – 81% SUCCESS RATE
CUMULATIVE PRODUCTION: 148 BCFE
CUMULATIVE EBITDAX: US$262 MILLION

FY1991–FY2010

OIL & GAS PRICES MOVED IN TANDEM – 6 TO 1 RATIO



FY2000–MID2008

HIGHER GAS PRICES

FY2002–FY2009

35 WELLS DRILLED IN USA – 74% SUCCESS RATE
7 WELLS DRILLED IN CHINA – 43% SUCCESS RATE
CUMULATIVE PRODUCTION: 52 BCFE
CUMULATIVE EBITDAX: US$280 MILLION

MID2008–CURRENT

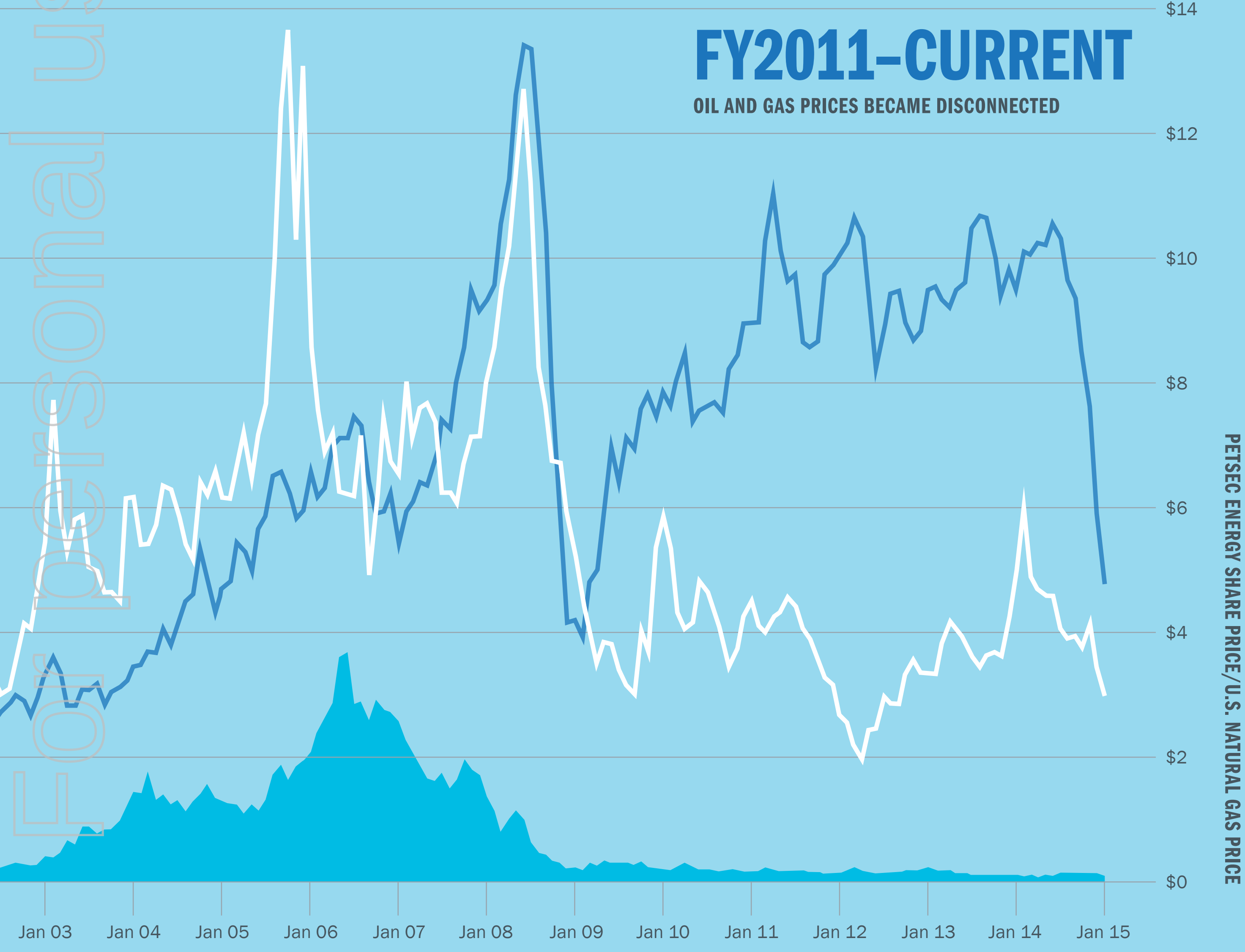
LOWER GAS PRICES

FY2010–FY2014

10 WELLS DRILLED IN USA – 60% SUCCESS RATE
CUMULATIVE PRODUCTION: 13.8 BCFE
CUMULATIVE EBITDAX: US$26 MILLION

FY2011–CURRENT

OIL AND GAS PRICES BECAME DISCONNECTED



OPERATIONS REVIEW

ABOUT US

Petsec Energy Ltd is an independent oil and gas exploration and production company listed on the Australian Stock Exchange with operations in the shallow waters of the Gulf of Mexico and onshore Texas and Louisiana, USA, and in The Republic of Yemen.

PRODUCTION

Petsec Energy produced 1,559 million cubic feet of gas and 8,821 barrels of oil/condensate (equivalent to 1,612 MMcfe) for the twelve months to 31 December 2014 from its producing fields onshore Louisiana, in the state waters of the Louisiana Gulf Coast and in the shallow waters of the Gulf of Mexico.

Following the divestment of the Marathon and Main Pass Block 270 interests in July 2014, the Company's remaining producing wells are at Main Pass Block 19 in the shallow waters of the Gulf of Mexico and the Adeline Sugar Factory #4 well in the Jeanerette Field, onshore Louisiana, USA.

MAIN PASS BLOCK 19

55% W. I. (NRI: 45.83%)

The Main Pass 19 lease is in 26 feet of water in the Gulf of Mexico and was acquired in 2004. Petsec drilled six wells on the lease during the period 2005 to 2006. A four-pile platform with compression facilities was set in 2005 and a 3,000-barrel oil storage facility was added in 2008.

ADELINE SUGAR FACTORY #4 WELL, JEANERETTE FIELD

12.5% W.I. (NRI: 9.0%)

The Adeline Sugar Factory ("ASF") #4 well located in the Jeanerette Field, St Mary Parish, Louisiana, was discovered and brought into production in June 2014. The well is the first well drilled on prospects acquired as part of the Marathon and Main Pass Block 270 divestiture transaction announced on 7 July 2014.

ASF #4 has produced at a consistent gross rate of approximately 10.4 MMcfpd and 62 bcpd since being brought into production.

Production from the well is currently constrained by flow line capacity. The operator plans to install additional flow lines and other upgrades to the main production facility to increase production rates.

MAIN PASS BLOCK 18

100% W. I. (NRI: 83.33%)

The Main Pass Block 18 field is directly north of Main Pass Block 19 and was acquired in 2005 at Federal Lease Sale No. 194. A single well (G-6) was drilled from the Main Pass Block 19 platform into Main Pass 18 in February 2006 and completed for production.

Production from the Main Pass Block 18 field ceased in March 2014 when the G-6 well was shut-in due to sand production.

CHANDELEUR BLOCK 31/32

The Chandeleur Block 31/32 fields are in 66 feet of water and both were acquired from a third party in November 2007.

The fields reached the end of their productive life in August 2013 and decommissioning operations were completed in August 2014.

Onshore exploration drilling

EXPLORATION

The Company's exploration strategy is to focus on high impact conventional exploration, in mainly gas/condensate and oil rich areas onshore Louisiana and Texas, and in the shallow waters of the Gulf of Mexico, USA.

In May 2014, the Company participated in the successful drilling of the onshore Adeline Sugar Factory #4 well gas/condensate discovery, acquired as part of the Marathon and Main Pass 270 divestiture transaction.

For much of 2014, the Company was actively seeking exploration prospects in which to participate. Nine prospects have been acquired/generated for drilling with two wells tested in 2014 for one discovery.

The 2015 exploration programme in the USA of seven wells is estimated to cost US$9.2 million for an estimated total target size exposure of 21.4 Bcfe net to the Company, and US$3 million for the production test of the Al Meashar oil field in Yemen.

2015 EXPLORATION PROGRAMME

USA exploration budget	US$9.2 million
USA exploration wells	7
Yemen budget	US$3 million
Cash at 1 Jan 2015	US$32.6 million

PROJECT TIMELINE

		Wells	Target size of prospects												
Geographical Location	**Activity**	**NO.**	**Net**	**Q1 2015**			**Q2 2015**			**Q3 2015**			**Q4 2015**		
				Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
USA			**Bcfe**[3]												
Onshore Louisiana	Exploration[1]	6	14.7												
Gulf of Mexico	Exploration[1]	1	6.7												
	USA total	**7**	**21.4**												
Republic of Yemen			**MMbbl**												
Block 7 Al Barqa Permit	Exploration & long term testing of Al Meashar oil discovery[2]	1	3.3												
	Yemen total	**1**	**3.3**												

Exploration

1. Timing of USA prospects drilled may vary subject to operators drilling schedule.
2. Block 7, Yemen activity is dependent on both government approvals of interest transfers and operators schedule.
3. 1 barrel of oil = 6 Mcf of gas.

ACQUISITIONS

BLOCK 7, AL BARQA PERMIT, REPUBLIC OF YEMEN

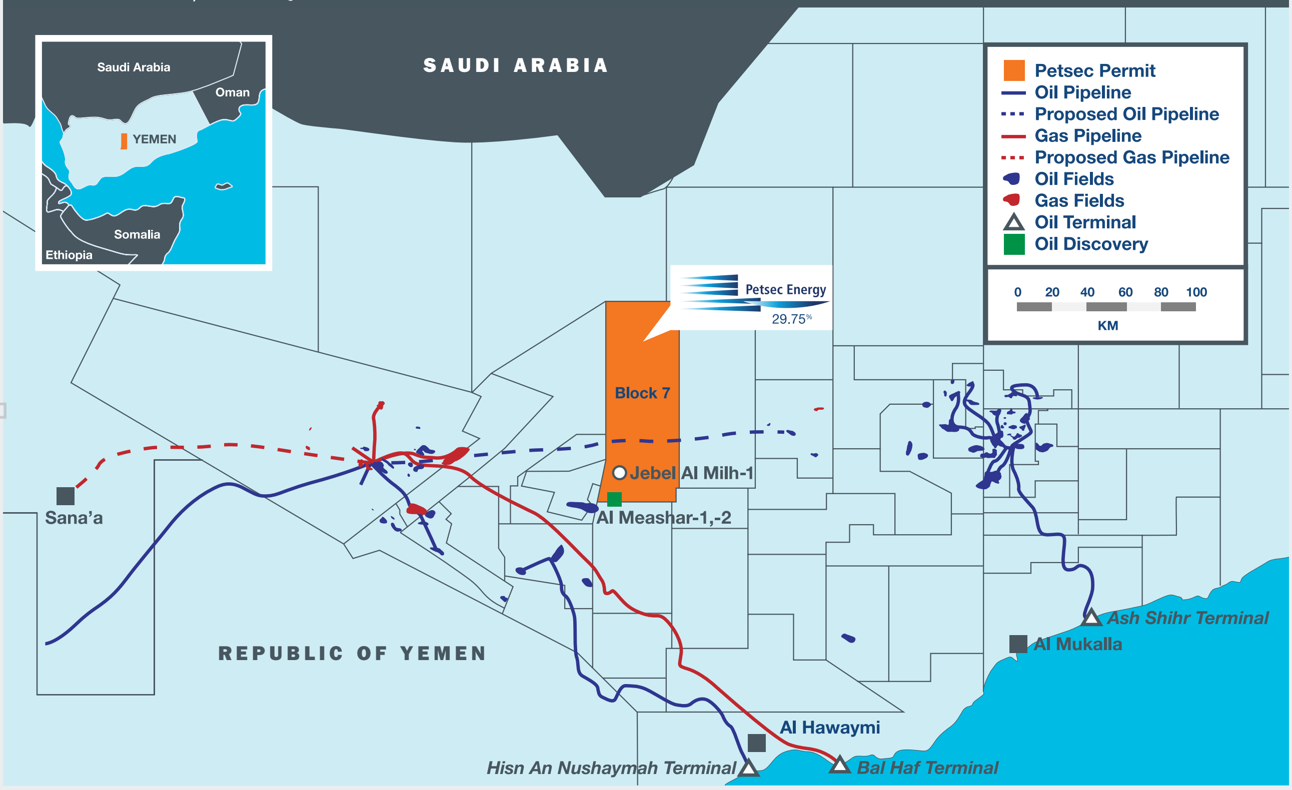
The Company executed agreements with AWE Limited (21.25%) and Mitsui E&P Middle East B.V. (8.5%) to acquire their respective Participating Interests in Block 7, Al Barqa Permit in the Republic of Yemen. Completion of both transactions is subject to customary approvals from the other Joint Venture Partners in the project, the Yemen Government, and the state-owned Yemen Oil and Gas Company. The Company anticipates that these transactions will be completed in 2015.

Block 7, operated by Australia's Oil Search Limited, is an onshore exploration permit covering an area of 5,000 square kilometres (1,235,527 acres) located 340 kilometres east of Sana'a, the capital of Yemen. It contains the undeveloped Al Meashar oil discovery and a number of large oil prospects/leads that hold significant oil potential.

Government approval to proceed with long-term production testing of the Al Meashar Oil Field is anticipated in the first half of 2015. Subject to that approval, exploration and long-term testing of the Al Meashar oil discovery are estimated to cost US$3 million in 2015.

Well testing – Al Meashar oil discovery 2010

MAP OF BLOCK 7, AL BARQA PERMIT IN THE REPUBLIC OF YEMEN



DIRECTORS' AND FINANCIAL REPORT

For Corporate Governance go to
www.petsec.com.au/about-us/corporate-governance

DIRECTORS' REPORT

FOR THE YEAR ENDED 31 DECEMBER 2014

The directors present their report together with the Financial Report of Petsec Energy Ltd ("the consolidated entity"), being Petsec Energy Ltd ("the Company") and its subsidiaries, for the financial year ended 31 December 2014 and the independent auditor's report thereon.

1. DIRECTORS

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

Terrence N Fern

Chairman and Chief Executive Officer

Mr Fern has been a director since 1987 and has over 35 years of extensive international experience in petroleum and minerals exploration, development and financing. He holds a Bachelor of Science degree from the University of Sydney and has followed careers in both exploration geophysics and natural resource investment. Mr Fern was formerly a director of TSX and ASX listed company Oceana Gold Corporation from 2006 until June 2011.

David A Mortimer AO

Non-executive Director

Chairman of the Audit Committee and the Nomination and Remuneration Committee

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

Mr Mortimer holds a Bachelor of Economics degree (First Class Honours) from the University of Sydney and is a Fellow of the University of Sydney Senate and the Australian Institute of Company Directors. Mr Mortimer's other roles include Governor of the Australia Israel Chamber of Commerce, and President of the Sydney University Football Club.

Mr Mortimer was formerly a non-executive director and more recently Chairman of ASX listed company Leighton Holdings Limited from 1997 until August 2011 and Chairman of Australia Post from 2006 to 2012.

Alan P Baden

Non-executive Director

Member of the Audit Committee and the Nomination and Remuneration Committee

Mr Baden was appointed to the Board in May 2013 and is a U.S. citizen, resident in Houston, Texas. He is a senior commercial lawyer with the legal firm of Thompson & Knight and has over 35 years of experience in the U.S. oil and gas industry, with a focus on mergers and acquisitions, public and private financings, and U.S. capital market activities, representing major U.S. E&P companies who operate in shale oil and conventional exploration in the Gulf of Mexico. He has been recognised by his peers to be a leading lawyer in oil and gas transactions and in securities and corporate finance.

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

Mark S Lober

Non-executive Director

Member of the Audit Committee and the Nomination and Remuneration Committee

Mr Lober was appointed to the Board in May 2013 and is a U.S. citizen, resident in Houston, Texas, who brings a wealth of technical and management expertise gained from his 35 years of experience in the U.S. oil and gas industry, where he was particularly engaged in prospect generation in those areas in which the Company operates for both conventional and unconventional exploration. In the last decade he has been actively involved in shale oil exploration in California, New Mexico, Texas and Louisiana.

