



# Discovering Hidden Value

Cairn Energy PLC Annual Report and Accounts 2013



## Highlights

“Cairn has an active drilling programme in 2014 that is complemented and balanced by its sustainable development and production portfolio.”

The strategy continues to focus on an attractive mix of frontier and mature basin exploration. By building a growing prospect and lead inventory, from which to select and high grade prospects for drilling, we aim to offer shareholders material potential growth opportunities over the long term.

Cairn is committed to resolving the Indian tax situation and in the meantime can, if required, adapt forward capital and equity exposures.”



**Simon Thomson**  
Chief Executive

### Financial

- Group net cash at 31 December 2013 of US\$1.25 billion (bn)
- ~10% residual shareholding in Cairn India Limited (CIL) valued at ~US\$1.0bn at 31 December 2013 which, while interactions are ongoing with the Indian Income Tax Department, Cairn is not able to sell
- The Group was compliant with tax legislation in place at the time in each relevant jurisdiction, including India. The Group will take whatever steps are necessary to protect its interests
- Following the restriction imposed on our ability to access the value of our shareholding in CIL, Cairn is committed to all of its planned operations in 2014 while capital allocation for future programmes will depend primarily on:
  - the progress of Catcher through to project sanction;
  - the conclusion of debt facilities for both Catcher and Kraken; and
  - the results of our 2014 drilling programme
- The existing portfolio provides many opportunities and we are looking closely at the allocation of capital for the programme beyond 2014, which will be guided by three core principles:
  - creating value through exploration
  - maintaining a balanced portfolio, with a strong operating cash flow in the future; and
  - capital discipline
- The Board has decided to suspend the previously announced share buy-back programme as of 21 March 2014 until the position regarding the CIL shareholding is resolved. To date 25,180,201 shares for an aggregate consideration of ~US\$94.7 million (m) have been repurchased as part of the buy-back programme. The total number of voting rights in Cairn, as at 17 March 2014 is 578,189,219

### Frontier basin exploration

#### Atlantic Margin Operated Programme (three wells, Q2-Q4 2014)

- The JM-1 well (Cairn 37.5% Working Interest (WI) and Operator) drilled to evaluate Upper Jurassic and Middle Jurassic objectives reached a total depth of 3,711m TVDSS and has been plugged and abandoned without testing
- As previously announced in December 2013, the FD-1 exploration well was plugged and abandoned. The primary target of the well was a Late Jurassic/Early Cretaceous deep-water turbidite slope fan and channel complex. While gas shows confirmed an active thermogenic petroleum system, the well did not encounter clastic reservoirs
- The first of two planned exploration wells offshore Senegal (Cairn 40% WI) will commence in April after operations in Morocco have been completed
- Operations offshore West of Republic of Ireland on the Spanish Point appraisal well are targeted to commence Q2/Q3 2014 (Cairn 38% WI)

#### Atlantic Margin Non-Operated Programme (one well, Q4 2014)

- One exploration well is planned to commence on the Cap Boujdour Contract Area in 2014 with Kosmos Energy (operator) and the Moroccan National Oil Company (ONHYM) (Cairn 20% WI) subject to government approval

### Mature basin exploration

#### (three wells Q2 2014 – Q1 2015) and development

- Two non-operated North Sea exploration wells (Aragon and West of Kraken) are scheduled in 2014 with one further well (Tulla) scheduled for 2015
- The second Skarfjell appraisal well successfully delineated the field and the partners are now examining possible development concepts for Skarfjell (Cairn 20% WI)
- The Kraken Field Development Plan (FDP) received approval from the Department of Energy and Climate Change (DECC) with first oil expected H2 2016/H1 2017. Consequently, Cairn has booked 30 million barrels of oil equivalent (mboe) 2P reserves. Peak forecast production is 50,000 barrels of oil per day (bopd) (12,500 bopd net to Cairn) (Cairn 25% WI)
- The Catcher FDP approval is expected by the operator in Q2 2014 (Cairn 30% WI)

### Chairman

- As previously announced, Sir Bill Gammell will retire as non-executive Chairman of the Company with effect from the conclusion of the Company's AGM on 15 May 2014; Ian Tyler, currently a non-executive director of the Company, will be his successor

# Committed to delivering material growth and shareholder value

Cairn Energy PLC is an established and pioneering independent oil and gas exploration company with a track record of delivering substantial returns and capital growth to shareholders.

Cairn's growth model is to create, add and realise value within a self funding business which has either balance sheet cash or operating cash flow from which to fund exploration. The exploration programme is focused on seeking to create value within frontier opportunities with suitable equity levels, which are

reflective of the company size, in the Atlantic Margin and Mediterranean basins. This frontier strategy is underpinned by the non-operated mature basin exploration and development projects in the North Sea which will provide growth and income in the medium term to fund future exploration.

In 2013, Cairn delivered on its priorities, creating a business offering multiple opportunities for growth within a coherent strategy and a sustainable business model.



## US\$1.25<sup>bn</sup>

Group net cash at 31 December 2013.

## 62 licences

in 11 countries in frontier and mature basins at 31 December 2013.



## 62 prospects

and 155 leads within the current portfolio.

## 7 wells

targeted in 2014.

## Strategic Review 02-61

What Cairn Did In 2013	02
Chairman & CEO Statement	04
What Cairn's Business Model Is	08
How Cairn Delivers Its Strategy	10
Global Oil and Gas Trends In 2013	12
Where Cairn Is Focused	14
Who Our Regional Team Is	16
How We Operate Responsibly	18
How We Work Responsibly	20
How We Nurture Our People	22
How We Monitor Performance	24
Operational Review	30
Financial Review	38
How We Manage Risk	42
Working Responsibly	50

## Leadership and Governance 62-98

Board of Directors	62
Directors' Report	64
Corporate Governance Statement	67
Audit Committee Report	78
Directors' Remuneration Report	81

## Financial Statements 99-146

Independent Auditors' Report	99
Group Income Statement	104
Group Statement of Comprehensive Income	104
Group Balance Sheet	105
Group Statement of Cash Flow	106
Group Statement of Changes in Equity	107
Section 1 – Basis of Preparation	108
Section 2 – Oil and Gas Assets and Related Goodwill	110
Section 3 – Financial Assets, Working Capital and Provisions	116
Section 4 – Results for the Year	121
Section 5 – Capital Structure and Other Disclosures	127
Section 6 – Post Balance Sheet Events	132
Company Balance Sheet	133
Company Statement of Cash Flow	134
Company Statement of Changes in Equity	135
Section 7 – Notes to the Company Financial Statements	136
Appendices to the Group and Company Financial Statements	140

## Additional Information 147-150

Cairn Group Licence List	147
Glossary	150
Company Information	Inside Back Cover
Corporate Offices	Back Cover

# A year of progress

### Quarter One

January to March 2013

## Q1: Building a Platform



Seismic survey vessel

Cairn farmed-in to the Aragon prospect (30% WI) in the UK in January. Furthermore, Cairn was awarded interests in two further licences in Norway in the Awards in Predefined Areas (APA) licence round. In March, drilling operations completed on the Timon exploration well located in the UK (Cairn 25% WI, as non-operator). The well reached a total depth of 10,787 feet but did not encounter hydrocarbons and was plugged and abandoned.

In March, Cairn added to its Atlantic Margin portfolio focus by farming-in as Operator to three blocks offshore Senegal with a WI of 65%. The three contiguous blocks – Rufisque Offshore, Sangomar Offshore and Sangomar Deep – cover an area of approximately 7,490km<sup>2</sup> in the Senegalese portion of the productive Mauritania-Senegal-Guinea-Bissau Basin. Subject to the necessary approvals, Cairn and its JV partners will begin their two well exploration programme in H1 2014.

During this period, Cairn also completed 680km<sup>2</sup> of 3D seismic acquisition over the Juby Maritime block, offshore Morocco.

30 Discover more: *Operational Review*  
P30-37

### Quarter Two

April to June 2013

## Q2: Developing the Business



Cajun Express drilling unit

In April, Cairn secured a year-long contract with Transocean for the Cajun Express drilling unit for use on its multi-well frontier exploration drilling campaign in North West Africa in Q4 2013 and 2014. The Cajun Express is a deepwater, 5th generation, dynamically positioned, semi-submersible drilling rig with shallow mooring capabilities and a 15,000 psi blow out preventer (BOP) stack.

In May, Cairn added further opportunities to its Atlantic Margin programme with new acreage in the Republic of Ireland following the farm-in, as Operator, to two licences in the Porcupine Basin which contain the undeveloped Spanish Point gas condensate and Burren oil discoveries, and six adjacent licensing option blocks. Cairn and its JV partners will commence an appraisal well on the Spanish Point discovery in Q2/Q3 2014. The acreage covers an area of 2,753km<sup>2</sup> with more than 500km<sup>2</sup> covered by 3D seismic data.

During this period the Group had success through its non-operated interests in the UK and Norwegian sectors of the North Sea: the appraisal well on the Skarfjell discovery (Cairn 20% WI), and the Bonneville exploration well and its side track on the Catcher licence (Cairn 30% WI) all discovered oil.