Mr Lober holds a Master of Science (Geophysics) Degree from the Boston College and a Bachelor of Science (Geology) Degree from the State University of New York at Brockport. Mr Lober is a Certified Professional Petroleum Geologist and a member of the American Association of Petroleum Geologists and the Society of Exploration Geophysicists.

He has held the positions of senior geophysicist, exploration manager and new ventures manager with Amoco Production Company, Standard Oil Production Company (SOHO), Amerada Hess Corporation, Prime Natural Resources, Inc., Meridian Resource Corporation and Caltex Gas Exploration where he is currently developing new resource play opportunities.

DIRECTOR'S REPORT CONTINUED

2. EXECUTIVE OFFICERS

Richard J Smith
Chief Executive Office of Petsec Energy Inc. ("PEI")

Mr Smith joined the Company in March 2014 and has over 35 years of experience in a wide variety of senior exploration and production roles predominantly with U.S. E&P companies including Amerada Hess Corporation, Amoco Production Company, Pedernales Production LLC, Houston Energy LLC, Prime Natural Resources (formerly F-W Oil Interests, Inc.), and F-W Oil Exploration LLC/F-W Oil Trinidad LLC. He holds an impressive record of growing the value of exploration and production companies through successful exploration and acquisitions. His North American experience is predominantly in the Gulf of Mexico, Louisiana and Texas onshore, in conventional and unconventional reservoirs. He also has international exploration experience in West Africa, North Africa, Europe and the Caribbean.

Mr Smith holds a Master of Science (Geology) from the University of Tennessee, Knoxville, Tennessee and a Bachelor of Science (Geology) from SUNY at Brockport, Brockport, New York.

Ross A Keogh
President of PEI and Group Chief Financial Officer

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

Ron Krenzke
Executive Vice President of Exploration of PEI

Mr. Krenzke joined the Company in November 2009 as the Executive Vice President of Exploration of Petsec Energy Inc. Mr. Krenzke has 40 years of experience in the oil and gas exploration and production industry. His career includes experience in many phases of management of oil and gas exploration and production operations. During his early career Mr. Krenzke worked in a variety of technical and management positions at major and large independent oil and gas companies including: Mobil Oil, Texas Eastern, Monsanto Oil and Amerada Hess. Since 1990 Mr. Krenzke has founded and co-founded three private E&P companies operating in the Gulf Coast region of the USA. Mr. Krenzke founded INEXS and South Coast Exploration in 1990, both of which were sold in 1997 to Xplor Energy. In 2000, he co-founded Gryphon Exploration Company, which was ultimately sold in to Woodside Petroleum in 2005 for US$285 million. From 2006 through 2009, Mr. Krenzke worked with small cap private companies primarily as a business and technical consultant. Mr. Krenzke holds a Bachelor of Science degree in Geophysics from Texas A&M University.

Paul Gahdmar
Company Secretary and Group Financial Controller

Mr Gahdmar joined the Company in 1999 as the Financial Accountant of the Petsec Energy Ltd group and has since held a number of management positions within the Company. Mr Gahdmar was appointed as the Company Secretary of Petsec Energy Ltd in 2008 and has over 20 years of experience in corporate accounting and finance in listed companies within the mining and resources industry. Mr Gahdmar holds a Master of Business and Technology degree from The University of New South Wales and a Diploma in Investor Relations from the Australasian Investor Relations Association. Mr Gahdmar is a Fellow of the Institute of Public Accountants and a Member of the Australian Institute of Company Directors.

3. DIRECTORS' MEETINGS

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

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

	Regular Board Meetings	Additional Board Meetings	Audit Committee Meetings	Nomination & Remuneration Committee Meetings
Total number held during the year	**8**	**–**	**4**	**3**
T N Fern[1]	8	–	4	3
D A Mortimer	8	–	4	3
A P Baden	8	–	4	3
M S Lober	2	–	1	2

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

DIRECTOR'S REPORT CONTINUED

4. REMUNERATION REPORT

The Remuneration Report is set out on pages 21 to 27 and forms part of the Directors' Report for the financial year ended 31 December 2014.

5. PRINCIPAL ACTIVITIES

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

In addition, the consolidated entity executed agreements during the year with AWE Limited (21.25%) and Mitsui E&P Middle East B.V. (8.5%) to acquire their respective interests in Block 7, Al Barqa Permit in the Republic of Yemen. Completion of both the AWE and Mitsui transactions is subject to customary approvals from the Joint Venture Partners, the Yemen government and the state owned Yemen Oil and Gas Company.

There were no other significant changes in the nature of the activities of the consolidated entity during the year.

6. FINANCIAL REVIEW

The consolidated entity incurred a net loss after tax for the full year of US$1.1 million (previous corresponding period: Loss of US$15.2 million) after the recognition of a gain of US$2.2 million on the sale of the Marathon and Main Pass assets, dry hole, impairment, exploration and work-over expense of US$3.0 million and depreciation, depletion, and amortisation ("DD&A") expense of US$1.8 million.

The consolidated entity generated net oil and gas revenues (after royalties and hedging) of US$8.2 million for the twelve months to 31 December 2014, from production of 1,612 million cubic feet of gas equivalent ("MMcfe") at an average natural gas equivalent sales price of US$5.08/Mcfe. This represents a reduction of 50% on the net oil and gas revenues achieved in the previous corresponding period of US$16.4 million due to the divestiture of Petsec Energy's working interests in the Marathon and Main Pass 270 producing fields in July 2014 (see *"Operations Review – Asset Divestiture"* section below for further details).

The consolidated entity realised an average gas equivalent sales price of US$5.08/Mcfe (including hedging) for the current period. This was 13% higher than the US$4.50/Mcfe achieved in the previous corresponding period, with the Company benefiting from high natural gas prices during the extremely cold USA Winter period which caused U.S. natural gas prices to increase substantially during the first quarter of 2014 – natural gas spot prices reached a high of approximately US$6.33/Mcf in mid-February 2014. The consolidated entity produced 45% of its 2014 production volumes in the March quarter and 85% of total production for the year in the first six months, prior to the sale of its interests in the Marathon and Main Pass 270 fields.

The consolidated entity realised an average sale price of US$4.68/Mcf and US$101.12/bbl for its natural gas and oil/condensate production, respectively (previous corresponding period: US$3.94/Mcf and US$107.89/bbl). Approximately 28% of natural gas production volumes for the current period were hedged at an average sales price of US$4.29/Mcf with the Company averaging US$4.83/Mcf for its unhedged production volumes.

Lease operating expense of US$2.5 million (previous corresponding period: US$3.7 million) and geological, geophysical and administrative ("GG&A") expense of US$4.3 million (previous corresponding period: US$5.1 million) were lower in the current period, reflecting the reduced size of the consolidated entity's U.S. operations. On a unit-basis, lease operating expense was US$1.53/Mcfe (previous corresponding period: US$1.01/Mcfe) and GG&A was US$2.66/Mcfe (previous corresponding period: US$1.39/Mcfe), both higher than the prior year due to lower production volumes.

Earnings before interest, income tax, depreciation, depletion, amortisation and rehabilitation, and exploration expense ("EBITDAX") for the current period was US$3.4 million, down 56% on the previous corresponding period EBITDAX of US$7.7 million mainly due to lower production.

The EBITDAX margin of US$2.10/Mcfe was in line with the previous corresponding period. The higher average sales price received for the current period coupled with the gain recognised on the sale of the Company's Marathon and Main Pass 270 interests, were absorbed by the impact of the higher unit operating costs attributable to lower production volumes.

Depreciation, depletion, amortisation and rehabilitation ("DD&A") expense for the twelve months to 31 December 2014 reduced significantly to US$1.8 million (previous corresponding period: US$7.0 million) following the sale of the Marathon and Main Pass 270 producing fields.

Financial position

At 31 December 2014, the consolidated entity held cash deposits of US$32.6 million and was debt free. This represents a 28% increase on the previous corresponding period cash balance of US$25.4 million. The cash deposits which are predominantly held in U.S. dollars include US$5.3 million held in an escrow account to secure operator bonds that are on issue to the Bureau of Ocean Energy Management ("BOEM").

7. OPERATIONS REVIEW

Petsec Energy Ltd (the "Company") is an independent oil and gas exploration and production company listed on the Australian Stock Exchange (ASX Ticker: PSA) with operations in the shallow waters of the Gulf of Mexico and onshore Texas and Louisiana, United States of America ("USA"), and in the Republic of Yemen where the Company has entered into agreements to acquire interests in Block 7, Al Barqa Permit which holds the Al Meashar oil discovery.

Appointment of new CEO of Petsec Energy Inc.

In March 2014, the Company appointed Mr. Richard Smith as Chief Executive Officer of its U.S. subsidiary, Petsec Energy Inc. ("PEI"). Mr. Smith is a U.S. citizen, resident of Texas, who has over 35 years' experience in a wide variety of senior Exploration and Production ("E&P") roles predominantly with U.S. E&P companies. He has a successful track record of managing E&P programmes and asset acquisitions resulting in significant, low-cost reserve additions.

Asset divestiture

In July 2014, the Company sold its working interests in the Marathon and Main Pass 270 fields, together with certain associated exploration interests, to a privately held U.S. exploration and production company ("Purchaser") for US$17 million plus the right to participate in four of the Purchaser's high potential exploration prospects. The transaction had an effective date of 1 January 2014 and was completed on 14 July 2014. Net cash on completion of the transaction was US$12.1 million.

DIRECTOR'S REPORT CONTINUED

One of the Purchaser's high potential South Louisiana exploration prospects has been drilled, the Adeline Sugar Factory ("ASF") No. 4 prospect, which was a success and brought into production on 30 June 2014.

The assets sold by the Company pursuant to the transaction included:

- All of Petsec's production and exploration rights in the Marathon field
- All of Petsec's interests in the Main Pass 270 producing wells
- Assignment of working interests in the exploration rights on Main Pass 270, Main Pass 273 and Main Pass 274

As a result of the transaction, Petsec retained a 12.5% working interest in the exploration rights in Main Pass 270, 273 and 274.

The Company received its share of production, revenues and lifting costs, in respect of the Marathon and Main Pass 270 fields, from 1 January 2014 through to the closing date (14 July 2014), and these were adjusted against the US$17 million cash consideration amount. As a result the net cash amount on completion of the transaction was US$12.1 million.

Production

Petsec Energy produced 1,559 million cubic feet of gas and 8,821 barrels of oil/condensate (equivalent to 1,612 MMcfe) for the twelve months to 31 December 2014 from its producing fields onshore Louisiana, in the state waters of the Louisiana Gulf Coast and in the shallow waters of the Gulf of Mexico, USA.

Following the divestment of the working interests in the Marathon (Atchafalaya Bay) and Main Pass Block 270 fields, the Company's remaining producing fields are Main Pass Block 19 in the shallow waters of the Gulf of Mexico and the Jeanerette Field, onshore Louisiana – brought into production on 30 June 2014.

Production from the Company's Main Pass Block 18 field ceased in March 2014, when the G-6 well was shut-in due to sand production. The well was recompleted in June 2014 at a cost of US$1.2 million and was returned to production for a few days before loading up with fluid and ceasing production. Efforts to restore the well to production were unsuccessful and the cost of the recompletion was expensed in the current period.

In May 2014, the Company decommissioned its Chandeleur Block 31/32 field, which had reached the end of its productive life in the prior year. The decommissioning operations were completed in August 2014 at a cost to the Company of US$3.2 million.

Exploration and development

The Company's strategy to grow reserves is to focus on high impact conventional exploration, in mainly gas/condensate and oil rich areas onshore Gulf Coast (Louisiana and Texas) and shallow Gulf of Mexico, USA, and to acquire onshore leases with producing reserves, or near term development reserves, with significant exploitation and exploration potential.

For the most part of 2014, the Company has been actively identifying exploration prospects in which to participate.

In December 2014, the Company announced that the Board had approved the 2014/2015 Exploration Programme in which five committed and three optional conventional exploration wells were planned to be drilled on the Gulf Coast and in the Gulf of Mexico, USA.

The Company expects to expose US$7.3 million in prospect and exploration drilling costs on the five committed exploration wells which will target prospects ranging in size from 10 to 66 Bcfe gross (2.4 to 6.7 Bcfe net to Petsec Energy) for a total exposure of 18.3 Bcfe, net to the Company.

The five committed exploration wells will test oil and gas/condensate prospects which are all located onshore Louisiana, other than the Company's Hummer Prospect which is located in 215 feet of water on the Main Pass Block 270/273/274 leases in the Gulf of Mexico, offshore Louisiana.

To-date, the Company has drilled one well in this programme – the Herbert Abstract Co. #1 well which reached its target depth in mid-December 2014 and was plugged and abandoned (see below for further details). A second well, the Ruth R. Bravanec, et al #1 well, which was not one of the five committed wells, was spud on 7 January 2015 and reached its planned true vertical depth in late January 2015. This well was also plugged and abandoned (further details are provided in section 19. *Events subsequent to balance date* of this Directors' Report).

Despite the dramatic fall in oil and gas prices over the last quarter of the 2014 year, from US$110/bbl to less than US$50/bbl for oil and from US$4/Mcf to US$3/Mcf for U.S. natural gas, the Company has determined that the remaining prospects in the programme are economically robust at current oil and gas prices.

Adeline Sugar Factory ("ASF") No. 4 well – Jeanerette Field

Petsec: 12.5% working interest (9% net revenue interest)

In the first half of the year, the Company participated in the exploration drilling of the onshore Adeline Sugar Factory ("ASF") No. 4 well for a 12.5% working interest. The ASF No. 4 was spud on 12 March 2014 and was located in the Jeanerette Field, St. Mary Parish, Louisiana.

The ASF No. 4 well reached a total depth of 15,300 feet (4,663 metres) in early May 2014 with wireline logging indicating a gas/condensate discovery in the primary objective lower Miocene sands. The well was tested at a peak flow rate of 15.8 million cubic feet of gas per day ("MMcfpd") and 105 barrels of condensate per day ("bcpd") through a 16/64th choke, at a flowing tubing pressure of 7,890 pounds per square inch in June 2014. Net drilling and completion cost to the Company was $1.9 million.

The well commenced production on 30 June 2014 and has produced at a consistent gross rate of approximately 10.4 MMcfpd and 62 bcpd on a 15/64th choke.

Production from the ASF No. 4 well is currently constrained by flow line capacity. The operator plans to install additional flow lines to the main production facility and upgrade the high pressure separator to increase production rates by some 4 MMcfpd.

Herbert Abstract Co. #1 Well – Southwest Holmwood Prospect

Petsec: 37.5% BPO/28.88% APO working interest (30.0% BPO/ 23.1% APO net revenue interest)

The Herbert Abstract Co. #1 well (Herbert #1 well) on the Southwest Holmwood Prospect in Calcasieu Parish, Louisiana was spud on 27 November 2014 and reached its planned TD of 12,000 feet (3,658 metres) in mid-December 2014.

DIRECTOR'S REPORT CONTINUED

The vertical well was drilled to test a fault closure immediately south of the Southwest Holmwood gas/condensate Field and on the east flank of the Lake Charles Field. The well intersected the objective Marg Tex sand, however the reservoir sand package was thicker than expected and was not adequately fault sealed from the adjacent Southwest Holmwood Field. The well encountered insufficient productive hydrocarbons to warrant completion. The well has been plugged and abandoned and no further exploration is planned for the prospect. The Company's net share of the drilling and upfront exploration costs of approximately US$1.7 million has been expensed.

Acquisition

Block 7, Al Barqa Permit, Republic of Yemen

Block 7 is an onshore exploration permit covering an area of 5,000 square kilometres (1,235,527 acres) located approximately 340 kilometres east of Sana'a, the capital of Yemen. The block is operated by Australia's Oil Search Limited and contains the Al Meashar oil discovery as well as an inventory of leads and prospects defined by 2D and 3D seismic surveys, which hold significant oil potential.

The Company announced in March 2014 that it had executed an agreement with a wholly owned subsidiary of AWE Limited to acquire its 21.25% Participating Interest in the Block 7, Al Barqa Permit, in the Republic of Yemen. The terms of the transaction include a cash consideration of US$1 million, the replacement of AWE's existing Letter of Credit with the Arab Bank, and working capital adjustments on completion.

The Company further announced in May 2014, following the agreement executed with AWE, that it had executed an agreement with Mitsui E&P Middle East B.V. to acquire its 8.5% Participating Interest in the Block 7, Al Barqa Permit, in the Republic of Yemen, thereby increasing Petsec Energy's total interest in Block 7 to 29.75%. The terms of the transaction include a cash consideration of US$0.4 million, the replacement of Mitsui E&P Middle East B.V.'s existing Letter of Credit with the Arab Bank, and working capital adjustments on completion.

Completion of both the AWE and Mitsui transactions is subject to customary approvals from the Joint Venture Partners, the Yemen government and the state owned Yemen Oil and Gas Company. The Company anticipates that these transactions will be completed in 2015.

Reservoir analysis, design and costing of production, storage and transportation facilities for the long term production testing of the Al Meashar Oil Field, was completed in late 2014 and has been presented to the Yemen authorities. Approval to proceed with the testing is anticipated in the first half of 2015.

Oil and gas reserves – USA

As of 1 January 2015, the independently estimated net proved and probable (2P) oil and gas reserves were 1.9 Bcfe, after net reserve sales/additions of 3.3 Bcfe, production of 1.6 Bcfe for the twelve months to 31 December 2014 and net reserve revisions of 0.4 Bcfe.

The table below provides a summary of the independently assessed reserve estimates and movements.

	Independent Assessment[1]		
Gas Equivalent (Bcfe*)	Net Proved Reserves[3]	Net Probable Reserves[3]	Net Proved and Probable Reserves[3]
USA Reserves			
Reserves as of 1 January 2014	6.2	1.0	7.2
Sale/added	(2.7)	(0.6)	(3.3)
Adjustments[2]	(0.3)	(0.1)	(0.4)
Production	(1.6)	–	(1.6)
USA Reserves as of 1 January 2015	**1.6**	**0.3**	**1.9**

* Billion cubic feet of gas equivalent using ratio of six thousand cubic feet of natural gas to one barrel of oil.

1. The independent reserve assessments as of 1 January 2014 and 1 January 2015 were estimated by independent petroleum engineers Ryder Scott Company.
2. Adjustments comprise reserves reclassified and reduced during the period.
3 Net reserves means those reserves representing the Company's net revenue interest which is the Company's working interest less royalties payable.

Qualified Petroleum Reserves and Resources Evaluator

The USA reserve estimates in this report are based on, and fairly represent, information and supporting documentation prepared by, or under the supervision of, qualified petroleum reserves and resources evaluator Mr. John Hamlin, an employee of Ryder Scott Company and a member of the Society of Petroleum Engineers. In accordance with ASX Listing Rule 5.44(b), the reserves statement as a whole was approved by Mr. John Hamlin. Mr. Hamlin has consented in writing to the form and context in which the reserve estimates are presented in this report.

The net reserves have been estimated using a deterministic method. Liquid hydrocarbons are expressed in standard 42 gallon barrels. All gas volumes are reported on an "as sold" basis expressed in millions of cubic feet (MMCF) at the official temperature and pressure bases of the areas in which the gas reserves are located. The net proved and probable (2P) reserves are the summation of the net proved (1P) reserves and net probable reserves.

DIRECTOR'S REPORT CONTINUED

The methodology for the determination of "Recoverable Amount" for the estimated reserves is consistent with that disclosed in the section on "Recoverable Amount" in the Company's 2013 Annual Report released to the market on 17 April 2014. This section covers reserves estimates, material assumptions and technical parameters underpinning the estimates. The Company confirms that it is not aware of any new information or data that materially affects the information included in the "Recoverable Amount" of the 2013 Annual Report, and that all the material assumptions and technical parameters underpinning the estimates therein continue to apply and have not materially changed.

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

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

8. OBJECTIVES, STRATEGY AND FUTURE PERFORMANCE

It is the consolidated entity's objective to increase the market capitalisation of the Company, and ultimately shareholder value, through successful oil and gas exploration, development, and production, and through acquisitions. The consolidated entity intends to produce its current reserves, pursue participation in high quality, high impact exploration drilling opportunities in the Gulf Coast onshore and bay areas of Texas and Louisiana, USA, and in Yemen and explore opportunities to acquire onshore producing oil and gas reserves which hold significant development, exploitation and low risk exploration potential.

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

Drilling and Production Risks

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

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

Operating Risks

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

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

DIRECTOR'S REPORT CONTINUED

Marketing and Sales Risks

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

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

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

- Hedging activities that are intended to reduce the risk of downward price fluctuations on a portion of our future production may limit the Company's potential income if oil and gas prices rise above a level established by its hedge instruments.
- Hedging counterparties require collateral when the mark-to-market value of our hedge instruments is in the counterparties' favour and exceeds the Company's credit limits with such counterparties. As a result, the Company may be required to provide substantial security to the counterparties when commodity prices change significantly. The security provided may be in the form of cash or letters of credit, and thus, could have a significant impact on the Company's liquidity.

Exchange Rate Risks

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

Other Risks

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

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

9. DIVIDENDS

Directors do not recommend the payment of a dividend for the financial year ended 31 December 2014. No dividends were paid during the financial year.

10. SIGNIFICANT CHANGES IN STATE OF AFFAIRS

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

11. ENVIRONMENTAL REGULATION

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

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

12. LIKELY DEVELOPMENTS

The consolidated entity intends to grow its reserve and production base through the prosecution of its 2014/2015 drilling programme in which five committed and three optional conventional exploration wells are planned to be drilled on the Gulf Coast and in the Gulf of Mexico, USA, and to conduct oil production testing on the Al Meashar Oil Field in Block 7, Yemen.

The consolidated entity expects to expose US$7.3 million in prospect and exploration drilling costs on the five committed exploration wells which target prospects ranging in size from 10 to 66 Bcfe gross (2.4 to 6.7 Bcfe net to Petsec Energy) in the USA.

The consolidated entity plans to also pursue opportunities to acquire onshore oil and gas reserves with low risk exploitation and development potential, by way of direct or corporate acquisitions and merger opportunities that have the potential to increase the size and scope of the Company and its operations, and that could be expected to lead to a growth in shareholder value.

In Yemen, the consolidated entity anticipates Yemen government approval for the assignment of the AWE and Mitsui E&P Middle East participating interests to Petsec Energy and for the long-term testing of the Al Meashar oil discovery on Block 7. The Company has budgeted US$3 million for exploration and testing in Block 7 in 2015.

DIRECTOR'S REPORT CONTINUED

13. DIRECTORS' INTERESTS

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

Director	Ordinary Shares	Options over Ordinary Shares
T N Fern	30,826,876	Nil
D A Mortimer	9,326,550	Nil
A P Baden	Nil	Nil
M S Lober	Nil	Nil

14. SHARE OPTIONS

Options granted to directors and officers of the Company

During or since the end of the financial year, no grants of options were made to directors or key management personnel of the Company as part of their remuneration.

As at 31 December 2014, there were 30,000 options over ordinary shares in Petsec Energy Ltd on issue, all of which are employee options exercisable on the Australian Securities Exchange at A$0.20 per share. The options expire on 1 January 2016 and exercise is dependent on completion of certain vesting periods, with no share price hurdles to be achieved. During the year, no options were granted or exercised, and 305,000 options were forfeited.

Shares issued on exercise of options

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

15. INDEMNIFICATION AND INSURANCE OF OFFICERS

During the year ended 31 December 2014, the Company maintained policies of insurance in respect of directors and officers liability. The policies insure persons who are directors or officers of the Company and its controlled entities against certain costs and expenses which may be incurred by them in defending proceedings and against other liabilities which may arise from their positions. The insured directors and officers are the directors, executive officers and secretaries of the Company and the directors, executive officers and secretaries of controlled entities.

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

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

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

16. NON-AUDIT SERVICES

During the year KPMG, the Company's auditor, has performed certain other services in addition to their statutory duties.

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

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

Details of the amounts paid to the auditor of the Company, KPMG, and its related practices for audit and non-audit services provided during the year are set out in Note 9 of the accompanying Financial Statements.

17. LEAD AUDITOR'S INDEPENDENCE DECLARATION

The Lead Auditor's Independence Declaration is set out on page 28 and forms part of the Directors' Report for the financial year ended 31 December 2014.

18. ROUNDING OFF

The Company is of a kind referred to in ASIC Class Order 98/100 dated 10 July 1998 and in accordance with that Class Order, amounts in the Financial Report and Directors' Report have been rounded off to the nearest one thousand dollars, unless otherwise stated.

DIRECTOR'S REPORT CONTINUED

19. EVENTS SUBSEQUENT TO BALANCE DATE

On 7 January 2015, Petsec Energy participated in the drilling of the Ruth R. Bravanec, et al #1 well on the West Crab Lake Prospect in Cameron Parish, onshore Louisiana, with the well reaching its planned true vertical depth of 12,500 feet (12,911 feet measured depth) in late January 2015.

The directional well was drilled to test multiple Lower Miocene age Marg (A) and Discorbis (B) sand reservoirs in a fault closure syncline separated from production in the Marg (A) and Discorbis (B) interval at the Crab Lake Field. The well intersected the target reservoirs as anticipated, but only a few thin zones were hydrocarbon bearing. These zones were too small to warrant completion and development, consequently the well was plugged and abandoned at an estimated cost to the Company of approximately US$0.7 million.

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

This report is made with a resolution of the directors:

T N Fern
Director

Sydney, 24 February 2015

20. REMUNERATION REPORT – AUDITED

20.1 Introduction

This Remuneration Report forms part of the Directors' Report. It outlines the overall remuneration strategy, framework and practices adopted by the Company and the consolidated entity ("Petsec Energy Group") for the year ended 31 December 2014 and has been prepared in accordance with Section 300A of the *Corporations Act 2001* and its regulations.

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

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

20.2 Executive summary

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

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

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

20.2.1 The annual review of key management personnel performance.

20.2.2 Annual review of the Nomination & Remuneration Committee Charter.

20.2.3 The awarding of discretionary bonuses to key management personnel in part as recognition of their personal efforts, and in part to encourage exemplary performance.

20.3 Nomination and Remuneration Committee

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

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

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

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

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

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

DIRECTOR'S REPORT CONTINUED

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

The Nomination and Remuneration Committee's Charter is available on the Company's website www.petsec.com.au.

20.4 Principles of compensation

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

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

The compensation structures take into account:

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

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

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

Fixed compensation

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

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

Performance-linked compensation

Performance-linked compensation includes both short-term and long-term incentives and is designed to reward key management personnel for meeting or exceeding the Company's financial objectives and agreed individual objectives. The short-term incentive (STI) is an "at risk" bonus provided in the form of cash, while the long-term incentive (LTI) is provided as either shares or options over ordinary shares of the Company under the rules of the Employee Share and Option Plans approved by shareholders at the Annual General Meeting held on 22 May 2013 (see note 19(b) to financial statements). The maximum number of securities in aggregate that may be issued under the Employee Share and Option Plans is 15,033,435.

Short-term incentive

Short-term incentives are provided to employees through bonuses and the Company's Nomination and Remuneration Committee has the right to grant discretionary bonuses. Factors considered by the Committee when granting discretionary bonuses include personal performance, the achievement of strategic objectives, and the retention and motivation of employees.

During the year, the Company awarded discretionary bonuses to certain key management personnel in part as recognition of their personal efforts, and in part to encourage exemplary performance.

Long-term incentive

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

No long-term incentives were awarded during the year.

Consequences of performance on shareholder wealth

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

	2014	2013	2012	2011	2010
Profit/(loss) attributable to owners of the company	**($1,048,000)**	($15,210,000)	($5,858,000)	$14,034,000	($35,237,000)
Dividend paid	**–**	–	–	–	–
Change in share price	**$0.025**	($0.09)	$0.06	($0.04)	($0.055)

Net profit/(loss) amounts for 2010 to 2014 have been calculated in accordance with Australian Accounting Standards (AASBs).

DIRECTOR'S REPORT CONTINUED

Service and employment agreements

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

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

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

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

Non-executive directors

Directors' fees are set having regard to periodic advice from external remuneration consultants, market surveys and the level of fees paid relative to those of other comparable companies. Directors' fees for the 2014 year were unchanged from the 2013 year and comprise base fees, plus statutory superannuation for Australian directors. Directors are also entitled to reasonable travel, accommodation and other expenses incurred in attending meetings or while engaged on Company business.

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

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

20.5 Directors' and Executive Officers' Renumeration Report

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

		Short-term benefits				Post-employment benefits		Share-based payment			
		Salary & fees US$	Short-term incentive/ retention cash bonus US$	Other benefits US$	Service agreements US$	Superannuation benefits US$	Termination benefits US$	Accounting fair value US$	Total US$	Proportion of remuneration performance related %	Accounting fair value as proportion of remuneration %
Directors[1]											
Executive											
T N Fern[1] (Note 1) Chairman, Managing Director	**2014**	**–**	**–**	**49,329**	**646,632**	**–**	**–**	**48**	**696,009**	**–**	**–**
	2013	–	–	26,638	694,008	–	–	19,008	739,654	–	2.6
Non-executive											
D A Mortimer[1] Director	**2014**	**58,377**	**–**	**–**	**–**	**5,473**	**–**	**–**	**63,850**	**–**	**–**
	2013	62,654	–	–	–	5,717	–	–	68,371	–	–
A P Baden Director	**2014**	**50,000**	**–**	**–**	**–**	**–**	**–**	**–**	**50,000**	**–**	**–**
	2013	29,167	–	–	–	–	–	–	29,167	–	–
M S Lober Director	**2014**	**50,000**	**–**	**–**	**–**	**–**	**–**	**–**	**50,000**	**–**	**–**
	2013	29,167	–	–	–	–	–	–	29,167	–	–
Former											
M L Harvey Director (resigned 29 May 2013)	**2014**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**
	2013	20,604	–	–	–	–	–	–	20,604	–	–
Total directors remuneration	**2014**	**158,377**	**–**	**49,329**	**646,632**	**5,473**	**–**	**48**	**859,859**	**–**	**–**
	2013	141,592	–	26,638	694,008	5,717	–	19,008	886,963	–	2.1

1 Australian-based directors' remuneration amounts are actually paid in Australian dollars and presented in US dollars at the following average FX rates i) 2014 – 0.8981 ii) 2013 – 0.9639.

DIRECTOR'S REPORT CONTINUED

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

		Short-term benefits				Post-employment benefits		Share-based payment			
		Salary & fees US$ *Note 4*	Short-term incentive/ retention cash bonus[2] US$ *Note 5*	Other benefits US$ *Note 6*	Service agreements US$	Superannuation /401K benefits US$	Termination benefits US$	Accounting fair value US$ *Note 7*	Total US$	Proportion of remuneration performance related %	Accounting fair value as proportion of remuneration %
Executives											
R J Smith Chief Executive Officer of Petsec Energy Inc. (PEI) (appointed 3 March 2014) (Note 2)	**2014**	**241,677**	**70,000**	**23,047**	**–**	**7,250**	**–**	**–**	**341,974**	**20.5**	**–**
	2013	–	–	–	–	–	–	–	–	–	–
R A Keogh President, PEI and Group Chief Financial Officer	**2014**	**280,000**	**70,000**	**29,195**	**–**	**13,000**	**–**	**–**	**392,195**	**17.8**	**–**
	2013	280,000	70,000	34,044	–	12,750	–	–	396,794	17.6	–
R Krenzke Executive Vice President Exploration, PEI	**2014**	**280,000**	**70,000**	**33,997**	**–**	**13,000**	**–**	**–**	**396,997**	**17.6**	**–**
	2013	280,000	70,000	34,044	–	12,750	–	–	396,794	17.6	–
P Gahdmar[1] Company Secretary, Group Financial Controller	**2014**	**151,320**	**25,596**	**8,419**	**–**	**14,194**	**–**	**6,352**	**205,881**	**–**	**3.1**
	2013	175,277	9,639	3,347	–	16,002	–	15,273	219,538	4.4	7.0
Former											
P Webb Vice President Business Development and Land, PEI (resigned 8 May 2013) (Note 3)	**2014**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**
	2013	96,635	–	8,200	–	–	56,250	60,888	221,973	–	27.4
Total executive remuneration	**2014**	**952,997**	**235,596**	**94,658**	**–**	**47,444**	**–**	**6,352**	**1,337,047**	**17.6**	**0.5**
	2013	831,912	149,639	79,635	–	41,502	56,250	76,161	1,235,099	12.1	6.2
Total directors and executive officer remuneration	**2014**	**1,111,374**	**235,596**	**143,987**	**646,632**	**52,917**	**–**	**6,400**	**2,196,906**	**10.7**	**0.3**
	2013	973,504	149,639	106,273	694,008	47,219	56,250	95,169	2,122,062	7.1	4.5

1 Australian-based executive officers' remuneration amounts are actually paid in Australian dollars and presented in US dollars at the following average FX rates i) 2014 – 0.8981 ii) 2013 – 0.9639.