30 Discover more: *Operational Review*  
P30-37

## Quarter Three

July to September 2013

## Q3: Shaping the Portfolio



Blackford Dolphin drilling unit

In July, Cairn entered into a contract to secure the drilling rig 'Blackford Dolphin' for the Spanish Point appraisal well in the Republic of Ireland in 2014. The rig, which underwent a US\$400m deepwater upgrade in 2006, is targeted to begin operations on this well in Q2/Q3 2014.

The shaping of the Atlantic Margin portfolio continued with ConocoPhillips farming in to a 25% WI in the three contiguous blocks located offshore Senegal acquired by Cairn in Q1 2013. Cairn retained operatorship and a 40% WI. In the event of commercial success, ConocoPhillips will have the option to operate any future development.

In August, Cairn farmed-in to a 35% WI in an exploration block offshore Mauritania, operated by Chariot Oil & Gas Investments (Mauritania) Limited, a wholly owned subsidiary of Chariot Oil & Gas Limited.

In the North Sea, Cairn carried out a series of asset swaps and exchanges as well as an agreement to dispose of Cairn's 6% WI in the Mariner field to Dyas UK Limited.

In addition, Cairn became a participating company of the Extractive Industries Transparency Initiative (EITI) (launched in 2002 to strengthen governance by improving transparency and accountability).

30 Discover more: *Operational Review*  
P30-37

## Quarter Four

October to December 2013

## Q4: Commencing Exploration



Cajun Express drilling unit

In October 2013, Cairn began operations on the FD-1 frontier exploration well offshore Morocco – the first well in its frontier exploration drilling programme using the Cajun Express. The primary target of the well was a Late Jurassic/Early Cretaceous deepwater turbidite slope fan and channel complex. Although the well penetrated the oldest stratigraphic section of any deepwater exploration well along the Moroccan margin it did not encounter sandstone reservoirs. Gas shows and gas composition ratios encountered in the well have confirmed an active thermogenic petroleum system. The well has been plugged and abandoned.

Cairn also entered into a farm-in agreement, subject to government approval, with Kosmos Energy for a 20% non-operated WI in an exploration block offshore Morocco which is scheduled for drilling in H2 2014. The farm-in to the Cap Boujdour exploration permit enables Cairn to access frontier acreage with significant potential containing a range of exploration play types. In the event of success, the area has significant follow-up potential.

In line with the Company's disciplined approach to managing its balance sheet, in October, following the announcement of the sale of the Company's 6% WI in the Mariner Asset in the North Sea, Cairn announced it would repurchase up to US\$300m of ordinary shares in the company to be reviewed by the Board on a quarterly basis. As at 31 December 2013, 8,217,615 ordinary shares have been repurchased for \$36,293,629.63.

In November, the FDP for Kraken was approved by DECC meaning 30 mmboe has been converted into 2P reserves.

30 Discover more: *Operational Review*  
P30-37



## Chairman & CEO Statement

Sir Bill Gammell and Simon Thomson

Our strategy is to focus on value creation and value realisation.

Cairn's vision is to create an exploration led and sustainable cash generative oil and gas business offering shareholders exposure to material capital growth potential. In particular, we seek to secure frontier or overlooked exploration opportunities, on appropriate commercial terms, which offer significant hidden value potential.

Cajun Express drilling unit

## Chairman's Introduction

As announced on 3 March, I intend to retire from the Board following the AGM on 15 May and I am delighted that Ian Tyler will take over as non-executive Chairman. When Ian was originally brought onto the Group's Board, as part of Cairn's long term succession planning, Cairn was aware of Ian's abilities as chairman and his extensive listed company experience. As a shareholder, I am confident that Ian will be an excellent leader of the Board and ensure its continued effectiveness.

In addition, Dr James Buckee has decided not to stand for re-election at the AGM. I would like to thank Jim for his valuable contribution to the Board during his tenure as a non-executive director.

## Corporate Overview

Our strategy is to focus on value creation and value realisation.

Cairn's vision is to create an exploration led and sustainable cash generative oil and gas business offering shareholders exposure to material capital growth potential. In particular, we seek to secure frontier or overlooked exploration opportunities, on appropriate commercial terms, which offer significant hidden value potential.

During 2013, Cairn delivered on its strategic goal of positioning the Group for future growth:

- i. we commenced a multi-well frontier exploration programme which offers investors substantial growth potential; and
- ii. we advanced two main pre-development projects, Kraken and Catcher, the former to project sanction, the latter's draft FDP was submitted to DECC early 2014.

The combination of future cash generating assets within a balanced exploration portfolio means we are well placed to fund future exploration activity and to repeat the cycle of creating, adding and realising shareholder value.

Our multiple frontier and mature basin exploration wells over the coming months are targeting close to 2 billion barrels of oil equivalent (bn boe) of mean un-risked gross prospective resource within a total of un-risked "Yet to Find" prospect potential in excess of 10 bn boe. By building a growing prospect and lead inventory, from which to select and high grade prospects for drilling, we aim to offer shareholders material potential growth opportunities over the long term.

Cairn's net cash of US\$1.25bn as at 31 December 2013 provides the necessary funding to meet planned exploration and development commitments. The FDP approval by DECC for the Kraken development in November 2013 means reserves have been booked and discussions are well advanced to secure debt finance for this project. Upon receiving FDP approval for Catcher we will similarly book Catcher reserves and progress debt financing to fund its development.

As the development plans progress, our revised valuation of the Kraken asset exceeds its carrying value in the financial statements of US\$300m, although there has been a fall in value of the Catcher assets to US\$250m (due to revisions to the cost and resource estimates) which results in an impairment. Deferred tax credits on both assets have also led to an impairment of goodwill. The impact of the impairments and tax credits result in a net charge of US\$218m. See the Financial Review for further details.

In January 2014, Cairn received a request from the Indian Income Tax Department to provide information in relation to the year ended 31 March 2007. The correspondence indicates that the request for information is in respect of amendments introduced in the 2012 Indian Finance Act which seek to tax prior year transactions under legislation applied retrospectively. While the interactions with the Indian Income Tax Department continue, Cairn has been restricted from selling its shares in CIL (valued at US\$1.0bn as at 31 December 2013). This matter is addressed further in the Financial Review.



Discover more on the Indian Income Tax situation: [Financial Review P39](#) and [How We Manage Risk P42-49](#)

In particular, we seek to secure frontier or overlooked exploration opportunities, on appropriate commercial terms, which offer significant hidden value potential.



## Chairman & CEO Statement

### Continued

In line with value realisation and the Group's disciplined approach to managing its balance sheet, Cairn announced in October 2013 it would return up to US\$300m to shareholders through a share repurchase programme. This maximum cash return effectively represented the aggregate of the proceeds realised from the sale of the Group's 6% WI in the North Sea Mariner Field and the capital expenditure allocated to that development.

The Board agreed to review the buy-back programme on a quarterly basis and has decided to suspend the share buy-back programme until the position with regard to the shareholding in CIL is resolved. To date 25,180,201 shares for an aggregate consideration of ~US\$94.7m have been repurchased as part of the buy-back programme. The total number of voting rights in Cairn, as at 17 March 2014 is 578,189,219.

### Frontier Basin Exploration: Atlantic Margin

Cairn's frontier Atlantic Margin exploration strategy is focused along the multiple play types related to the breakup of the former supercontinent Pangea. Our current portfolio includes exploration acreage offshore Morocco, Senegal, Ireland, Mauritania and Greenland.

Offshore Morocco, we operate two exploration permits and are also a non-operator partner in one exploration permit.

Our first well in the programme was the offshore Morocco, FD-1 well (Cairn 50% WI, Operator), which was plugged and abandoned in December 2013. The well established a working hydrocarbon system with a thermogenic source rock, however, the anticipated target reservoirs were not encountered.

The JM-1 well (Cairn WI 37.5%, Operator) drilled to evaluate Upper Jurassic and Middle Jurassic objectives reached a total depth of 3,711m TVDSS and has been plugged and abandoned without testing.

In the Upper Jurassic section, the well has confirmed the presence of heavy oil over a gross interval of 110 metres (m) as originally tested in the 1968 MO-2 well, some 2km from the JM-1 well. Reservoir quality and the oil gravity in the Upper Jurassic across the Cap Juby structure require further evaluation by Cairn and its joint venture partners (Office National Des Hydrocarbures et Des Mines "ONHYM" and Genel Energy). Work is ongoing to correlate the core and log data from JM-1 with other wells on Cap Juby to evaluate the extent of moveable hydrocarbons and how any further assessment should be conducted.

The Middle Jurassic objective was encountered with limited primary porosity and evaluation of well logs and side wall cores continues.

The two well exploration programme offshore Senegal (Cairn 40% WI, Operator) is expected to start in April after drilling operations are completed in Morocco.

The first exploration well will be located on the North Fan Prospect in 1,427m water depth. This well will be immediately followed by a second exploration well targeting a Shelf Edge Prospect in 1,100m of water. These will be the first deep water (>1,000m) wells drilled in Senegal and only the second and third deep water wells along this underexplored part of the margin.

An appraisal well on the Spanish Point gas/condensate discovery offshore West of Republic of Ireland (Cairn 38% WI, Operator) and a 3D seismic survey on acreage nearby are both planned to commence Q2/Q3 2014.

One exploration well is planned to commence on the Cap Boujdour Contract Area in 2014 with Kosmos Energy (operator) and the Moroccan National Oil Company (ONHYM) (Cairn 20% WI) subject to government approval.