2 2014 short-term incentive/retention cash bonus amounts have been accrued in respect of the 2014 financial year and will be paid in 2015. Bonuses accrued in respect of the 2013 year were paid in 2014.

Notes

1) Included in service agreements above is an amount of US$646,632 (2013: US$694,008) which was paid or is payable to, a company of which Mr Fern is a director.

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

2) Mr Smith was appointed to the role of Chief Executive Officer of the Company's U.S. subsidiary, Petsec Energy Inc., effective 3 March 2014.
3) Mr Webb resigned from his position of Vice President Development and Land of Petsec Energy Inc. on 8 May 2013.
4) Salary and fees for certain specified executives includes the movement during the reporting period of accruals for annual leave and long service leave.
5) Short-term incentive/retention cash bonuses represent discretionary bonus amounts granted based on a number of factors including personal performance, the achievement of strategic objectives, retention and motivation of employees.
6) Other benefits represent amounts paid on behalf of the Managing Director and Executive Officers in respect of insurance, car parking and fringe benefits.
7) The fair value of options is calculated at the date of the grant using the Black-Scholes model and allocated to each reporting period over the period from grant date to vesting date.

No termination benefits or other long-term benefits were paid to key management personnel for the year ended 31 December 2014 (2013: US$56,250).

DIRECTOR'S REPORT CONTINUED

The following table sets out the factors and assumptions used in determining the fair value of the options issued to the above individuals.

Grant date	Expiry date	Average fair value per option	Exercise price	Price of shares on grant date	Estimated volatility	Risk-free interest rate	Dividend yield
29/1/10	31/12/14	A$0.087	A$0.23	A$0.22	62.8%	4.66%	–
16/2/12	31/1/17	A$0.107	A$0.20	A$0.165	117.7%	3.64%	–

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

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

No amounts vest in future financial years in respect of the bonus schemes for the 2014 year.

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

20.7 Equity instruments

Options over equity instruments granted as compensation

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

During 2014, no options over ordinary shares in Petsec Energy Ltd were granted as compensation to key management personnel (2013: nil) and no options vested.

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

	Held at 1 January 2014	Granted as compensation	Exercised	Other changes[1]	Held at 31 December 2014	Vested during the year	Vested and exercisable at 31 December 2014
Directors							
T Fern	–	–	–	–	–	–	–
Executives							
R Smith[2]	–	–	–	–	–	–	–
R Keogh	–	–	–	–	–	–	–
R Krenzke	–	–	–	–	–	–	–
P Gahdmar	200,000	–	–	(200,000)	–	–	–

	Held at 1 January 2013	Granted as compensation	Exercised	Other changes[1]	Held at 31 December 2013	Vested during the year	Vested and exercisable at 31 December 2013
Directors							
T Fern			–	–	–	–	–
Executives							
R Keogh	150,000	–	–	(150,000)	–	–	–
R Krenzke	–	–	–	–	–	–	–
P Webb[3]	1,000,000	–	–	(1,000,000)	–	–	–
P Gahdmar	225,000	–	–	(25,000)	200,000	66,667	–

1 Other changes represent options that expired or were forfeited during the year.
2 Mr. Smith was appointed as Chief Executive Officer of the Company's U.S. subsidiary, Petsec Energy Inc., effective 3 March 2014.
3 Mr. Webb resigned from the Company on 8 May 2013.

Key management personnel related parties held no options.

DIRECTOR'S REPORT CONTINUED

Movements in shares

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

	Held at 1 January 2014	Granted as compensation	Purchases	Received on exercise of options	Sales/ Disposal of relevant interest	Held at 31 December 2014
Directors						
T Fern	30,826,876	–	–	–	–	30,826,876
D Mortimer	9,326,550	–	–	–	–	9,326,550
A Baden	–	–	–	–	–	–
M Lober	–	–	–	–	–	–
Executives						
R Smith	–	–	–	–	–	–
R Keogh	3,612,500	–	–	–	–	3,612,500
R Krenzke	2,250,000	–	–	–	–	2,250,000
P Gahdmar	550,000	–	200,000	–	–	750,000

	Held at 1 January 2013	Granted as compensation	Purchases	Received on exercise of options	Sales/ Disposal of relevant interest	Held at 31 December 2013
Directors						
T Fern	30,826,876	–	–	–	–	30,826,876
D Mortimer	9,326,550	–	–	–	–	9,326,550
A Baden	–	–	–	–	–	–
M Lober	–	–	–	–	–	–
Executives						
R Keogh	3,612,500	–	–	–	–	3,612,500
R Krenzke	2,250,000	–	–	–	–	2,250,000
P Gahdmar	520,000	–	30,000	–	–	550,000

No options have been granted or exercised since the end of the financial year through the date of this report.

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

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

Exercise of options granted as compensation

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

DIRECTOR'S REPORT CONTINUED

Analysis of Movement in Options

During the reporting period, 305,000 options were cancelled and no options were granted or exercised.

The movement during the reporting period, by value, of options over ordinary shares in the Company held by each director and each of the named Company executives is detailed below.

	Value of Options				
2014	Granted in year[1] $	Exercised in year[2] $	Total option value in year A$	Options exercisable during the year A$	Date exercisable
Executives					
P Gahdmar	–	–	–	–	n/a

Details of the movement, by value, of options over ordinary shares in the Company held by each director and each of the named Company executives in the previous corresponding period is detailed below.

	Value of Options				
2013	Granted in year[1] $	Exercised in year[2] $	Total option value in year A$	Options exercisable during the year A$	Date exercisable
Executives					
R Keogh	–	–	–	–	n/a
P Gahdmar	–	–	–	–	n/a

1 The value of options granted in the year is the fair value of the options calculated at grant date using the Black-Scholes model. This amount is allocated to remuneration over the vesting period.

2 The value of options exercised during the year is calculated as the market price of shares of the Company on the ASX as at the close of trading on the date the options were exercised after deducting the price paid to exercise the option.

LEAD AUDITOR'S INDEPENDENCE DECLARATION

UNDER SECTION 307C OF THE *CORPORATIONS ACT 2001*

To: the directors of Petsec Energy Ltd

I declare that, to the best of my knowledge and belief, in relation to the audit for the financial year ended 31 December 2014 there have been:

(i) no contraventions of the auditor independence requirements as set out in the *Corporations Act 2001* in relation to the audit; and

(ii) no contraventions of any applicable code of professional conduct in relation to the audit.

KPMG

KPMG

Anthony Jones
Partner

Sydney, 24 February 2015

CONSOLIDATED STATEMENT OF PROFIT AND LOSS AND OTHER COMPREHENSIVE INCOME

FOR THE YEAR ENDED 31 DECEMBER

	Note	2014 US$'000	2013 US$'000
Revenues from sale of oil & gas		**8,692**	17,656
Royalties paid		**(501)**	(1,238)
Net revenues after royalties		**8,191**	16,418
Other income/(expenses)	5	**2,021**	(21)
Lease operating expenses		**(2,459)**	(3,676)
Geological, geophysical and administrative expenses		**(4,364)**	(5,075)
Depreciation, depletion, and amortisation		**(1,817)**	(7,026)
Exploration and work-over expense		**(54)**	171
Dry hole and impairment expense	7	**(2,965)**	(14,563)
Derivative gains/(losses)	8	**(34)**	(1,287)
Financial income	10	**58**	75
Financial expenses	10	**(224)**	(226)
Profit/(loss) before income tax		**(1,647)**	(15,210)
Income tax benefit/(expense)	11	**599**	–
Profit/(loss) from continuing operations		**(1,048)**	(15,210)
Profit/(loss) for the period		**(1,048)**	(15,210)
Other comprehensive income/(loss)			
Items that may be reclassified subsequently to profit or loss:			
Foreign exchange translation differences		**(130)**	(827)
Cash flow hedges, net of tax		**(2)**	2
Total comprehensive income/(loss) for the period		**(1,180)**	(16,035)

		US Cents	
	Note	2014	2013
Earnings/(loss) per share			
Basic and diluted earnings/(loss) per share	12	**(0.5)**	(6.4)

The statement of profit and loss and other comprehensive income is to be read in conjunction with the notes to the consolidated financial statements set out on pages 33 to 58.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31 DECEMBER

In thousands of USD	Share capital US$'000	Translation Reserve US$'000	Cashflow hedge Reserve US$'000	Share-based compensation US$'000	Accumulated losses US$'000	Total Equity US$'000
Balance at 1 January 2013	186,375	2,743	–	111	(137,301)	51,928
Total comprehensive income for the period						
Profit/(loss) for the period	–	–	–	–	(15,210)	(15,210)
Other comprehensive income						
Foreign exchange translation difference	–	(827)	–	–	–	(827)
Cash flow hedges, net of tax	–	–	2	–	–	2
Total other comprehensive income/(loss)	–	(827)	2	–	–	(825)
Total comprehensive income/(loss) for the period	–	(827)	2	–	(15,210)	(16,035)
Transactions with owners, recorded directly in equity						
Contributions by and distributions to owners						
Shares bought back	(577)	–	–		–	(577)
Vesting of share options	157	–	–	(157)	–	–
Share-based payments expense	–	–	–	103	–	103
Total transactions with owners	(420)	–	–	(54)	–	(474)
Balance at 31 December 2013	185,955	1,916	2	57	(152,511)	35,419
Balance at 1 January 2014	**185,955**	**1,916**	**2**	**57**	**(152,511)**	**35,419**
Total comprehensive income/(loss) for the period						
Profit/(loss) for the period	**–**	**–**	**–**	**–**	**(1,048)**	**(1,048)**
Other comprehensive income/(loss)						
Foreign exchange translation differences	**–**	**(130)**	**–**	**–**	**–**	**(130)**
Cash flow hedges, net of tax	**–**	**–**	**(2)**	**–**	**–**	**(2)**
Total other comprehensive income/(loss)	**–**	**(130)**	**(2)**	**–**	**–**	**(132)**
Total comprehensive income/(loss) for the period	**–**	**(130)**	**(2)**	**–**	**(1,048)**	**(1,180)**
Transactions with owners, recorded directly in equity						
Contributions by and distributions to owners						
Vesting of share options	**46**	**–**	**–**	**(46)**	**–**	**–**
Share-based payments expense	**–**	**–**	**–**	**6**	**–**	**6**
Total transactions with owners	**46**	**–**	**–**	**(40)**	**–**	**6**
Balance at 31 December 2014	**186,001**	**1,786**	**–**	**17**	**(153,559)**	**34,245**

The statement of changes in equity is to be read in conjunction with the notes to the consolidated financial statements set out on pages 33 to 58.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

AS AT 31 DECEMBER

	Note	2014 US$'000	2013 US$'000
ASSETS			
Current assets			
Cash and cash equivalents		**27,290**	20,123
Trade and other receivables	13	**2,206**	3,430
Fair value of derivative financial instruments		**–**	22
Prepayments		**286**	392
Total current assets		**29,782**	23,967
Non-current assets			
Restricted cash deposits[1]		**5,301**	5,300
Receivables	13	**1,093**	1,176
Other financial assets	14	**–**	668
Property, plant and equipment		**144**	99
Exploration, evaluation and development expenditure – Tangible	15(a)	**1,674**	11,806
Exploration and evaluation expenditure – Intangible	15(b)	**2,064**	1,569
Intangible assets – Software		**5**	12
Total non-current assets		**10,281**	20,630
Total assets		**40,063**	44,597
LIABILITIES			
Current liabilities			
Trade and other payables	17	**2,638**	2,572
Fair value of derivative instruments		**–**	20
Rehabilitation provisions	19	**618**	3,721
Employee benefits provisions		**142**	145
Total current liabilities		**3,398**	6,458
Non-current liabilities			
Rehabilitation provisions	19	**2,219**	2,503
Employee benefits provisions		**201**	217
Total non-current liabilities		**2,420**	2,720
Total liabilities		**5,818**	9,178
Net assets		**34,245**	35,419
EQUITY			
Issued capital		**186,001**	185,955
Reserves		**1,803**	1,975
Accumulated losses		**(153,559)**	(152,511)
Total equity		**34,245**	35,419

1 Relates to cash used to guarantee certain future rehabilitation obligations (see *note 24 –Contingencies and Legal Matters for further details*).

The statement of financial position is to be read in conjunction with the notes to the consolidated financial statements set out on pages 33 to 58.

CONSOLIDATED STATEMENT OF CASHFLOW

FOR THE YEAR ENDED 31 DECEMBER

	Note	2014 US$'000	2013 US$'000
Cashflows from operating activities			
Cash receipts from customers		**11,191**	16,800
Cash payments for royalties		**(537)**	(1,303)
Cash payments to suppliers and employees		**(10,168)**	(7,561)
Interest received		**48**	58
Withholding tax refund		**608**	–
Restricted deposits[1]		**–**	125
Net cash from operating activities	30	**1,142**	8,119
Cashflows from investing activities			
Payments for property, plant and equipment		**(93)**	(40)
Payments for exploration, evaluation and development expenditure		**(5,948)**	(9,745)
Payments for investments		**(130)**	(404)
Proceeds from sale of assets		**11,975**	–
Proceeds from sale of investments		**293**	61
Net cash from investing activities		**6,097**	(10,128)
Cashflows from financing activities			
Payments for shares purchased under buy-backs		**–**	(577)
Net cash from financing activities		**–**	(577)
Net increase/(decrease) in cash and cash equivalents		**7,239**	(2,586)
Cash and cash equivalents at 1 January		**20,123**	23,019
Effects of exchange rate changes on cash held		**(72)**	(310)
Cash and cash equivalents at 31 December		**27,290**	20,123

1 Relates to cash used to guarantee certain future rehabilitation obligations (see note 24 – Contingencies and Legal Matters for further details).

The statement of cashflows is to be read in conjunction with the notes to the consolidated financial statements set out on pages 33 to 58.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2014

1. REPORTING ENTITY

Petsec Energy Ltd (the "Company") is a company domiciled in Australia. The registered office of the Company is Level 13, 1 Alfred Street Sydney NSW 2000. The consolidated financial statements of the Company as at and for the year ended 31 December 2014 comprise the Company and its subsidiaries (together referred to as the "consolidated entity").

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

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

2. BASIS OF PREPARATION

(a) Statement of compliance

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

The Board of Directors approved the financial statements on 24 February 2015.

(b) Basis of measurement

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

- Derivative financial instruments are measured at fair value;

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

The consolidated entity is of a kind referred to in ASIC Class Order 98/100 dated 10 July 1998 (updated by CO 05/641 effective 28 July 2005 and CO 06/51 effective 31 January 2006) and in accordance with that Class Order, all financial information presented in US dollars has been rounded to the nearest thousand unless otherwise stated.

(c) Use of estimates and judgements

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

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

In particular, information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amount recognised in the financial statements are described in Note 3(d) – Exploration, evaluation and development expenditure – Intangible and tangible, Note 3(m) Rehabilitation provision and Note 3(r) – Income tax.

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

(d) Going concern basis of preparation

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

3. SIGNIFICANT ACCOUNTING POLICIES

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

(a) Basis of consolidation

(i) Subsidiaries

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

In the Company's financial statements, investments in subsidiaries are carried at the lower of cost and recoverable amount.

(ii) Joint operating arrangements

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

(iii) Transactions eliminated on consolidation

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

(iv) Loss of control

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

(b) Foreign currency

(i) Functional and presentation currency

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

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

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

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

(ii) Foreign currency transactions and balances

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

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

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

(c) Derivative financial instruments and hedging activities

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

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

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

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

(i) Cash flow hedge

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

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

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

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

(iii) Other derivative financial instruments

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

(d) Exploration, evaluation and development expenditure – Intangible and tangible

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

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

3. SIGNIFICANT ACCOUNTING POLICIES CONTINUED

(d) Exploration, evaluation and development expenditure – Intangible and tangible continued

Development expenditures relating to an area of interest are capitalised as tangible deferred costs, and are carried forward to the extent that they are expected to be recouped either through the sale or successful exploitation of the area of interest.

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

(e) Amortisation of exploration, evaluation and development expenditure

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

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

(f) Intangible assets – Software

Software acquired by the consolidated entity, which have finite useful lives, is measured at cost less accumulated amortisation.

(g) Property, plant and equipment

(i) Recognition and measurement

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

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

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

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

(ii) Leased assets

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

(iii) Subsequent costs

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

(iv) Depreciation and amortisation

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

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

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

	2014	2013
Property, plant and equipment		
Furniture and fittings	**5 – 8 years**	5 – 8 years
Office equipment	**3 – 4 years**	3 – 4 years
Leasehold improvements	**5 – 7 years**	5 – 7 years

(h) Impairment – Non-financial assets

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

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

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

The measurement of recoverable amount for the consolidated entity's exploration, evaluation and development expenditure requires significant estimation and judgement. Note 15 provides further details of the key assumptions adopted by the consolidated entity in measuring the recoverable amount of exploration, evaluation and development expenditure.

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

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

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

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

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

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

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

(l) Borrowing costs
Borrowing costs comprise interest payable on borrowings calculated using the effective interest rate method, lease finance charges and amortisation of discounts or premiums relating to borrowings.

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

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

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

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

The rehabilitation provision requires significant estimation and judgement. These estimates include:
- Expected method of remediation;
- Forecast costs-to-complete the future remediation; and
- Anticipated timing of the remediation work.

The consolidated entity monitors the estimates and judgements involved in measuring this provision. Changes in estimated rehabilitation provisions are accounted for on a prospective basis and affect provisions.

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

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

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

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

(iv) Employee incentive plans
Under the employee incentive plan, a liability may be recognised for bonuses for eligible employees based on the consolidated entity's performance for the year based on a number of pre-determined performance criteria.

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

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

3. SIGNIFICANT ACCOUNTING POLICIES CONTINUED

(o) Leases

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

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

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

(p) Revenue and other income recognition

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

Sale of oil and gas

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

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

Sale of non-current assets

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

Interest income

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

(q) Earnings per share

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

(r) Income tax

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

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

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

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

Tax consolidation

The Company and its wholly owned Australian resident entities have formed a tax-consolidated group with effect from 1 July 2002 and are therefore taxed as a single entity from that date. The head entity within the tax-consolidated group is Petsec Energy Ltd.

Current tax expense/income, deferred tax liabilities and deferred tax assets arising from temporary differences of the members of the tax-consolidated group are recognised in the separate financial statements of the members of the tax-consolidated group using the 'separate taxpayer within group' approach by reference to the carrying amount of assets and liabilities in the separate financial statements of each entity and the tax values applying under tax consolidation.

Any current tax liabilities (or assets) and deferred tax assets arising from unused Australian tax losses of the subsidiaries are assumed by the head entity in the tax-consolidated group and are recognised by the Company as amounts payable (receivable) to/(from) other entities in the tax-consolidated group in conjunction with any tax funding arrangement amounts (refer below). Any difference between these amounts is recognised by the Company as an equity contribution or distribution.

The Company recognises deferred tax assets arising from unused tax losses of the tax-consolidated group to the extent that it is probable that future taxable profits of the tax-consolidated group will be available against which the asset can be utilised.

Any subsequent period adjustments to deferred tax assets arising from unused tax losses as a result of revised assessments of the probability of recoverability are recognised by the head entity only.

Nature of tax funding arrangements and tax sharing arrangements

The head entity, in conjunction with other members of the Australian tax-consolidated group, has entered into a tax funding arrangement, which sets out the funding obligations of members of the tax-consolidated group in respect of tax amounts. The tax funding arrangements require payments to/from the head entity equal to the current tax liability/(asset) assumed by the head entity and any tax-loss deferred tax asset assumed by the head entity, resulting in the head entity recognising an inter-entity receivable/(payable) equal in amount to the tax liability/(asset) assumed. The inter-entity receivable/(payable) is at call.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

The head entity in conjunction with other members of the Australian tax-consolidated group has also entered into a tax sharing agreement. The tax sharing agreement provides for the determination of the allocation of income tax liabilities between the entities should the head entity default on its tax payment obligations. No amounts have been recognised in the financial statements in respect of this agreement, as payment of any amounts under the tax sharing agreement is considered remote.

(s) Goods and services tax

Revenues, expenses and assets are recognised net of the amount of goods and services tax (GST), except where the amount of GST incurred is not recoverable from the taxation authority. In these circumstances, the GST is recognised as part of the cost of acquisition of the asset or as part of the expense.

Receivables and payables are stated with the amount of GST included. The net amount of GST recoverable from, or payable to, the taxation authority is included as a current asset or liability in the balance sheet.

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

(t) Segment reporting

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

(u) Changes in accounting policies

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

(v) New standards and interpretations not yet adopted

A number of new standards, amendments to standards and interpretations are effective for annual periods beginning after 1 January 2015, and have not been applied in preparing these consolidated financial statements. Those which may be relevant to the consolidated entity are set out below. The consolidated entity does not plan to adopt these standards early.

(i) AASB 9 Financial Instruments

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

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

The consolidated entity is assessing the potential impact on its consolidated financial statements resulting from the application of AASB 9.

(ii) AASB 15 Revenue from Contracts with Customers

AASB 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaces existing revenue recognition guidance, including AASB 18 *Revenue* and AASB 111 *Construction Contracts*.

AASB 15 is effective for annual reporting periods beginning on or after 1 January 2017, with early adoption permitted.

The consolidated entity is assessing the potential impact on its consolidated financial statements resulting from the application of AASB 15.

4. DETERMINATION OF FAIR VALUES

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

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

Commodity derivatives

The fair values of commodity derivative hedging instruments (level 3 category instruments) are determined relative to the relationship between the agreed contracted fixed and floor prices and estimated future natural gas prices quoted in an active market at period end, taking into account the effect of the Company's own credit risk (when in an asset position) and counterparty credit risk (when in a liability position). The estimated future natural gas prices have been determined using mathematical approximations of market values as of a given date derived from proprietary models and methodologies based on certain assumptions regarding past, present and future market conditions or other factors, or from other sources of pricing information.

Equity securities

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

5. OTHER INCOME AND EXPENSES

	2014 US$'000	2013 US$'000
Other income and expenses		
Production and project overhead income	**57**	57
Net foreign exchange gains / (losses)	**3**	135
Net gain on disposal of assets[1]	**2,232**	–
Net gain on disposal of property, plant and equipment	**75**	149
Net loss on disposal of investments	**5**	3
Change in fair value of investments	**(351)**	(365)
	2,021	(21)

1 **Assets sold during the period**

In July 2014, the consolidated entity sold its working interests in the Marathon and Main Pass 270 fields, together with certain associated exploration interests within the USA segment.

The consolidated statement of profit or loss and cash flows generated from these assets prior to disposal in July 2014 are detailed below:

	2014 US$'000
Revenue	6,794
Expenses	(2,830)
Results from operating activities	**3,964**
Net cash from operating activities	**4,928**

The profit from the assets sold of $2,232,000 is attributable entirely to the owners of the Company.

6. PERSONNEL EXPENSES

	2014 US$'000	2013 US$'000
Wages and salaries	**1,414**	1,442
Service agreements for executives	**647**	694
Contract labour	**312**	300
Superannuation & 401(k) plans	**63**	67
Share-based payment compensation	**6**	111
Other employee-related expenses	**1**	1
	2,443	2,615

7. PROFIT/(LOSS) FOR THE PERIOD

	2014 US$'000	2013 US$'000
Profit/(loss) for the period includes the following items that are significant because of their nature, size or incidence:		
Expenses		
Dry hole and impairment expense	**(2,965)**	(14,563)

Impairment and abandonment expense

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

During the current period, the consolidated entity incurred total dry hole and impairment expense of US$2,965,000, mainly comprised dry hole costs pertaining to the unsuccessful Main Pass 18 G-6 well recompletion (US$1.2 million), the Herbert #1 well drilled on the Southwest Holmwood prospect (US$1.6 million), and pre-drill costs of US$0.2 million associated with the West Crab Lake prospect drilled in January 2015.

In the previous corresponding period, the consolidated entity recognised a net impairment charge of US$14,563,000. This amount comprised an impairment of US$7.9 million against the Company's total share of costs incurred to-date in respect of its shale oil projects in Canada and Texas, US$6.2 million impairment against the Main Pass 270 field due to reserve revisions, additional abandonment provisioning of US$0.3 million and US$0.2 million impairment against certain lease costs.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

8. DERIVATIVE GAINS/(LOSSES)

The following table presents details of the change in fair value recognised in the current and comparative period:

	2014 US$'000	2013 US$'000
Change in fair value of securities held in unrelated entities	**(174)**	(1,287)
Net derivative gain on liquidation of swap hedge contracts	**140**	–
	(34)	(1,287)

The consolidated entity holds share options in an unrelated entity. The carrying amount of the share options is measured at fair value using the Black-Scholes-Merton formula. Measurement inputs include the share price on the measurement date, the exercise price of the instrument, expected volatility, expected term of the instruments, expected dividends and the risk free interest rate (based on Australian government bonds). Changes therein are recognised immediately in profit or loss.

The share options are categorised as a level 2 financial instrument as the measurement inputs used in the calculation of the fair value of these instruments requires the use of inputs other than quoted prices that are observable in the market, either directly (as prices) or indirectly (derived from prices). Refer to Note 21 for further details.

During the year, the consolidated entity held natural gas swap derivative contracts to hedge the price risk associated with selling a portion of its 2014 gas production. Following the divestiture of its interests in the Marathon and Main Pass 270 producing fields, the Company liquidated its July through December 2014 natural gas futures contracts, realising a net derivative gain of US$140,000.

9. AUDITOR'S REMUNERATION

	2014 US$	2013 US$
Audit services:		
Auditors of the Company		
KPMG Australia		
Audit and review of financial reports	**98,578**	83,578
Overseas KPMG Firms		
Audit and review of financial reports	**–**	27,510
Other services:		
Auditors of the Company		
KPMG Australia		
Corporate, tax and compliance services	**–**	–
	98,578	111,088

10. FINANCE INCOME AND EXPENSE

	2014 US$'000	2013 US$'000
Interest income – Other parties	**58**	75
Financial income	**58**	75
Interest expense		–
Unwinding of discount	**(224)**	(226)
Financial expense	**(224)**	(226)
Net financial income	**(166)**	(151)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

11. INCOME TAX EXPENSE

	2014 US$'000	2013 US$'000
Recognised in the statement of comprehensive income		
Deferred tax expense		
Origination and reversal of temporary differences	–	–
Total income tax benefit/(expense) in the statement of comprehensive income	–	–
Numerical reconciliation between tax expense and pre-tax net profit/(loss)		
Profit/(loss) before tax	(1,048)	(15,210)
Income tax expense/(benefit) using the Australian corporation tax rate of 30% (2013: 30%)	(314)	(4,563)
Increase/(decrease) in income tax expense due to:		
Non-deductible expenses	438	899
U.S. income taxes assessed at different rate	(19)	(289)
Canadian income taxes assessed at different rate	1	344
Deferred tax movements not brought to account in current year	(106)	3,609
U.S. withholding tax refund	(599)	–
Under/(over) provided in prior years	–	–
Income tax expense/(benefit) on pre-tax net profit/(loss)	(599)	–

12. EARNINGS PER SHARE

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

In addition to the ordinary shares, the Company has 30,000 (2013: 335,000) options outstanding under the Employee Option Plan. In determining potential ordinary shares, 30,000 (2013: 335,000) are not dilutive.

During the year, no options were granted and 305,000 were forfeited. No options were exercised and converted to ordinary shares.

Basic earnings/ (loss) per share

The calculation of basic earnings/ (loss) per share at 31 December 2014 was based on the loss attributable to ordinary shareholders of US$1,048,000 (2013: Loss of US$15,210,000) and a weighted average number of ordinary shares outstanding during the year ended 31 December 2014 of 231,161,630 (2013: 237,276,614), calculated as follows:

Profit/ (loss) attributable to ordinary shareholders

	2014 US$'000	2013 US$'000
Profit/(loss) for the period	(1,048)	(15,210)

Weighted average number of shares (basic)

In thousands of shares	2014	2013
Issued ordinary shares at 1 January	231,162	237,684
Effect of shares issued in 2014 and 2013, respectively	–	(407)
Weighted average number of ordinary shares at 31 December	231,162	237,277

Earnings/(loss) per share

In USD cents	2014	2013
Basic and diluted earnings/(loss) per share	(0.5)	(6.4)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

13. TRADE AND OTHER RECEIVABLES

	2014 US$'000	2013 US$'000
Current		
Trade receivables	**2,194**	3,419
Other receivables	**12**	11
	2,206	3,430
Non-current		
Loan receivable from related parties	**1,093**	1,176
	1,093	1,176

14. OTHER FINANCIAL ASSETS

	2014 US$'000	2013 US$'000
Investments in unrelated entities	**–**	668
	–	668

15. EXPLORATION, EVALUATION AND DEVELOPMENT EXPENDITURE

	2014 US$'000	2013 US$'000
(a) Tangible		
Costs carried forward in respect of areas of interest in the following phases:		
Production phase – at WDV		
Balance at 1 January	**11,806**	22,061
Additions	**3,328**	3,146
Disposals	**(10,522)**	–
Dry hole and impairment expense	**(1,251)**	(6,416)
Current year amortisation expense	**(1,687)**	(6,985)
Balance at 31 December	**1,674**	11,806
Exploration and/or evaluation phase – at cost		
Balance at 1 January	**–**	3,448
Additions	**1,558**	765
Dry hole and impairment expense	**(1,558)**	(4,213)
Balance at 31 December	**–**	–
Total costs carried forward	**1,674**	11,806
(b) Intangible		
Costs carried forward in respect of areas of interest in the following phase:		
Exploration and/or evaluation phase – at cost		
Balance at 1 January	**1,569**	3,580
Additions	**735**	1,658
Disposals	**(84)**	–
Impairment expense	**(156)**	(3,669)
Balance at 31 December	**2,064**	1,569

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

15. EXPLORATION, EVALUATION AND DEVELOPMENT EXPENDITURE CONTINUED

Recoverable amount

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

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

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

Risk of future impairments

The determination of the estimated recoverable amount of Petsec's producing oil and gas properties is highly sensitive to a change in estimated recoverable reserves and oil and gas prices.

As a result of historical impairments, certain properties are carried at recoverable amounts. Consequently any reduction in recoverable reserves or a reduction in the oil or gas price may trigger the need for further impairment on these specific properties.