### Mature Basin Exploration and Development: UK and Norwegian North Sea

Over the last two years, the Group has built an attractive business and acreage position in the North Sea. Importantly, this is an area which provides an active market place for asset trades as evidenced by the various swaps, farm-ins and divestments the Group has completed during the last year, with such activity set to continue.

In the UK, the Kraken and Catcher development projects are a key part of the portfolio, acquired to provide cash flow following first oil production in 2016/17. In Norway, the Group has built a strategic position around its Skarfjell discovery (Cairn WI 20%), including other discoveries and prospects which offer the potential for a hub and satellite development scheme in the future.

The strategic intention is to use free cash from these future developments to fund future exploration programmes.

Over the last two years, the Group has built an attractive business and acreage position in the North Sea. Importantly, this is an area which provides an active market place for asset trades as evidenced by the various swaps, farm-ins and divestments the Group has completed during the last year, with such activity set to continue.



## Questions and Answers

## Q&amp;A with CEO

## People

We would like to recognise and thank all the effort, hard work and commitment the management, employees and contractor teams working for Cairn have put in during the last year.

We have an equal opportunities policy across the Group. To ensure we deliver our goals and provide shareholder value we must employ the right people in the right roles. We seek to ensure a diverse workforce. For example women currently comprise 20% of our board, 28% of our management and 50% of our staff across our whole organisation.

## Outlook

The results of this year's exploration programme and the timing of the resolution of the Indian tax situation will inevitably shape the Group beyond 2014. We believe the executive team, supported by the Board, is well-placed to lead the Group and continue the strategic focus of delivering significant growth potential as the Group continues to evolve in response to changing circumstances.

We look forward to what we hope will be a successful exploration programme in 2014.



**Sir Bill Gammell**

Chairman



**Simon Thomson**

Chief Executive  
17 March 2014

**What do you think Cairn Energy will look like in three years' time?**

We've done a lot of work over the last 18 months to build a balanced portfolio that offers multiple exploration opportunities as well as providing future cash flow through interests in development assets in the North Sea, thereby providing a platform to sustain Cairn as an exploration company. Our portfolio provides us with significant opportunities. In three years' time, we would like to see Cairn in the process of repeating the cycle once more of developing and realising value.

**What do you think makes the business model different?**

We are focused yet adaptable. We are prepared to make robust decisions quickly. We focus on value not scale. We build lasting partnerships where we believe we will all add value. We place an emphasis on understanding the potential risks and on managing them. To maintain a sustainable business as part of our portfolio we have interests in development assets which offer future free cash flow to sustain Cairn in the long term and fund future exploration activity.

**What did the Company achieve last year?**

We set objectives which included focusing on exploration-led growth: we have further built the portfolio during 2013 to include additional frontier exploration opportunities which offer potential growth to shareholders. While we added additional acreage to our portfolio it remained focused on the Atlantic Margin, Mediterranean and North Sea regions.

The multi-well frontier exploration programme commenced with the first in the series of wells offshore Morocco.

The FDP for the Kraken field in which Cairn has an interest received UK DECC approval during 2013; Catcher FDP is targeted by the operator to be submitted in Q2 2014.

We promised we would maintain suitable equity levels to frontier exploration opportunities. By farming down some of our interests offshore Senegal to ConocoPhillips, we ensured we maintained appropriate exposure to this acreage.

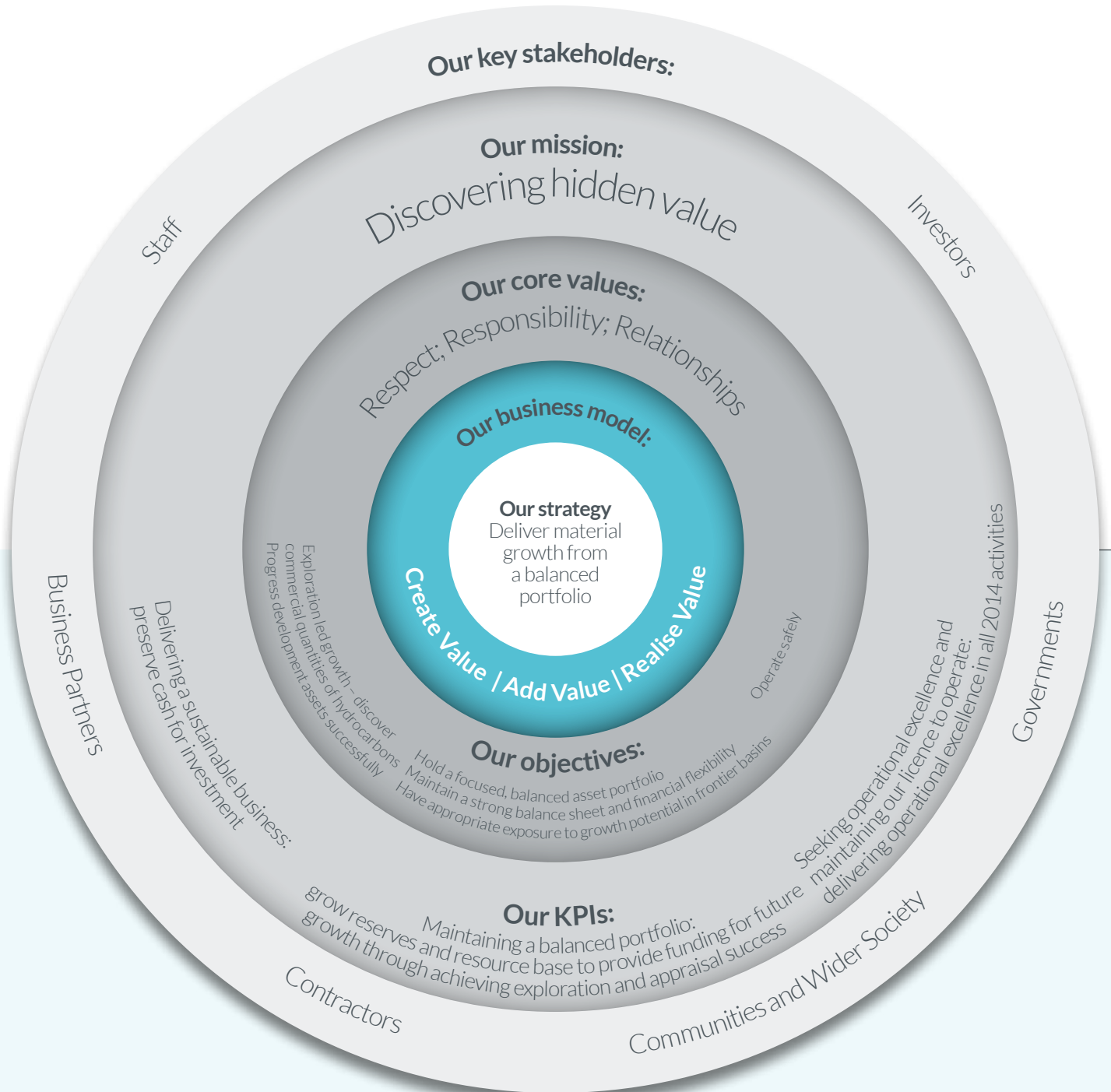
We said we would operate safely; we were therefore disappointed by two Lost Time Incidents (LTIs) during our operational activity offshore Morocco. We will continue to focus our energy and resource on avoiding incidents and delivering safe operations.



## What Cairn's Business Model Is

# Cairn creates, adds and realises value for shareholders

The diagram below represents Cairn's business. The outer circle reflects the environment in which Cairn works. Within the image, the Group's mission, philosophy, business model and strategy are captured as well as the objectives and measurements that the Group sets.



Cairn's business is constantly evolving to adapt to new opportunities and the competitive landscape. The strategy is to focus efforts on frontier exploration opportunities which offer potential for growth within a balanced sustainable portfolio.

Cairn's success stems from being pioneers and partners. The Group focuses on identifying assets that are capable of providing significant and sustainable growth and capturing appropriately sized equity positions on attractive terms. The Group maintains a balanced portfolio with frontier exploration and mature basin exploration, plus development projects which provide free cash flows in the medium term.

Cairn's growth model is to create, add and realise value within a sustainable self funding business.



### Create Value

Cairn seeks to create value in a number of ways: by acquisition of new assets or by securing farm-in transactions at appropriate equity levels to offer growth potential; early stage participation and entry into frontier basins; and through successful exploration and development of hydrocarbon finds. Examples of this were the successful farm-ins to acreage offshore Senegal, Republic of Ireland, Mauritania and Morocco\*.

\* Subject to Government of Morocco approval.

### Add Value

Cairn does this through optimising existing assets, seeing hidden value in assets that others may have overlooked, and through asset swaps and exchanges. Examples of this in 2013 were:

- The farm-in to the acreage offshore Senegal which Cairn undertook at the beginning of the year. Cairn subsequently farmed down part of its interest in this acreage to ConocoPhillips who, in the event of exploration success, have the option to operate the future development;
- Multiple North Sea asset swaps to hone and optimise the mature basin portfolio and increase acreage around existing discoveries.

### Realise Value

Cairn has a proven track record of realising value for shareholders, whether this be from bringing exploration successes to production and subsequent free cash flow or by selling assets. Proceeds can be either reinvested in the business, creating a virtuous cycle, or returned to shareholders. Cairn is careful to maintain a strong balance sheet which can fund the Group's exploration programmes that offer growth opportunities. As a result of the Mariner transaction and the Company's commitment to realising value, Cairn entered into a programme to repurchase up to US\$300m of ordinary shares in the Company to be reviewed quarterly.

# Generating material growth from a balanced portfolio

What our objectives were in 2013 and will be in 2014	
Delivering a sustainable business	Focus on exploration led growth.
	Progress development assets successfully to transform discovered resources to reserves and cash flow generation.
Maintaining a balanced portfolio	Hold a focused, balanced asset portfolio.
	Have appropriate exposure to growth potential in frontier basins.
	Maintain a strong balance sheet and financial flexibility.
Seeking operational excellence	Complete 2013 operations safely and without environmental incident.

## What we achieved in 2013

- Added further exploration acreage.
- Started multi-well frontier exploration campaign in the Atlantic Margin.
- Contracted rigs to deliver Atlantic Margin exploration campaign.

- DECC approval of Kraken FDP.
- Catcher FDP submission by the operator targeted Q2 2014.

- Farmed-in to acreage offshore Senegal, Ireland, Mauritania and Morocco.
- Disposed of non-core Mariner asset.

- Farmed down 25% WI in Senegal licences to ConocoPhillips, leaving Cairn's remaining WI of 40%.

- Return of up to US\$300m to shareholders through share repurchase programme.
- Group net cash at 31 December US\$1.25bn (see page 39 for details on the Company's CIL investment).

- Despite focusing on safety, we were concerned that during the beginning of operations offshore Morocco, two LTIs occurred. A thorough review has been undertaken to capture lessons learned and avoid similar incidents happening again.

## 2 billion boe

close to 2.0bn boe mean unrisked gross prospective resource is being targeted in the current frontier exploration programme.

## 12,500 bopd

Kraken field forecasted production 50,000 bopd, 12,500 bopd net to Cairn.

## US\$250m-300m

~US\$250m-300m allocated annually to exploration and appraisal activity.

## 5 countries

Acquired additional interests in Senegal, Republic of Ireland, Mauritania, Norway and Morocco (subject to government approval).

## 2 drilling campaigns

Two drilling campaigns completed with a focus on safety.

# The wider business background and industry context which drive Cairn's strategy and activities

## Challenges and Opportunities

The World Energy Council expects global demand for oil and gas to continue to grow at 1% and 2% per year respectively. Given population growth pressures, even with increasing energy diversity, the dominant role of fossil fuels in global energy supplies, and pressures to replace oil and gas reserves, are expected to continue for at least another forty years.<sup>1</sup>

In recent years, unconventional sources of oil and gas have been successfully exploited, most notably in the USA and Canada.<sup>2</sup> Although production from equivalent sources is being considered in earnest elsewhere, in the short to medium term, oil and gas supply growth outside of North America is likely to continue to be from conventional sources, with deepwater opportunities playing an increasingly important role in the pursuit of material reserves by Independent Oil Companies (IOCs) to underpin their value-growth strategies.<sup>3,4</sup>

## The Global Economy

Signs of a more solid recovery were visible in global economic trends in 2013.<sup>5</sup>

The global economy grew by 3.0% in 2013 and the International Monetary Fund (IMF) forecasts a rise in global growth rates to around 3.7% in 2014, and 3.9% in 2015, with the increase driven by recovery in the advanced economies rather than emerging market countries, where growth has slowed due to structural bottlenecks.<sup>6</sup>

Throughout 2013, central banks in a number of the world's advanced economies continued to utilise quantitative easing (QE) and low interest rates, which supported improved GDP growth in countries including the United Kingdom (+1.9%) and Japan (+1.7%).<sup>7,8</sup> The extended QE policies also supported significant out-performance in equity markets, and several indices, including the German DAX and the US Dow Jones, touched all-time highs.<sup>9</sup>

The International Energy Agency (IEA) estimates that global demand for oil in 2013 grew by 1.2 mmbopd (or 1.4%) to 91.2 mmbopd, with the largest increases in demand sourced from Asia and the Americas.<sup>10</sup> The IEA expect oil demand growth to continue in 2014, increasing by a forecast 1.3 mmbopd as the macroeconomic picture continues to improve.

## Oil and Gas Markets: Changing Dynamics

The impact of significant growth in unconventional production in the USA continued to play a key role in the changing dynamics of global oil and gas markets, as the Organisation of Petroleum Exporting Countries' (OPEC's) share of total oil supplies continued to reduce.<sup>11</sup>

According to the IEA, global oil supplies increased by 0.7% in 2013 averaging 91.6 mmbopd.<sup>12</sup> Lower oil production in several OPEC countries contributed to total OPEC oil supplies falling 2.1% to 36.8 mmbopd. Non-OPEC oil supplies increased by 2.4% to 54.7 mmbopd, representing almost 60% of the total. The IEA predict that non-OPEC supplies will continue to increase in 2014, with the biggest contributions to growth sourced from North America, and largely attributable to an increasing contribution from unconventional sources.

Brent crude spot prices reached a peak of US\$118.6/bbl in February 2013 and averaged US\$108.7/bbl over the year, down 2.7% on 2012's record average price of US\$111.7/bbl. The US Energy Administration forecasts a further weakening of Brent to an average US\$105/bbl in 2014 as non-OPEC supplies continue to increase.<sup>13</sup>

The discount of WTI crude oil to Brent narrowed during 2013, averaging US\$10.7/bbl, compared to US\$18/bbl in 2012, as US transportation costs reduced following the commission of new pipeline infrastructure.

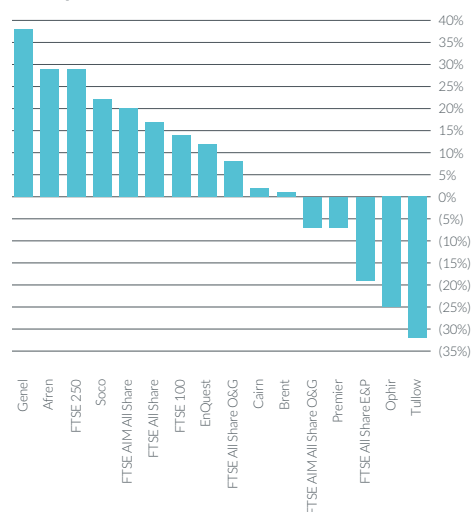
The Energy Administration estimate global natural gas production in 2013 at 322 bcf/d, and forecast growth of 1.7% per year to 2040.<sup>14</sup> The USA remained the world's largest gas producer in 2013, increasing production by 1% and contributing an estimated 20% of the total, again on the back of continuing growth from unconventional sources.<sup>15</sup> North American natural gas prices remained at very low levels and were decoupled from both domestic crude and international gas prices. Henry Hub averaged US\$3.7/mmbtu in 2013, around one-third of natural gas import prices to Europe and one-fifth of those to Japan.<sup>16</sup>

The North Sea continued to be an area of focus for the oil and gas industry in 2013. Capital investment is estimated to have been a record £13.5bn and 13 new fields were brought on stream.<sup>17,18</sup> During 2013, the development plan for the Kraken field (in which Cairn has a 25% non-operated WI) was approved by the UK's DECC. Cairn also participated in exploration and appraisal drilling in the UK and Norwegian North Sea.

## UK Oil and Gas Sector Performance

Global equity markets in 2013 were generally buoyant with stocks achieving significant growth. The UK's Financial Times Stock Exchange (FTSE) 250 Index achieved an annual increase of 28.8%, outperforming the FTSE 100 (+14.4%). The oil and gas sector as a whole underperformed relative to wider equities. In general, larger companies performed better: the FTSE Oil and Gas Producers Index (broadly representative of the majors in the sector) achieved growth of 8%, reversing 2012's trend (a decline of 11.4%), but the FTSE AIM Oil and Gas Index (largely representative of the sector's junior participants) fell by 6.6%.

### UK Equities: 2013 Performance



Source: Jefferies

The FTSE All Share Exploration and Production (E&P) Index (representative of mid-sized Independent E&P companies) fell by 18.7%, but this figure masks a wide divergence in performance with 6 of its 14 component companies achieving positive growth in 2013. Cairn is included in this index and achieved capital growth of 1.9% in 2013.

## Mergers and Acquisitions (M&A) and Industry Consolidation – Low Levels

In 2013, a slight softening of oil prices, financing constraints, and a greater emphasis on capital discipline by investors contributed to a more cautious stance adopted by potential industry purchasers.

In 2013, the total value of upstream oil and gas transactions of US\$237 billion was down 17% from 2012's US\$286 billion.<sup>19</sup> The number of high value deals (defined as >US\$100m) in 2013 was also below average, down 22% from 2012 levels. Asset transactions rather than corporate acquisitions continued to dominate the deal mix, accounting for 86% of 2013's upstream deals.