16. DEFERRED TAX ASSETS

Recognised deferred tax assets and liabilities

	Assets		Liabilities		Net	
	2014 US$'000	2013 US$'000	2014 US$'000	2013 US$'000	2014 US$'000	2013 US$'000
Exploration, evaluation and development expenditure	**3,656**	5,125	**–**	–	**3,656**	5,125
Other items	**484**	104	**–**	–	**484**	104
Deferred tax balances not brought to account	**(4,140)**	(5,229)	**–**	–	**(4,140)**	(5,229)
Deferred tax assets/(liabilities)	**–**	–	**–**	–	**–**	–

Unrecognised deferred tax assets

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

	2014 US$'000	2013 US$'000
Deductible temporary differences in USA (net)	**4,140**	5,229
Tax operating loss carry-forwards in USA (net)	**31,492**	31,554
Deductible temporary differences in Canada (net)	**1,717**	1,747
Tax operating loss carry-forwards in Canada (net)	**223**	192
Deductible temporary differences in Australia (net)	**103**	75
Tax operating loss carry-forwards in Australia (net)	**3,004**	2,314
	40,679	41,111

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

16. DEFERRED TAX ASSETS CONTINUED

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

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

Movement in temporary differences during the year

	Balance 1 Jan 13 US$'000	Recognised in income US$'000	Recognised in equity US$000	Reclassified to other balance sheet account US$000	Balance 31 Dec 13 US$'000
Exploration, evaluation and development expenditure	2,436	2,689	–	–	5,125
Other items	302	(198)	–	–	104
Deferred tax balances in USA not brought to account	(2,738)	(2,491)	–	–	(5,229)
	–	–	–	–	–

	Balance 1 Jan 14 US$'000	Recognised in income US$'000	Recognised in equity US$000	Reclassified to other balance sheet account US$000	Balance 31 Dec 14 US$'000
Exploration, evaluation and development expenditure	**5,125**	**(1,469)**	**–**	**–**	**3,656**
Other items	**104**	**380**	**–**	**–**	**484**
Deferred tax balances in USA not brought to account	**(5,229)**	**1,089**	**–**	**–**	**(4,140)**
	–	**–**	**–**	**–**	**–**

17. TRADE AND OTHER PAYABLES

	2014 US$'000	2013 US$'000
Current		
Trade and other payables, stated at cost		
Trade payables	**844**	668
Exploration and development accruals	**150**	429
Operational and administration accruals	**1,599**	1,453
Related party payables	**45**	22
	2,638	2,572

18. EMPLOYEE BENEFITS

(a) Superannuation/pension plans

The consolidated entity contributes to several defined contribution employee superannuation plans in Australia. Employer contributions are based on various percentages of their gross salaries. The consolidated entity is under no legal obligation to make contributions in excess of those specified in Superannuation Industry (Supervision) legislation. The amount recognised, as expense was, US$23,000 for the year ended 31 December 2014 (2013: US$29,000).

U.S. based employees are eligible to participate in a voluntary retirement savings plan under Section 401(k) of the US tax code ("401(k) plan"). Employer matching contributions under the 401(k) plan recognised as an expense was US$40,000 for the year ended 31 December 2014 (2013: US$38,000).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

18. EMPLOYEE BENEFITS CONTINUED

(b) Share-based payments

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

Employee Share Plan

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

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

In thousands of shares	Weighted average share price 2014	Number of shares 2014	Weighted average share price 2013	Number of shares 2013
Outstanding at the beginning of the period	**A$0.20**	**2,400**	A$0.20	2,400
Granted during the period	**–**	**–**	–	–
Forfeited during the period	**–**	**–**	–	–
Outstanding at the end of the period	**A$0.20**	**2,400**	A$0.20	2,400

No new shares were granted under the Company's Employee Share Plan ("ESP") to key management personnel as long term incentive compensation during the current year (2013: Nil).

Employee Option Plan

The following sets forth the share-based compensation transactions under the Company's Employee Option Plan.

The number and weighted average exercise prices of share options, is as follows:

In thousands of options	Weighted average exercise price 2014	Number of options 2014	Weighted average exercise price 2013	Number of options 2013
Outstanding at the beginning of the period	**A$0.23**	**335**	A$0.24	2,007
Granted during the period		**–**	–	–
Exercised during the period		**–**	–	–
Forfeited during the period	**A$0.23**	**305**	A$0.25	1,672
Outstanding at the end of the period	**A$0.20**	**30**	A$0.23	335
Exercisable at the end of the period	**A$0.20**	**20**	A$0.23	315

The options outstanding at 31 December 2014 have an exercise price of A$0.20 and a weighted average contractual life of 1.0 years. During the year, no share options were exercised (2013: Nil).

Each option is convertible to one ordinary share. The exercise prices of the options, determined in accordance with the Rules of the plan, are based on the ruling market prices when the options are issued.

All options expire on the earlier of their expiry date or when the holder's employment ceases unless otherwise approved by the Remuneration Committee. Options may not be exercised until they are vested and thereafter exercise is conditional on satisfaction of share price hurdles and the terms of issue. The vesting periods range from six months to four years after granting. The plan does not represent remuneration for past services.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

18. EMPLOYEE BENEFITS CONTINUED

The terms and conditions of the option grants are as follows, whereby all options are settled by physical delivery of shares:

Grant date/employees entitled	Number of instruments	Contractual life of options
Option grant to other personnel at 31 July 2012	30,000	2.92 years
Total share option schemes with all or a portion of options outstanding at 31 December 2014	**30,000**	

The fair value of services received in return for share options granted are measured by reference to the fair value of share options granted. The estimate of the fair value of the services received is measured using an option pricing model – the Black-Scholes-Merton formula. The contractual life of the option is used as an input into this model.

Share and option grants to key management personnel

No share or option grants were made to key management personnel during the year ended 31 December 2014 (2013: Nil).

The following table summarises the fair value assumptions of shares and options granted to key management personnel during the years ended 31 December 2014 and 2013.

	Key management personnel 2014	Key management personnel 2013
Weighted average fair value at measurement date	–	–
Weighted average share price	–	–
Weighted average exercise price	–	–
Expected volatility (expressed as weighted average used in the modelling under Black-Scholes model)	–	–
Expected option life (expressed as weighted average used in the modelling under Black-Scholes model)	–	–
Expected dividends	–	–
Risk-free interest rate (based on national government bonds)	–	–

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

Shares and options are granted under a service condition and minimum share price hurdles. Such conditions are not taken into account in the grant date fair value measurement of the services received, however, are considered in assumptions about the number of shares and options that are expected to become exercisable.

19. REHABILITATION PROVISIONS

	2014 US$'000	2013 US$'000
Current		
Balance at 1 January	**3,721**	147
Provisions made during the year	**62**	250
Provisions reclassed from non-current classification	**24**	3,525
Provisions used during the year	**(3,189)**	(201)
Balance at 31 December	**618**	3,721
Non-current		
Balance at 1 January	**2,503**	5,756
Provisions made during the year	**17**	46
Sale of interests	**(501)**	–
Provisions reclassed to current classification	**(24)**	(3,525)
Unwind of discount	**224**	226
Balance at 31 December	**2,219**	2,503
	2,837	6,224

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

20. CAPITAL AND RESERVES

Share capital

	Ordinary Shares	
In thousands of shares	**2014**	**2013**
On issue at 1 January	**231,162**	237,684
Shares bought back	–	(6,522)
On issue at 31 December – fully paid	**231,162**	231,162

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

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

Translation reserve

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

Cash flow hedge reserve

The hedging reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions that had not yet transpired.

Share-based compensation

The share-based compensation represents the value of unvested options issued under the Company's Employee Option Plan.

Capital management

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

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

21. FINANCING ARRANGEMENTS AND ADDITIONAL FINANCIAL INSTRUMENTS DISCLOSURES

Financing arrangements

At 31 December 2014, the consolidated entity had no debt outstanding (2013: Nil).

Additional financial instruments disclosures

Overview

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

- Credit risk
- Liquidity risk
- Market risk

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

Risk Management Framework

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

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

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

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

Credit risk

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

21. FINANCING ARRANGEMENTS AND ADDITIONAL FINANCIAL INSTRUMENTS DISCLOSURES CONTINUED

Exposure to credit risk

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

	Consolidated	
	2014 US$'000	2013 US$'000
Cash and restricted cash deposits	**32,591**	25,423
Trade and other receivables	**2,206**	3,430
	34,797	28,853

As at 31 December 2014, there was no material exposure to credit risk in relation to cash held by banks as $11.5 million was held with Australian financial institutions rated AA with the remaining balances held in the USA with institutions rated A or higher.

Where possible, the consolidated entity manages its credit risk on trade receivables by dealing with only large reputable customers for its oil and gas sales. Following the consolidated entity's divestment of its two main producing fields during the year, approximately 47% of trade and other receivables were due from two such customers at balance date. The remainder of the receivables were due mainly from a number of joint owners of the jointly owned properties. The consolidated entity does not consider there to be any impairment indicators associated with these debtors. The consolidated entity's credit risk is limited to the carrying value of its financial assets. None of the consolidated entity's receivables are materially past due (2013: is consistent with 2014).

Liquidity risk

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

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

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

		Contractual cashflows				
31 December 2014	Carrying amount US$000	6 mths or less US$000	6 – 12 mths US$000	1 – 2 years US$000	2 – 5 years US$000	5 years or more US$000
Trade and other payables	**2,638**	**2,638**			**–**	**–**
Total	**2,638**	**2,638**			**–**	**–**

		Contractual cashflows				
31 December 2013	Carrying amount US$000	6 mths or less US$000	6 – 12 mths US$000	1 – 2 years US$000	2 – 5 years US$000	5 years or more US$000
Fair value of derivative instruments	20	11	9			
Trade and other payables	2,572	2,572	–	–	–	–
Total	2,592	2,583	9	–	–	–

Market risk

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

Foreign exchange risk

During 2013 and 2014, operating costs were incurred in Australian, Canadian and US dollars.

Throughout 2013 and 2014, the consolidated entity held the majority of its liquid funds in US dollars.

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

21. FINANCING ARRANGEMENTS AND ADDITIONAL FINANCIAL INSTRUMENTS DISCLOSURES CONTINUED

Commodity price risk

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

Swaps

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

Collars

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

At 31 December 2014, the consolidated entity had no outstanding oil or natural gas hedges in place. In the previous corresponding period, the consolidated entity had the following outstanding natural gas hedges in place:

Production period	Hedge types	Total MMBtu volume	Weighted average US$ Price/MMBtu
2014	Swaps	912,500	4.17

Interest rate risk

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

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

	2014 US$'000	2013 US$'000
Financial assets		
Cash and restricted cash deposits	**32,591**	25,423
	32,591	25,423

Sensitivity analysis

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

The estimated impact of a 10 per cent change in the average commodity price for the year ended 31 December 2014 would have increased or decreased the consolidated entity's profit or loss by US$630,000 (2013: US$984,000) excluding potential impact of impairments. The estimated impact of a change of 100 basis points in interest rates would have increased or decreased the consolidated entity's profit or loss by US$6,000 (2013: US$8,000). The estimated impact of a 10 per cent change in the USD/AUD and USD/CAD exchange rates would have increased or decreased the consolidated entity's profit or loss by a total of US$75,000 (2013: US$870,000).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

21. FINANCING ARRANGEMENTS AND ADDITIONAL FINANCIAL INSTRUMENTS DISCLOSURES CONTINUED

Fair values of financial assets and liabilities

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

	2014		2013	
	Carrying amount US$'000	Fair value US$'000	Carrying amount US$'000	Fair value US$'000
Trade and other receivables	**2,206**	**2,206**	3,430	3,430
Cash and restricted cash deposits	**32,591**	**32,591**	25,423	25,423
Financial derivative instruments – assets	**–**	**–**	22	22
Financial derivative instruments – liabilities	**–**	**–**	(20)	(20)
Trade and other payables	**(2,638)**	**(2,638)**	(2,572)	(2,572)
	32,159	**32,159**	26,283	26,283

The carrying values of all other financial assets and liabilities are estimated to approximate fair value because of their short maturity.

The carrying amounts shown in the balance sheet of the Company are equal to fair value.

The following tables detail the consolidated entity's fair values of financial instruments categorised by the following levels:

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

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

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

2014	Level 1 US$000	Level 2 US$000	Level 3 US$000	Total US$000
Assets				
Fair value of derivative financial instruments (net)	–	–	–	–
Other financial assets	–	–	–	–
Total assets	–	–	–	–

2013	Level 1 US$000	Level 2 US$000	Level 3 US$000	Total US$000
Assets				
Fair value of derivative financial instruments (net)	–	–	2	2
Other financial assets	495	173	–	668
Total assets	495	173	2	670

Unless otherwise stated, the carrying amounts of financial instruments reflect their fair value.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

22. OPERATING LEASES

Leases as lessee

Non-cancellable operating lease rentals are payable as follows:

	2014 US$'000	2013 US$'000
Less than one year	**366**	261
Between one and five years	**361**	246
	727	507

The consolidated entity leases office space in Australia and the USA under operating leases. The leases typically run for a period of 3 years. None of the leases includes contingent rentals.

During the year ended 31 December 2014, US$540,000 was recognised as an expense in the statement of comprehensive income in respect of operating leases including month-to-month leases (2013: US$842,000).

23. CAPITAL AND OTHER COMMITMENTS

	2014 US$'000	2013 US$'000
Capital expenditure commitments		
Exploration, evaluation and development expenditure		
Contracted but not provided for and payable:		
Within one year	**3,680**	330
One year or later and no later than five years	**–**	–
	3,680	330

24. CONTINGENCIES AND LEGAL MATTERS

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

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

The Company's U.S. subsidiary, Petsec Energy Inc. ("PEI") is required to provide bonding or security for the benefit of U.S. regulatory authorities and certain lease operators in relation to its obligations to pay lease rentals and royalties, the plugging and abandonment of oil and natural gas wells, and the removal of related facilities. As of 31 December 2014, the consolidated entity was contingently liable for US$5,301,000 of surety and supplemental bonds (2013: US$5,300,000) issued through a surety company to secure those obligations. At balance date US$5,301,000 of these bonds were collateralised by cash (2013: US$5,300,000).

25. DEED OF CROSS GUARANTEE

Pursuant to an ASIC Class Order 98/1418 dated 13 August 1998, relief is granted to certain wholly owned Australian subsidiaries of the Company from the *Corporations Act* requirements for preparation, audit, and publication of Financial Reports and Directors' Reports.

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

The subsidiaries subject to the Deed are:

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

25. DEED OF CROSS GUARANTEE CONTINUED

A consolidated statement of comprehensive income and consolidated balance sheet, comprising the Company and subsidiaries which are a party to the Deed, after eliminating all transactions between parties to the Deed of Cross Guarantee, as at 31 December 2014 and 2013, is set out as follows:

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

	2014 US$000	2013 US$000
Other income and expenses	8,008	9,496
Operating expenses	(1,680)	(1,846)
Finance income	58	76
Net movement in provisions against loans and investments in controlled entities	(18,210)	(12,271)
Profit/(loss) before tax	(11,824)	(4,545)
Income tax benefit/(expense)	599	–
Profit/(loss) after tax	(11,225)	(4,545)
Other comprehensive income	–	–
Total comprehensive income for the period	(11,225)	(4,545)
Retained earnings/(accumulated losses) at beginning of year	(164,758)	(160,213)
Retained earnings/(accumulated losses) at end of year	(175,983)	(164,758)

Balance sheet

	2014 US$000	2013 US$000
Assets		
Cash and cash equivalents	11,450	12,376
Other receivables	740	885
Prepayments	71	77
Total current assets	12,261	13,338
Loans receivable from controlled entities	16	–
Loans receivable from related parties	1,093	1,176
Other financial assets	23,042	18,619
Other investments	1,018	18,856
Property, plant and equipment	36	49
Total non-current assets	25,205	38,700
Total assets	37,466	52,038
Liabilities		
Trade and other payables	202	205
Employee benefits provision	25	30
Total current liabilities	227	235
Loans payable to controlled entities	485	543
Employee benefits provision	201	217
Total non-current liabilities	686	760
Total liabilities	913	995
Net assets	36,553	51,043
Equity		
Issued capital	186,001	185,955
Reserves	26,535	29,846
Retained earnings/(accumulated losses)	(175,983)	(164,758)
Total equity	36,553	51,043

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

26. CONSOLIDATED ENTITIES

		Ownership interest	
	Country of Incorporation	2014 %	2013 %
Parent entity			
Petsec Energy Ltd			
Significant subsidiaries			
Petsec Investments Pty. Limited	Australia	**100**	100
Petroleum Securities Pty. Limited	Australia	**100**	100
Najedo Pty. Limited	Australia	**100**	100
Petroleum Securities Share Plan Pty. Limited	Australia	**100**	100
Petsec America Pty. Limited	Australia	**100**	100
Petsec (U.S.A.) Inc.	USA	**100**	100
Petsec Energy Inc.	USA	**100**	100
Petsec Exploration and Production LLC	USA	**100**	100
Petsec Energy Resources Inc.	USA	**100**	100
Petsec Energy Canada Ltd	Canada	**100**	100
Laurel Bay Petroleum Limited	Australia	**100**	100
Ginida Pty. Limited	Australia	**100**	100
Western Medical Products Pty. Limited	Australia	**100**	100
Petsec Energy Yemen Ltd[1]	British Virgin Islands	**100**	–

1 Petsec Energy Yemen Ltd was incorporated on 17 March 2014 and holds the consolidated entity's interests in Block 7, Al Barqa Permit in the Republic of Yemen.