North America and Europe continued to dominate in terms of the numbers of deals reported, but total transaction value fell in the USA, Canada and Australia, while increasing in Africa, the CIS/Russia and the Middle East.<sup>20</sup>

Major oil companies were net sellers as they continued to highgrade their portfolios.<sup>21</sup> National Oil Companies from Asia, private equity companies and Master Limited Partnerships in the USA continued to dominate the spectrum of buyers.<sup>22</sup>

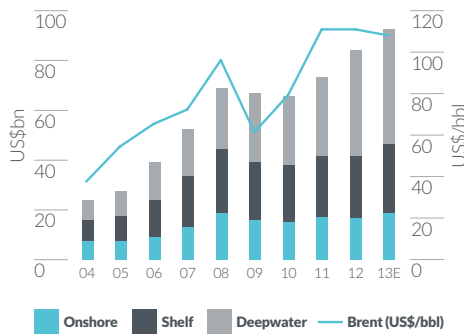
UK public market oil and gas M&A was generally limited to small-scale sector consolidation through mergers, with some junior companies also seeking to deliver shareholder value through a formal sales process.<sup>23</sup>

## Exploration – Continuing Deepwater Focus

Wood Mackenzie estimate that in 2013, total upstream spend exceeded US\$1 trillion for the first time, but that the rate of growth slowed to around 5%.<sup>24</sup> IHS reported that inflationary pressures on upstream costs also eased in 2013, against a backdrop of relatively steady oil prices.<sup>25</sup> Exploration spend increased by 10% in 2013 and exploration investment focus continued to be on the material growth offered by deepwater and unconventional opportunities.

For the second year in a row, deepwater drilling accounted for half of total conventional exploration spend, increasing by 9% from 2012, to US\$47 billion, and up 91% from 2008.<sup>26</sup>

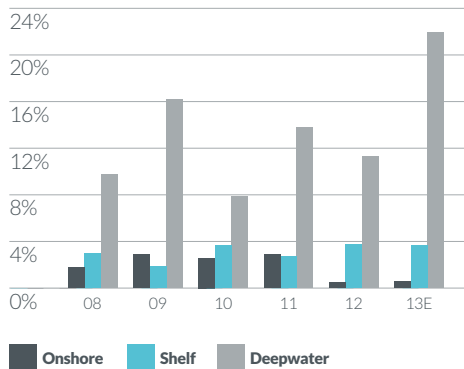
### Conventional Exploration Investment



Source: Wood Mackenzie

Deepwater prospects continued to offer explorers a significantly higher chance of material success, accounting for an estimated 60% of conventional fields >100 mmboe discovered over the last three years and more than 75% of those discovered in 2013.

### Material (>100 mmboe) Drilling Success Rates



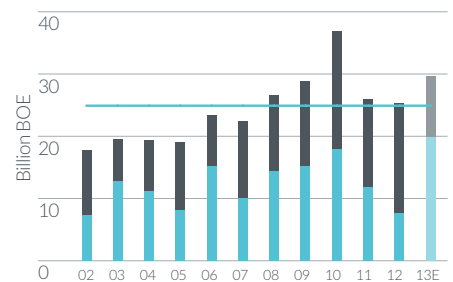
Source: Wood Mackenzie, based on discoveries reported at 31 January 2014

During the ten-year period 2003 to 2012, discovered volumes of recoverable oil and gas from conventional exploration drilling averaged around 25 bn boe per year.<sup>27</sup> This average was lifted by a string of exceptional high impact and largely deepwater exploration

successes (mainly oil discoveries in Brazil and gas discoveries in East Africa) in the period 2008 to 2012.

Based on reported volumes during 2013 relative to equivalent figures for 2012, Wood Mackenzie estimate that, following full disclosure and anticipated appraisal updates, discovered volumes of recoverable oil and gas for 2013 (as an indicator of global exploration performance) are likely to be in line with earlier years i.e. in the range 20-30 bn boe.

### Conventional New Field Discovery Volumes

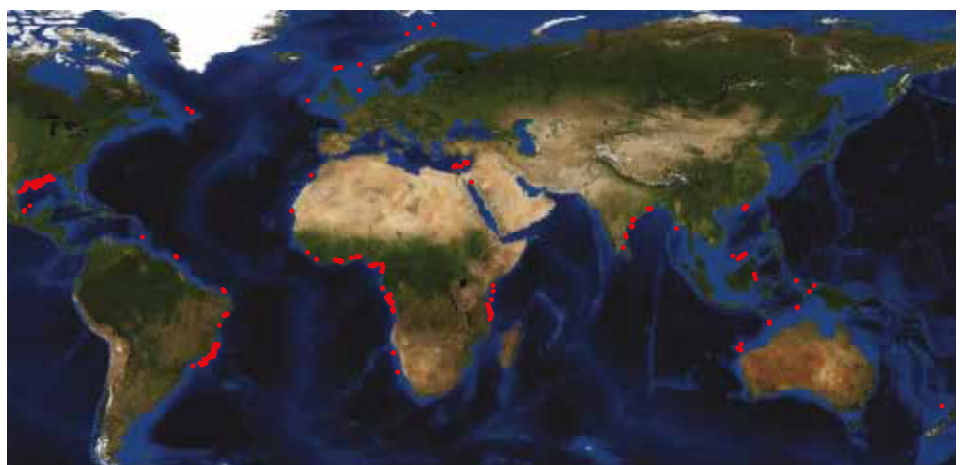


Source: Wood Mackenzie

During 2013, "Top" explorers, as defined by Wood Mackenzie, also continued to position themselves for future high impact growth through acreage acquisition in deepwater and frontier areas including the Atlantic Margin, East Africa, Australasia and the Arctic.<sup>28</sup>

Cairn's exploration strategy is focused on frontier opportunities within the Atlantic Margin and Mediterranean regions, underpinned by mature basin exploration and development projects in the UK and Norwegian North Sea, which will provide production in the medium term to fund future exploration. Consistent with this strategy, in 2013, Cairn acquired new interests in Morocco, Senegal, Republic of Ireland, Mauritania and the North Sea.

### 2013 Global Deepwater Drilling



Source: IHS

- World Energy Council 2013 – World Energy Scenarios: Composing energy future to 2015
- Oil and gas extracted from sources including shale, tight and coal-bed methane reservoirs using unconventional techniques
- Deepwater regions are assumed to include those with water depths  $\geq$  400 metres
- IFP Energies Nouvelles Offshore Hydrocarbons 2012
- IMF World Economic Outlook Update, January 2014
- IMF World Economic Outlook Update, January 2014
- UK Office for National Statistics
- IMF World Economic Outlook Update, January 2014
- Bloomberg News, 30 December 2013
- IEA Oil Market Report, January 2014
- IEA Oil Market Report, December 2013
- IEA Oil Market Report, January 2014
- EIA Short-Term Energy Outlook, January 2014
- EIA International Energy Outlook, July 2013
- EIA Natural Gas Production Lookback 2013
- IEA World Energy Outlook, 12 November 2013
- Oil and Gas UK Economic Report 2013
- Wood Mackenzie Review of 2013 UK Upstream Sector
- EY Global oil and gas transactions review 2013
- EY Global oil and gas transactions review 2013
- Wood Mackenzie Upstream Forum, November 2013
- PLS and Derrick Petroleum Services review of global upstream M&A activity, January 2014
- EY Global oil and gas transactions review 2013
- Wood Mackenzie, "The end of the upstream spending boom", October 2013
- IHS CERA Upstream Capitals Costs Index (UCCI), October 2013
- Wood Mackenzie Upstream Service, January 2014
- Wood Mackenzie Upstream Forum, November 2013
- Wood Mackenzie Upstream Forum, November 2013

## Where Cairn Is Focused

# A targeted portfolio with multiple growth opportunities

### Our Areas of Focus

Cairn's exploration strategy is focused on operated exploration in frontier basins along the Atlantic Margin and in the Mediterranean. This frontier exploration is complemented by mature basin activity of mainly non-operated interests in the UK and Norway.

Cairn's operated exploration drilling programme over the next year targets various passive margin and rift basin play types at a number of locations along the Atlantic Margin.

Cairn is focused on high value, appropriate equity and acreage positions in areas which have follow-on potential and good commercial terms in the case of success, whether they be emerging plays in frontier basins or new play concepts in mature areas such as the North Sea.

### Why We Focus on These Areas

Cairn's technical expertise combines experience in passive margin and rift basins with operational capability in frontier areas, including arctic and deepwater capability. The Atlantic Margin, formed by the break-up of a supercontinent millions of years ago, provides a range of underexplored, but promising opportunities which suit the Company's expertise. A number of other companies in the industry including Chevron Corporation, Genel Energy and Kosmos Energy are also pursuing exploration programmes in the region.

Illustrative geological reconstruction of the world  
~175 million years ago



----- Atlantic Margin

## Frontier basins

### The Atlantic Margin

#### Greenland

Site survey  
Preparation for future drilling  
Plugging and abandonment of wells

Discover more: [Operational Review P30-37](#)



#### Republic of Ireland

Preparation for appraisal drilling

Discover more: [Operational Review P30-37](#)



#### Morocco

Exploration seismic  
Site survey  
Exploration drilling

Discover more: [Operational Review P30-37](#)



#### Mauritania

Farmed in as non-operator,  
assessing existing 3D seismic

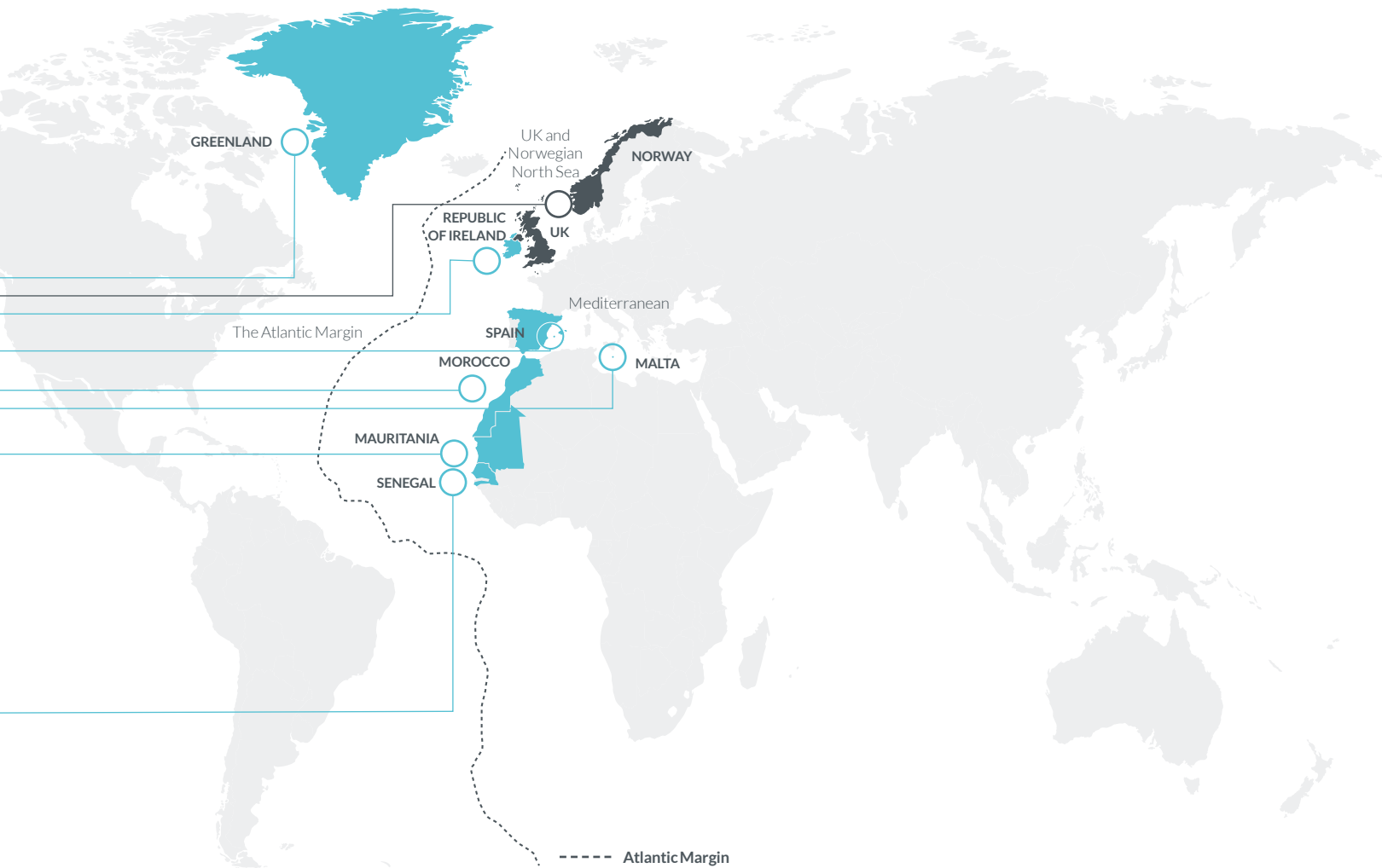
Discover more: [Operational Review P30-37](#)





Cairn's operated exploration drilling programme over the next year targets various passive margin and rift basin play types at a number of locations along the Atlantic Margin.

Present day map of the world



Mature basins

UK and Norwegian North Sea

Mediterranean

### Senegal

Site survey  
Preparation for exploration drilling

### Spain

Preparation for exploration 3D seismic

### Malta

Preparation for exploration 2D seismic

### UK and Norway

Non-operator appraisal drilling  
Non-operator exploration drilling  
Non-operator development projects

Discover more: [Operational Review](#)  
P30-37



Discover more: [Operational Review](#)  
P30-37



Discover more: [Operational Review](#)  
P30-37



Discover more: [Operational Review](#)  
P30-37



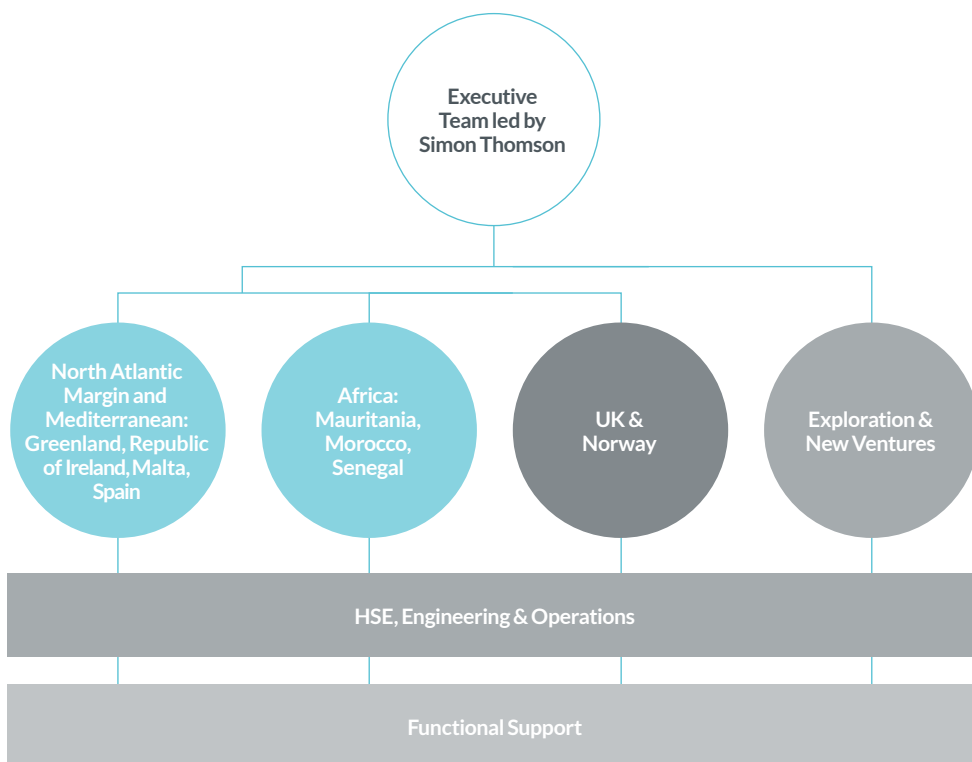
## Who Our Regional Team Is

# Cairn is structured for effective delivery of its regional portfolios

Cairn is led by Simon Thomson, CEO. Simon is joined on the executive team by Deputy Chief Executive Dr Mike Watts, who has responsibility for exploration and new ventures, and Managing Director and Chief Financial Officer, Jann Brown, whose responsibilities include the finance, human resources, corporate responsibility, corporate affairs and company secretariat functions. Jann is also the Director responsible for HSE matters.

Also reporting directly to Simon are Paul Mayland, Cairn's Chief Operating Officer (COO), with responsibility for regional operations as well as the commercial and legal functions within the Group and Phil Dolan, Cairn's Director of Operations, with responsibility for engineering, drilling and the Group's operational health, safety, security and environmental function. Richard Heaton, who reports to Mike is focused on new venture opportunities and exploration in his role as Exploration Director. The senior management works with established teams made up of experts in their various fields.

Reflecting the Company's focus on frontier and mature basins in the Atlantic Margin, the Mediterranean, and the UK and Norwegian North Sea, while recognising the different geographies and synergies within those areas, Cairn's organisational structure is divided into three regions (North Atlantic Margin and Mediterranean, Africa, UK and Norway). Each of these three regions is led by individuals with the appropriate skills to deliver efficient and safe operations. They in turn are supported by teams with the relevant experience required, whether it be geo-science, engineering, drilling or HSE. In each region Cairn takes care to consider the needs locally and, where it is appropriate and possible, the Group hires teams based in the country to help deliver projects.



### Our Regional Team

#### Chief Operating Officer Paul Mayland

Paul has been COO at Cairn Energy since January 2013 and has 24 years' industry experience. Paul rejoined the Group in August 2010 as Director of Business Development and Planning and played a key part in re-shaping Cairn's portfolio during 2011/2012 including the acquisitions of Agora Oil and Gas AS and Nautical Petroleum Plc.

Paul originally joined Cairn in 1996 from British Gas as Senior Petroleum Engineer. Paul was involved in all the key projects in Asia including Rajasthan.

From September 2006 Paul worked as Petroleum Engineering Manager for BG Canada before joining Vermilion Energy as a Senior Advisor in Corporate Business Development from 2008 to 2010, working on a number of asset and corporate acquisitions before returning to Cairn.



The senior management works with carefully established teams made up of experts in their field. Each of Cairn's three regions (North Atlantic Margin and Mediterranean, Africa, UK and Norway) are led by individuals with the appropriate skills to deliver efficient and safe operations.