With the exception of Petsec Energy Yemen Ltd, all entities carry on business in the country where they were incorporated.

27. SEGMENT REPORTING

The consolidated entity operates in the oil and gas industry.

Segment information is presented in the consolidated financial statements in respect of the consolidated entity's geographic segments, which reflects the presentation of information to the chief operating decision maker and may differ from the information required to be disclosed in accordance with the Accounting Standards.

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

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

	Australia		USA		Canada		Yemen		Consolidated	
	2014 US$'000	2013 US$'000	2014 US$'000	2013 US$'000	2014 US$'000	2013 US$'000	2014 US$'000	2013 US$'000	2014 US$'000	2013 US$'000
Oil and gas sales and royalties	**–**	–	**8,692**	17,656	**–**	–	**–**	–	**8,692**	17,656
Royalties paid	**–**	–	**(501)**	(1,238)	**–**	–	**–**	–	**(501)**	(1,238)
Net revenues after royalties*	**–**	–	**8,191**	16,418	**–**	–	**–**	–	**8,191**	16,418
Segment net profit/(loss) before tax	**(2,022)**	(2,412)	**404**	(5,921)	**(20)**	(6,877)	**(9)**	–	**(1,647)**	(15,210)
Income tax expense	**599**	–	**–**	–	**–**	–	**–**	–	**599**	–
Profit/(loss) after tax	**(1,423)**	(2,412)	**404**	(5,921)	**(20)**	(6,877)	**(9)**	–	**(1,048)**	(15,210)
Depreciation, depletion, amortisation & reclamation	**13**	13	**1,739**	6,985	**65**	28	**–**	–	**1,817**	7,026
Dry hole, impairment and abandonment expense	**–**	–	**3,057**	7,786	**(92)**	6,777	**–**		**2,965**	14,563
Exploration and work-over expense	**–**	–	**(54)**	171	**–**	–	**–**		**(54)**	171
Segment assets	**12,663**	14,356	**27,392**	30,222	**–**	19	**8**	–	**40,063**	44,597
Acquisition of property, plant and equipment and exploration, evaluation and development assets	**4**	40	**6,029**	6,563	**–**	3,182	**8**	–	**6,041**	9,785

* There are no inter-segment sales

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

27. SEGMENT REPORTING CONTINUED

	Australia		USA		Canada		Yemen		Consolidated	
	2014 US$'000	2013 US$'000	2014 US$'000	2013 US$'000	2014 US$'000	2013 US$'000	2014 US$'000	2013 US$'000	2014 US$'000	2013 US$'000
Segment liabilities	**429**	569	**5,319**	8,520	**70**	89	**–**	–	**5,818**	9,178
Cash flows from operating activities	**(961)**	(1,933)	**2,067**	10,113	**45**	(61)	**(9)**	–	**1,142**	8,119
Cash flows from investing activities	**167**	(383)	**5,938**	(6,563)	**–**	(3,182)	**(8)**	–	**6,097**	(10,128)
Cash flows from financing activities	**–**	(578)	**–**	–	**–**	–	**–**	–	**–**	(578)

28. INTERESTS IN UNINCORPORATED JOINT OPERATING ARRANGEMENTS

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

	2014 US$'000	2013 US$'000
Assets		
Exploration, evaluation and development expenditure – Tangible:		
Leases now in production		
Producing leases – at cost	**38,831**	94,823
Less: accumulated amortisation and impairment	**(37,157)**	(83,298)
	1,674	11,525
Represented by the following lease carrying values:		
– Main Pass 270[1]	**–**	4,127
– Main Pass 19	**–**	16
– Atchafalaya Bay[1]	**–**	7,382
– Jeanerette Field	**1,674**	–
Total exploration, evaluation and development expenditure – Tangible	**1,674**	11,525
Exploration and evaluation expenditure – Intangible:		
Not in production		
– Block 7, Yemen	**8**	–
– Onshore Louisiana	**572**	–
– Other Gulf of Mexico leases	**1,484**	1,569
Total exploration, evaluation and development expenditure – Intangible	**2,064**	1,569
Liabilities		
Rehabilitation provision:		
– Main Pass 19	**2,017**	1,831
– Main Pass 270	**–**	422
– Other Gulf of Mexico leases	**250**	250
– Onshore Louisiana	**167**	147
– Atchafalaya Bay	**–**	52
– Onshore Canada	**69**	27
	2,503	2,729
The contribution of the consolidated entity's joint operating arrangements to EBIT (including exploration write-offs and impairments; and excluding the effects of hedging and any gain on sale of interests):		
– Main Pass 19	**20**	(183)
– Main Pass 270[1]	**169**	(5,935)
– Atchafalaya Bay[1]	**3,662**	5,463
– Jeanerette Field	**370**	–
– Onshore Louisiana	**(1,817)**	–
– Other Gulf of Mexico leases	**(69)**	(497)
– Onshore Canada	**92**	(6,877)
	2,427	(8,029)

1. The consolidated entity sold its working interests in the Main Pass 270 and Atchafalaya Bay fields together with certain associated exploration interests in July 2014.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

28. INTERESTS IN UNINCORPORATED JOINT OPERATING ARRANGEMENTS CONTINUED

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

	Interest held 2014	Interest held 2013
– Main Pass 19	**55.00%**	55.00%
– Main Pass 270[1]	**–**	22.50%
– Atchafalaya Bay[1]	**–**	8.00%
– Onshore Louisiana	**12.50% to 45.00%**	–
– Onshore Canada	**24.50%**	24.50%
– Other Gulf of Mexico leases[1]	**12.50% to 75.00%**	37.50% to 75.00%
– Block 7, Republic of Yemen[2]	**29.75%**	–

1 The consolidated entity sold its working interests in the Main Pass 270 and Atchafalaya Bay fields together with certain associated exploration interests in July 2014.

2 The interests acquired in Block 7, Al Barqa Permit, in the Republic of Yemen are subject to customary approvals from the Joint Venture Partners, the Yemen government and the state owned Yemen Oil and Gas Company.

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

29. WHOLLY OWNED AREAS OF INTEREST

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

	2014 US$'000	2013 US$'000
Assets		
Exploration, evaluation and development expenditure – Tangible:		
Leases now in production		
Producing leases – at cost	**49,600**	48,429
Less: accumulated amortisation and impairments	**(49,600)**	(48,148)
	–	281
Represented by the following lease carrying values:		
– Main Pass 18	**–**	281
– Chandeleur 31/32[1]	**–**	–
Total exploration and evaluation expenditure – Intangible	**–**	281
Liabilities		
Rehabilitation provision:		
– Main Pass 18	**182**	172
– Chandeleur 31/32[1]	**152**	3,323
	334	3,495
The contribution of the consolidated entity's areas of interest to EBIT (including exploration write-offs and impairments; and excluding the effects of hedging):		
– Chandeleur 31/32[1]	**(54)**	(152)
– Main Pass 18	**(1,230)**	433
	(1,284)	281

1 The Chandeleur 31/32 Area field reached the end of its productive life in August 2013 and was decommissioned in August 2014.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

30. RECONCILIATION OF CASH FLOWS FROM OPERATING ACTIVITIES

	2014 US$'000	2013 US$'000
Cash flows from operating activities		
Profit/(loss) for the period	**(1,048)**	(15,210)
Adjustments for:		
Depreciation, depletion and amortisation	**1,817**	7,026
Dry-hole, impairment and abandonment expense	**2,965**	14,563
Work-over expense	**54**	(268)
Net movement in fair value of investments	**524**	1,652
Net foreign exchange losses/(gains)	**(3)**	(135)
Net loss/(gain) on assets	**(2,232)**	–
Net loss/(gain) on property, plant and equipment	**(75)**	(149)
Net loss/(gain) on investments	**(5)**	(3)
Share-based payment expenses	**6**	111
Operating profit before changes in working capital and provisions	**2,003**	7,587
Decrease/(increase) in restricted cash deposits	**–**	125
Decrease/(Increase) in receivables and prepayments	**1,330**	(712)
(Decrease)/Increase in payables and provisions	**(2,191)**	1,119
Net cash from operating activities	**1,142**	8,119

31. RELATED PARTIES

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

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

Executives
R J Smith (Chief Executive Officer, Petsec Energy Inc.)
R A Keogh (President, Petsec Energy Inc.)
R A Krenzke (Executive Vice President Exploration, Petsec Energy Inc.)
P Gahdmar (Company Secretary and Group Financial Controller, Petsec Energy Ltd)

Key management personnel compensation

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

	2014 US$'000	2013 US$'000
Wages and salaries	**1,111,374**	973,504
Service agreements	**646,632**	694,008
Superannuation & 401(k) plans	**52,917**	47,219
Bonuses	**235,596**	149,639
Termination benefits	**–**	56,250
Share-based payment compensation	**6,400**	95,169
Other benefits	**143,987**	106,273
	2,196,906	2,122,062

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

31. RELATED PARTIES CONTINUED

Individual directors and executives compensation disclosures

Information regarding individual directors' and executives' compensation and some equity instruments disclosures as permitted by Corporations Regulations 2M.3.03 and 2M.6.04 are provided in the Remuneration Report section of the Directors' Report on pages 21 to 27.

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

Non-executive directors appointed prior to 2003 are entitled to receive a retirement benefit that is equivalent to the remuneration received in the three years prior to retirement. Incoming non-executive directors appointed thereafter are not entitled to receive retirement benefits in accordance with the recommendations made by the ASX Corporate Governance Council. Directors' retirement obligations are presently US$160,000 in total (2013: US$174,000).

Transactions with key management personnel

Key management personnel of the Company and their immediate relatives control approximately 20.2 percent of the voting shares of the Company.

No shares were issued by the Company under its shareholder approved Employee Share Plan ("ESP") to key management personnel as long term incentive compensation during the year (2013: nil).

The aggregate amounts recognised during the year relating to key management personnel and their personally related entities, were a total expense of US$647,000 (2013: US$694,000). Refer to Remuneration Report for further details.

Assets and liabilities arising from the above related party transactions

	2014 US$'000	2013 US$'000
Non-current assets		
Related party receivables	**1,093**	1,176
Current liabilities		
Related party payables	**45**	22

Other related party disclosures

Information relating to subsidiaries is set out in note 26.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

32. PARENT ENTITY DISCLOSURES

As at, and throughout, the financial year ending 31 December 2014 the parent entity of the consolidated group was Petsec Energy Ltd.

	2014 US$'000	2013 US$'000
Result of parent entity		
Profit/(loss) for the period	(10,733)	(4,182)
Other comprehensive income	(3,306)	(8,753)
Total comprehensive income/(loss) for the period	(14,039)	(12,935)
Financial position of parent entity at year end		
Current assets	12,261	13,338
Total assets	44,172	58,731
Current liabilities	228	234
Total liabilities	7,634	8,194
Total equity of the parent entity comprising of:		
Share capital	186,001	185,955
Share-based payment compensation reserve	17	57
Foreign currency translation reserve	26,597	29,870
Accumulated losses	(176,077)	(165,344)
Total equity	36,538	50,538

Parent entity guarantees in respect of the debts of its subsidiaries

The parent entity has entered into a Deed of Cross Guarantee with the effect that the Company guarantees debts in respect of its subsidiaries. Further details of the Deed of Cross Guarantee and the subsidiaries subject to the deed are disclosed in note 25.

Parent entity contingencies and capital commitments

The parent entity had no contingent liabilities and capital commitments outstanding at 31 December 2014.

33. EVENTS SUBSEQUENT TO BALANCE DATE

On 7 January 2015, Petsec Energy participated in the drilling of the Ruth R. Bravanec, et al #1 well on the West Crab Lake Prospect in Cameron Parish, onshore Louisiana, with the well reaching its planned true vertical depth of 12,500 feet (12,911 feet measured depth) in late January 2015.

The directional well was drilled to test multiple Lower Miocene age Marg (A) and Discorbis (B) sand reservoirs in a fault closure syncline separated from production in the Marg (A) and Discorbis (B) interval at the Crab Lake Field. The well intersected the target reservoirs as anticipated, but only a few thin zones were hydrocarbon bearing. These zones were too small to warrant completion and development, consequently the well was plugged and abandoned at an estimated cost to the Company of approximately US$0.7 million.

DIRECTORS' DECLARATION

1 In the opinion of the directors of Petsec Energy Ltd ("the Company"):

(a) the financial statements and notes and the Remuneration report in the Directors' Report, set out on pages 21 to 58, are in accordance with the *Corporations Act 2001* including:

(i) giving a true and fair view of the financial position of the Company and the consolidated entity as at 31 December 2014 and of their performance, as represented by the results of their operations and their cash flows, for the year ended on that date; and

(ii) complying with Australian Accounting Standards and the Corporations Regulation 2001; and

(b) the financial report also complies with International Financial Reporting Standards as disclosed in note 2; and

(c) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

2 There are reasonable grounds to believe that the Company and the controlled entities identified in Note 26 will be able to meet any obligations or liabilities to which they are or may become subject to by virtue of the Deed of Cross Guarantee between the Company and those controlled entities pursuant to ASIC Class Order 98/1418.

3 The directors have been given the declarations required by Section 295A of the *Corporations Act 2001* from the chief executive officer and chief financial officer for the financial year ended 31 December 2014.

Signed in accordance with a resolution of the directors:

Terrence N. Fern
Director

Sydney, 24 February 2015

INDEPENDENT AUDITOR'S REPORT

Independent auditor's report to the members of Petsec Energy Ltd

Report on the financial report

We have audited the accompanying financial report of Petsec Energy Ltd (the company), which comprises the consolidated statement of financial position as at 31 December 2014, and consolidated statement of profit and loss and other comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year ended on that date, notes 1 to 33 comprising a summary of significant accounting policies and other explanatory information and the directors' declaration of the Group comprising the company and the entities it controlled at the year's end or from time to time during the financial year.

Directors' responsibility for the financial report

The directors of the company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the directors determine is necessary to enable the preparation of the financial report that is free from material misstatement whether due to fraud or error. In note 2(a), the directors also state, in accordance with Australian Accounting Standard AASB 101 *Presentation of Financial Statements*, that the financial statements of the Group comply with International Financial Reporting Standards.

Auditor's responsibility

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

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

We performed the procedures to assess whether in all material respects the financial report presents fairly, in accordance with the *Corporations Act 2001* and Australian Accounting Standards, a true and fair view which is consistent with our understanding of the Group's financial position and of its performance.

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

INDEPENDENT AUDITOR'S REPORT CONTINUED

Independence

In conducting our audit, we have complied with the independence requirements of the *Corporations Act 2001*.

Auditor's opinion

In our opinion:

(a) the financial report of the Group is in accordance with the *Corporations Act 2001*, including:

(i) giving a true and fair view of the Group's financial position as at 31 December 2014 and of its performance for the year ended on that date; and

(ii) complying with Australian Accounting Standards and the Corporations Regulations 2001; and

(b) the financial report also complies with International Financial Reporting Standards as disclosed in note 2(a).

Report on the remuneration report

We have audited the Remuneration Report included in pages 21 to 27 of the directors' report for the year ended 31 December 2014. The directors of the company are responsible for the preparation and presentation of the remuneration report in accordance with Section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the remuneration report, based on our audit conducted in accordance with auditing standards.

Auditor's opinion

In our opinion, the remuneration report of Petsec Energy Ltd for the year ended 31 December 2014, complies with Section 300A of the *Corporations Act 2001*.