### Regional Director – UK and Norway Brita Holstad

Brita joined Cairn as Regional Director of Assets (UK and Norway) in 2013. Prior to this Brita worked at Hess Norge AS where she was the Managing Director, leading Hess' business activities in Norway. Brita, who holds an MSc in Petroleum Geology from the Norwegian Institute of Technology, has over 20 years of experience in the industry, primarily in the Norwegian Continental Shelf with a number of years spent in France, working on fields offshore Congo. She has worked for a number of large and mid-sized independents, new starter and consultancy organisations, including Elf, Aker Kvaerner, Revus Energy ASA, Wintershall Norge AS and finally Hess. Since 2009, Brita held a number of senior leadership roles in Hess Norge AS, which encompassed responsibility for managing the asset base including Valhall, the largest Hess production base outside of the USA.



### Regional Director – North Atlantic Margin and Mediterranean Ian Watt

Ian Watt has been a Regional Director of Assets since Cairn's operations commenced in Greenland in 2008 and he is responsible for the North Atlantic Margin and Mediterranean. Ian has had wide-ranging experience in project planning, operations and risk management, including the preparation and evaluation of corporate contingency plans, operations management and political/risk assessment. He has designed and implemented crisis management plans and carried out operational reviews for numerous multi-national companies.



### Regional Director – Africa Robert JE Jones

Rob is the Regional Director of Assets (Africa) at Cairn; he has worked with Cairn for 15 years having formerly been Cairn's Business Development Director in India and Managing Director in Bangladesh. Rob has a Masters degree from Kingston University and has been in the oil and gas industry since graduating in 1977, having worked for Phillips Petroleum, Norsk Hydro and Natwest Markets in Egypt, Norway, the Far East, Sub-Saharan Africa, US and Vietnam. During his time in the industry Rob has been involved in a number of multi-billion barrel discoveries.



# Protecting people, the environment and communities at every stage

## Cairn complements technical skill with social and environmental consideration at every stage of the upstream oil and gas lifecycle

Cairn helps to create, add and realise value for stakeholders, but not at the expense of the safety of people and the environment. As well as responsibly managing risks associated with our business, we take a long-term approach. The diagram on this page offers an overview of the stages of oil and gas exploration and production.

### 1. Due Diligence

Before making an acquisition or investment, applying for an exploration licence or farming-in to an existing project, Cairn carries out an extensive risk screening process which includes assessing whether there are potential health and safety, social, human rights, political, corruption, security or environmental impacts. This is used in decision making on whether or not to proceed, and if investment goes ahead, it informs approaches to risk management going forward.

We have undertaken a number of due diligence processes for investment opportunities in 2013, including for interests acquired offshore Morocco, Mauritania, Senegal and Republic of Ireland.

### 2. Prequalification

When we apply for an exploration licence, the necessary documents are submitted to the relevant authorities. Typically this includes information about our legal status, financial capability, technical competence and plans to manage health, safety and environmental risks and contributions to local economic development.

### 3. Exploration Seismic

Once Cairn has been awarded the right to explore in a certain area, we may carry out seismic surveys to develop a picture of geological structures below the surface. This helps identify the likelihood of an area containing hydrocarbons. Seismic surveys are usually preceded by an assessment of environmental, social or human rights impacts which are managed through the Project Delivery Process.

During 2013, we completed a seismic survey offshore Morocco, continued seeking approval for a survey offshore Spain and began planning a seismic survey offshore Malta.

### 4. Site Survey

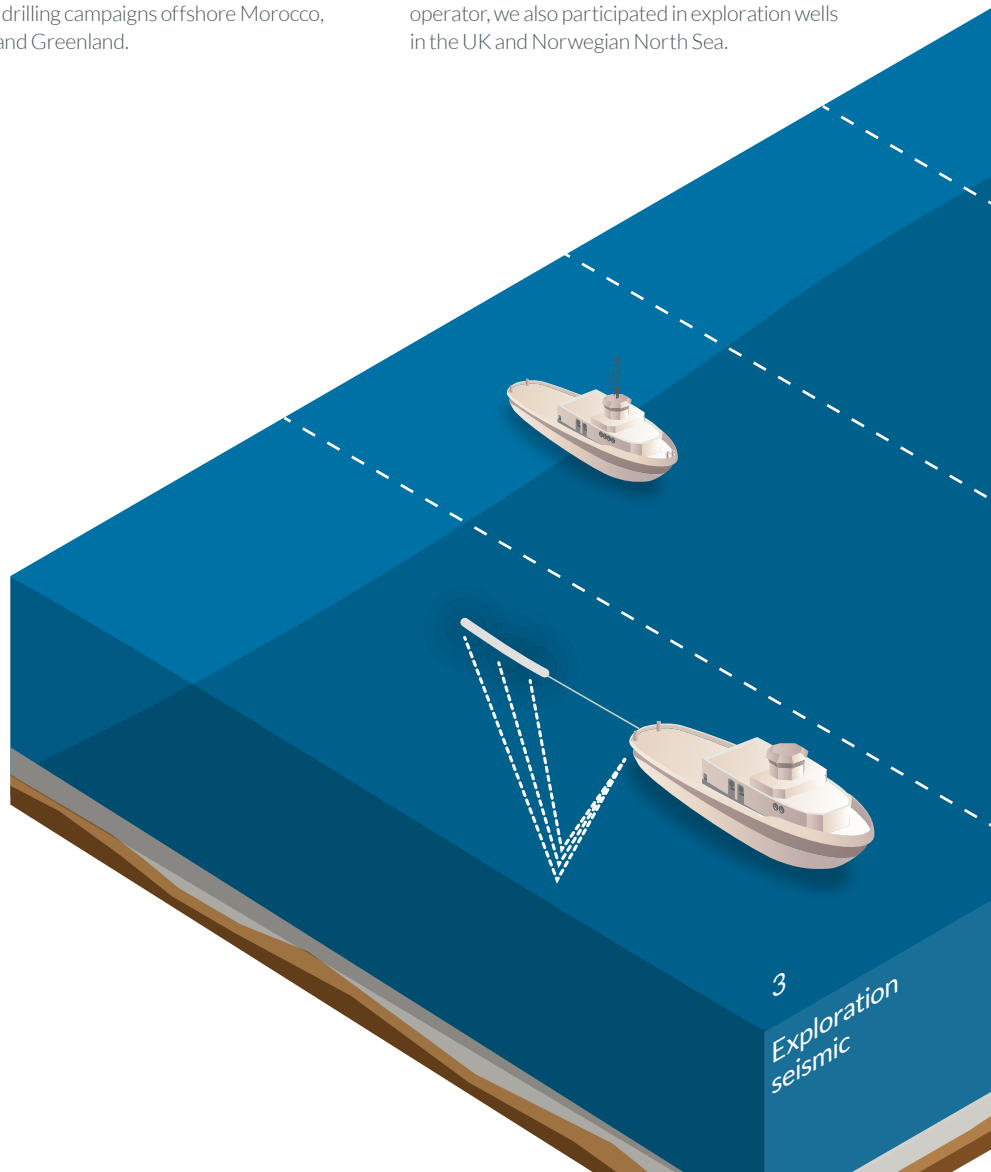
Before we commence on any drilling activity, site surveys are carried out to gain more detailed information on the area where an exploration well may be drilled and to confirm that the selected drilling location is safe and that any sensitive environments can be avoided. The process normally involves taking geological samples from the seabed and carrying out shallow seismic surveys. These activities have low social or environmental impacts and, therefore, usually do not require a separate environmental or social impact assessment.

In 2013, we completed site surveys in advance of future drilling campaigns offshore Morocco, Senegal and Greenland.

### 5. Exploration Drilling

Exploration wells are drilled to determine whether oil or gas is present. This phase can be accompanied by a step-change in activity and visibility to local people as offshore exploration can involve a drilling rig, supply vessels and helicopters for transporting personnel. Exploration drilling is preceded by an assessment to understand potential health, safety, environmental, social, security and human rights impacts. This identifies appropriate steps to reduce impacts and operate responsibly. Limited community development programmes may also be put into place at this time depending on the nature of the programme.

In 2013, we undertook exploration drilling offshore Morocco, and expect to drill further exploration wells in Morocco and Senegal in 2014. As non-operator, we also participated in exploration wells in the UK and Norwegian North Sea.



## 6. Appraisal Drilling

If promising amounts of oil and gas are confirmed during the exploration phase, field appraisal is used to establish the size and characteristics of the discovery and to provide technical information to determine the optimum method for recovery of the oil and gas. The potential impacts associated with appraisal drilling are comparable to exploration drilling and similar assessments are carried out in advance.

In 2013, appraisal drilling was undertaken on the Skarvfjell discovery, for which Cairn is non-operator. In 2014, Cairn, as Operator, and our JV partners intend to drill an appraisal well on the Spanish Point discovery.