KPMG

KPMG

Anthony Jones
Partner

Sydney

24 February 2015

EXPLORATION AND PRODUCTION INTERESTS

AS AT 31 DECEMBER 2014

PRODUCTION INTERESTS

Geographical Location	Field/Prospect	Working Interest	Revenue Interest
USA Onshore Louisiana	Jeanerette	12.5%	9.22%
USA Gulf of Mexico	Main Pass 18	100.0%	83.33%
	Main Pass 19	55.0%	45.83%

EXPLORATION INTERESTS

Geographical Location	Field/Prospect	Working Interest	Revenue Interest
USA Onshore Louisiana	Southwest Holmwood	30.0%	23.10%
	Northeast Starks	45.0%	33.75%
	West Crab Lake	20.0%	14.40%
USA Gulf of Mexico	Main Pass 270 [1]	12.5%	10.42%
	Breton Sound 39	56.3%	45.70%
	Breton Sound 42	37.5%	30.47%
	Main Pass 132	75.0%	60.94%
	Main Pass 273	12.5%	10.16%
	Main Pass 274	12.5%	9.97%
	Ship Shoal 74	75.0%	60.94%

Geographical Location	Field/Prospect	Paying Interest	Participating Interest
Republic of Yemen Shabwa Basin	Block 7, Al Barqa Permit [2]	35.00%	29.75%

1. Main Pass 270 area encompasses the N/2; NW/4 of the SW/4; W/2 of the NE/4 of the SW/4; SE/4 of the NE/4 of the SW/4; NE/4 of the SE/4; N2 of the NW/4 of the SE/4 in Block 270.
2. In March and May 2014, Petsec Energy entered into separate agreements with AWE and Mitsui E&P Middle East to acquire their respective interests in Block 7, Al Barqa Permit, in the Republic of Yemen.
   Both acquisitions are subject to customary approvals from the joint venture partners, the Yemen government and the state owned Yemen Oil and Gas Company

SHAREHOLDER INFORMATION

AS AT 20 MARCH 2015

NUMBER OF SHAREHOLDERS

Issued capital was 231,161,630 ordinary shares held by 2,049 shareholders.

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

DISTRIBUTION OF SHAREHOLDERS

Size of Holding	No of Holders
1-1,000	182
1,001-5,000	313
5,001-10,000	529
10,001-100,000	822
100,001 and over	203
Total number of shareholders	2,049
Number holding less than a marketable parcel	**457**

LARGEST TWENTY SHAREHOLDERS

The largest twenty shareholders held 133,205,757 ordinary shares being 57.625% of the issued ordinary capital.

Name of Holder	No of Shares	%
CANNING OIL PTY LTD	25,709,116	11.122
MARTIN PLACE SECURITIES NOMINEES PTY LTD	24,426,981	10.567
HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED	13,065,136	5.652
LIPPO SECURITIES NOMINEES (BVI) LTD <CLIENT A/C>	11,332,500	4.902
MR DAVID A MORTIMER & MRS BARBARA L MORTIMER <WALLAROY PROVIDENT FUND A/C>	8,636,448	3.736
NATIONAL NOMINEES LIMITED	5,547,720	2.400
MARTIN PLACE SECURITIES NOMINEES PTY LTD <GULF STREAM A/C>	5,241,475	2.267
CITICORP NOMINEES PTY LIMITED	4,353,003	1.883
KIRMAN PTY LTD <BEEGEES SUPER FUND A/C>	4,129,700	1.786
HUMBOLDT CAPITAL CORPORATION	3,674,532	1.590
MR ROSS ADRIAN KEOGH	3,612,500	1.563
MR PETER RAYMOND GACKA & MRS JENNY ELAINE GACKA <PETER & JENNY GACKA S/F A/C>	3,526,000	1.525
DEN DUYTS CORPORATION PTY LTD	3,057,635	1.323
PIAT CORP PTY LTD	3,000,000	1.298
CALVESTON WORLDWIDE LTD	2,460,000	1.064
SINO CHAMPION DEVELOPMENT LIMITED	2,459,579	1.064
PETROLEUM SECURITIES SHARE PLAN PTY LIMITED	2,400,000	1.038
ASIAN CORPORATE ADVISERS (BVI) LIMITED	2,250,000	0.973
MR RON KRENZKE	2,250,000	0.973
MS DAN LUO	2,073,432	0.897
Substantial shareholders disclosed in substantial shareholder notices given to the Company are as follows:		
CANNING OIL PTY LTD including its associates	30,826,876	13.336

5 YEAR COMPARATIVE DATA SUMMARY

		2010	2011	2012	2013	2014	% change
Financial Performance							
Net Production (Bcfe)[1]		3.9	2.3	2.4	3.6	**1.6**	(56%)
Average Gas Price Received	(US$/Mcfe)	$6.98	$5.69	$3.50	$4.50	**$5.08**	13%
US$ millions							
Net Revenue	(US$m)	$27.1	$13.0	$8.6	$16.4	**$8.2**	(50%)
Net Profit/(Loss) after Tax	(US$m)	($35.2)	$14.0	($5.9)	($15.2)	**($1.1)**	n/a
Realised hedge gains[2]	(US$m)	$0.0	$1.5	$0.0	$0.0	**$0.0**	n/a
Depreciation, depletion & amortisation	(US$m)	$12.5	$5.2	$3.9	$7.0	**$1.8**	(74%)
Exploration Writeoffs, Impairments, abandonment and work-over expenses	(US$m)	$20.0	$20.6	$3.2	$14.4	**$3.0**	(79%)
Derivative (gains)/losses	(US$m)	($1.2)	$0.9	($1.1)	$1.3	**$0.1**	(92%)
Gain on discharge of debt	(US$m)	$0.0	($11.3)	$0.0	$0.0	**$0.0**	n/a
Net financial expense	(US$m)	$3.0	$0.5	$0.4	$0.2	**$0.2**	0%
Income tax (benefit)/expense	(US$m)	$13.6	$0.0	$0.0	$0.0	**$0.0**	n/a
(Profit)/Loss from discontinued operation[3]	(US$m)	$0.4	($29.8)	$0.0	$0.0	**$0.0**	n/a
Tax (benefit)	(US$m)	$0.0	$0.0	$0.0	$0.0	**($0.6)**	n/a
EBITDAX[4]	(US$m)	$13.1	$1.6	$0.5	$7.7	**$3.4**	(56%)
EBITDAX Margin /Mcfe	(US$/Mcfe)	$3.36	$0.72	$0.22	$2.09	**$2.10**	0%
Balance Sheet							
Total Assets	(US$m)	$90.1	$66.4	$64.3	$44.6	**$40.1**	(10%)
Cash[5]	(US$m)	$23.1	$41.6	$28.4	$25.4	**$32.6**	28%
Debt[6]	(US$m)	$28.9	$0.0	$0.0	$0.0	**$0.0**	n/a
Shareholders Equity	(US$m)	$42.8	$57.3	$51.9	$35.4	**$34.2**	(3%)
Cashflow and Capital Expenditures							
Net Cashflow from:							
Operations	(US$m)	$1.8	($6.6)	($1.4)	$8.1	**$1.1**	(86%)
Investing	(US$m)	($11.9)	$37.0	($10.6)	($10.1)	**$6.1**	n/a
Financing	(US$m)	($0.2)	($12.8)	$0.0	($0.6)	**$0.0**	n/a
		($10.3)	$17.6	($12.0)	($2.6)	**$7.2**	
Capital Expenditures[7]							
Exploration	(US$m)	$7.7	$0.6	$4.9	$2.8	**$3.2**	14%
Development	(US$m)	$1.2	$2.8	$8.4	$2.9	**$1.3**	(55%)
Acquisition	(US$m)	$1.7	$0.5	$1.5	$0.0	**$1.2**	n/a
		$10.6	$3.9	$14.8	$5.7	**$5.7**	
A$ million							
EBITDAX[4]	(A$m)	$14.3	$1.5	$0.5	$8.0	**$3.8**	(53%)
Net Profit/(Loss) after Tax	(A$m)	($38.3)	$13.5	($5.7)	($15.8)	**($1.2)**	(92%)
(US$/A$ exchange rate)		$0.92	$1.04	$1.04	$0.96	**$0.90**	(7%)

5 YEAR COMPARATIVE DATA SUMMARY CONTINUED

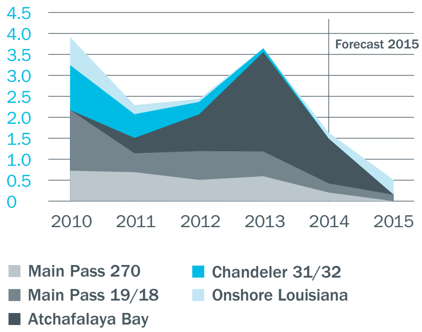
		2010	2011	2012	2013	2014	% change
Operating Margins & Costs							
Average Gas Price Received	(US$/Mcfe)	$6.98	$5.69	$3.50	$4.50	**$5.08**	13%
+ Other Income	(US$/Mcfe)	$0.27	$0.07	$0.63	($0.01)	**$1.25**	n/a
- Operating Costs (GG&A + LOE)	(US$/Mcfe)	$3.99	$5.04	$3.92	$2.40	**$4.23**	76%
= EBITDAX[4]	(US$/Mcfe)	$3.26	$0.72	$0.22	$2.09	**$2.10**	0%
Depreciation, Depletion & Amortisation	(US$/Mcfe)	$3.22	$2.29	$1.59	$1.93	**$1.13**	(42%)
Reserves							
Proved and Probable Reserves (2P)[8]	(Bcfe)	34.3	15.4	11.1	7.2	**1.9**	(74%)
Reserves Replacement Ratio	(%)	(55%)	n/a	n/a	n/a	**n/a**	n/a

1 Bcfe = billion cubic feet of gas equivalent. Mcfe = thousand cubic feet of gas equivalent. Conversion ratio: 1 barrel of oil = 6 Mcf of gas
2 Realised hedge gains in FY2011 relate to derivative natural gas collar contracts which settled during the period. The Company had included the impact of the realised hedge gains, in the reported Net Revenue and EBITDAX amounts in the above table and elsewhere in the comparative Full Year Financial Statements to better reflect the commercial impact and rationale for holding these derivative instruments.
3 Profit from discontinued operation in FY2011 reflects the accounting gain recognised on the disposal of the wholly owned subsidiary which held the China oil interests.
4 EBITDAX = earnings before interest (financial income and expense), income tax, depreciation, depletion and amortisation, and exploration (including dry hole, impairment and abandonment expense, seismic and work-over expense) and realised hedge gains. EBITDAX is a non-IFRS number and is unaudited.
5 FY2014 includes US$5.3m of cash deposits held in an escrow account to secure operator bonds that are on issue to the Bureau of Ocean Energy Management (“BOEM”).
6 FY2010 debt is shown net of original issue discount and transaction costs.
7 Excludes minor (non oil & gas) property, plant & equipment expenditure and investments.
8 FY2010 2P reserve estimates are based on Petsec Energy assessment and include previously booked China oil reserves (sold in June 2011). FY2011 through FY2014 2P reserve estimates are based on independent reserve assessments.

5 YEAR COMPARATIVE DATA SUMMARY CONTINUED

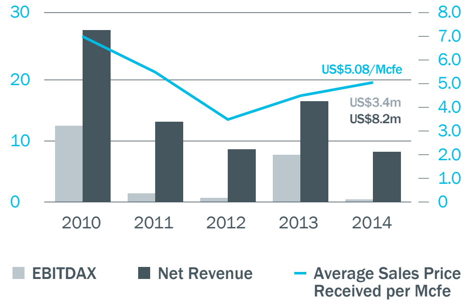
Production history by field

Bcfe



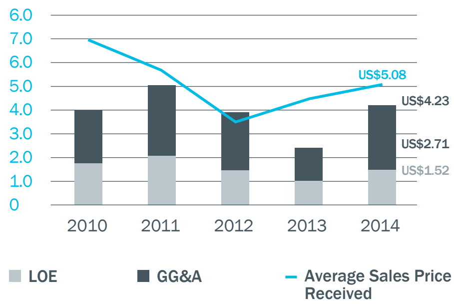
EBITDAX, Net Revenue & Average Sales Priced Received per Mcfe

US$ Million / US$



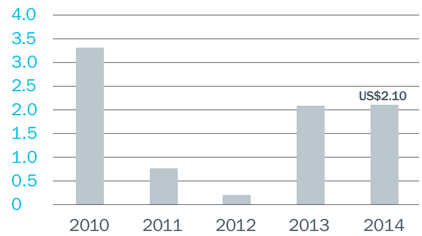
Total operating expense (LOE & GG&A) per Mcfe and Average Sales Price Received per Mcfe

US$/Mcfe



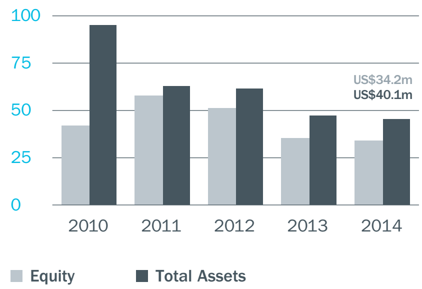
Cash operating margins

US$/Mcfe



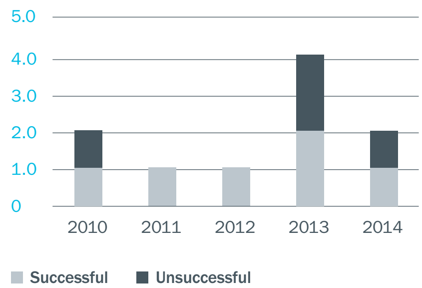
Balance sheet equity and total assets

US$ Million



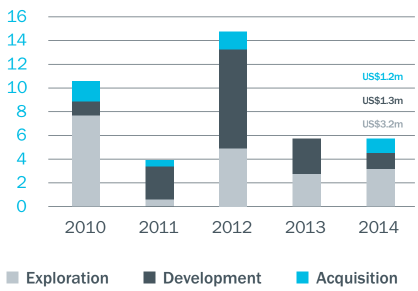
Wells drilled/successful [60% success rate – 5 years to 2014]

Number of wells



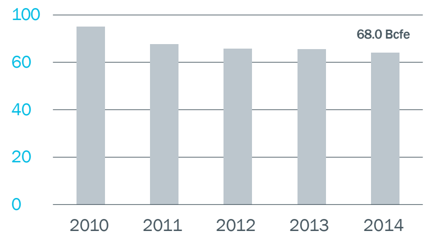
Exploration, development and acquisition expenditure

US$ Million



Cumulative 2P net reserve additions

Bcfe



GLOSSARY

1P	Proved reserves
2P	Proved and probable reserves
AMI	Area of mutual interest
Bcf	Billion cubic feet of gas
Bcfe	Billion cubic feet of gas equivalent
capex	Capital expenditure
cps	Cents per share
DD&A	Depreciation, depletion and amortisation
EBITDAX	Earnings before Interest, taxation, depreciation, amortisation and exploration expense EBITDAX is a non-IFRS number
Field	An area consisting of a single reservoir or multiple reservoirs all grouped on or related to the same individual geological structural feature and/or stratigraphic condition
JV	Joint venture
Mcf	Thousand cubic feet of gas
Mcfe	Thousand cubic feet of gas equivalent
MMcf	Million cubic feet of gas
MMcfe	Million cubic feet of gas equivalent
NRI	Net revenue interest
Oil	Crude oil and condensate
Proved reserves	The estimated quantities of crude oil, natural gas and natural gas liquids that geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic and operating conditions.
Working Interest or W.I.	The operating interest which gives the owner the right to drill, produce and conduct operating activities on the property and a share of production.

CORPORATE DIRECTORY

BOARD OF DIRECTORS
Terrence N Fern – Chairman
David A Mortimer – Non-executive Director
Alan P Baden – Non-executive Director
Mark S Lober – Non-executive Director

COMPANY SECRETARY
Paul Gahdmar

USA MANAGEMENT
Richard J Smith – Chief Executive Officer of Petsec Energy Inc. (PEI)
Ross A Keogh – President of PEI and Group Chief Financial Officer
Ron A Krenzke – Executive Vice President of Exploration of PEI

AUSTRALIAN MANAGEMENT
Terrence N Fern – Chairman & Managing Director
Paul Gahdmar – Company Secretary & Group Financial Controller

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STOCK EXCHANGE
Listed on the Australian Stock Exchange,
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Traded in USA on ADRs, Symbol: PSJEY

FOR FURTHER INFORMATION
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