## 7. Development

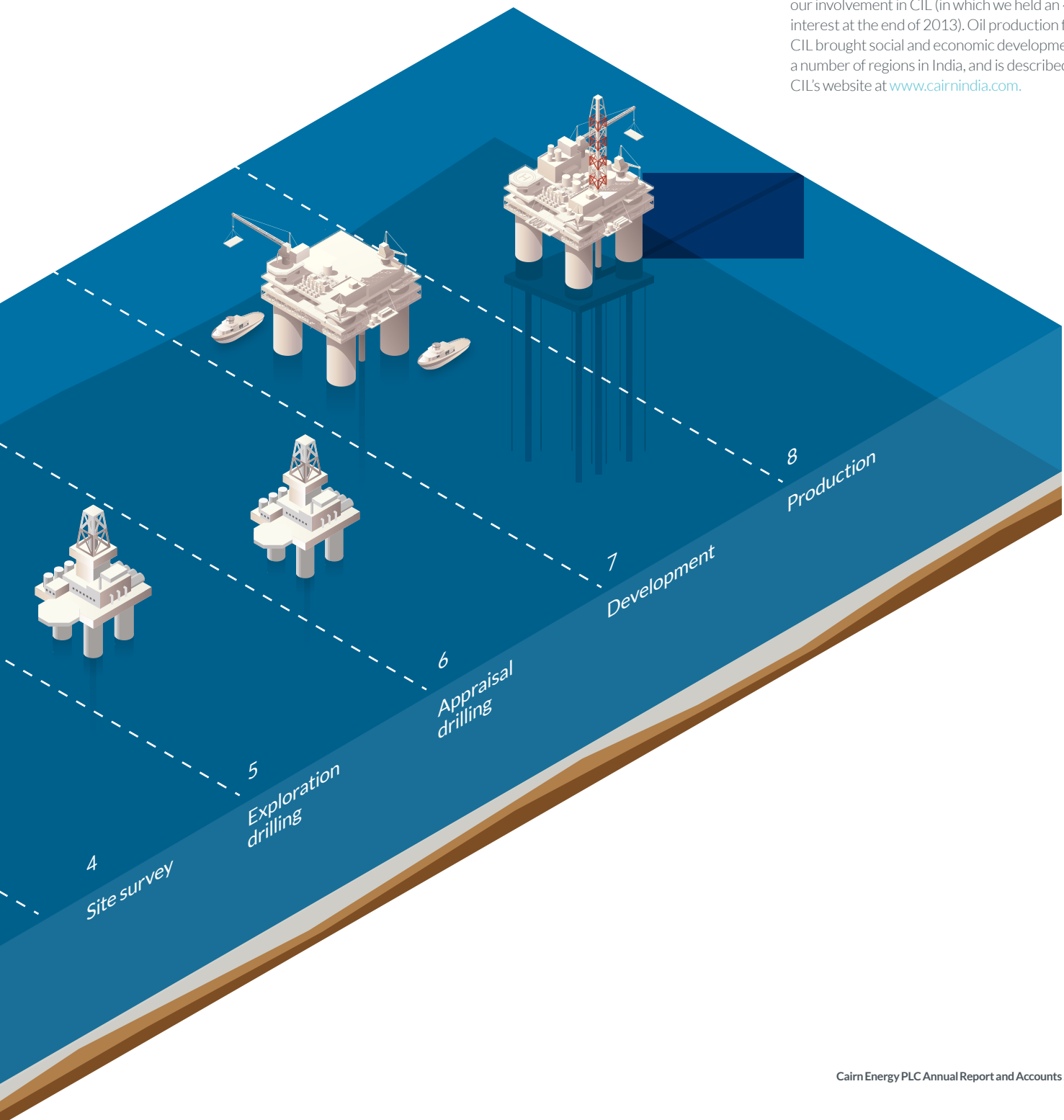
If appraisal wells show technically and commercially viable quantities of oil and gas, a development plan is prepared and submitted to the relevant authorities for approval. This includes a rigorous assessment of all the potential risks and a long-term assessment of environmental and social impacts covering a timeframe of between 10-30 years. The plan will also detail projected benefits to local communities, for example employment and supplier opportunities, as well as proposing how to manage potential impacts such as an influx of workers from outside the local community.

We are participating, in a non-operator capacity, in two development projects, the Kraken and Catcher Fields in the UK North Sea which when on stream will provide free cash flows to fund future activities.

## 8. Production

A variety of options are available for the production of oil and gas. During this phase, which can last many decades, regular reviews are made of social and environmental performance to ensure that impacts identified in the assessments are mitigated. Changes in the risks associated with activities are assessed throughout the production period.

We currently have no operated production, but historically had significant production through our involvement in CIL (in which we held an ~10% interest at the end of 2013). Oil production from CIL brought social and economic development to a number of regions in India, and is described on CIL's website at [www.cairindia.com](http://www.cairindia.com).



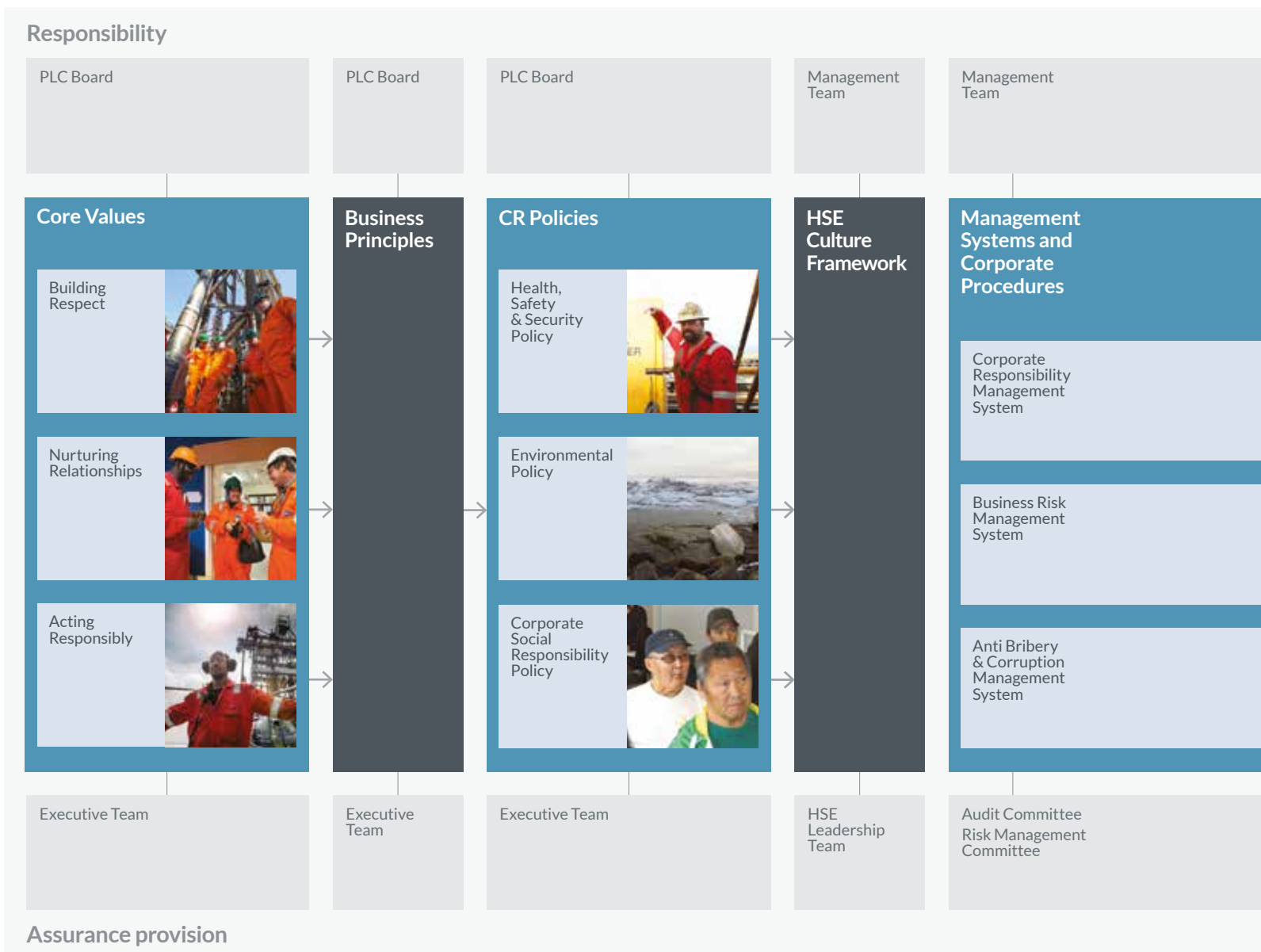
## How We Work Responsibly

# Cairn Energy's approach to managing Corporate Responsibility links its core values to everyday practice

Our goal is to contribute towards meeting the world's energy needs responsibly which means protecting the health, safety, security and wellbeing of people and the environment takes priority. We have comprehensive systems in place to manage our activities responsibly, known as Corporate Responsibility (CR). It is against this backdrop that we look to deliver value for our shareholders from within a balanced and sustainable portfolio.

Cairn's Business Principles and CR policies, which are based on our core values of building respect, nurturing relationships and acting responsibly (the 3Rs), define the Company's approach towards people, the environment, local communities and wider society. Our Business Principles spell out our commitment to the UN Global Compact through which we align our operations and strategies with the ten universally accepted principles in the areas of human rights, labour, environment and anti-

corruption. These Business Principles and CR Policies were updated most recently in September 2013 to reflect the expectations of our stakeholders and to strengthen the Company's commitments to anti-bribery and corruption, biodiversity and climate change management. Cairn also became a Participatory Company to the Extractive Industries Transparency Initiative (EITI) in September 2013. Our Business Principles and CR policies are available on our website at [www.cairnenergy.com/responsibility](http://www.cairnenergy.com/responsibility).



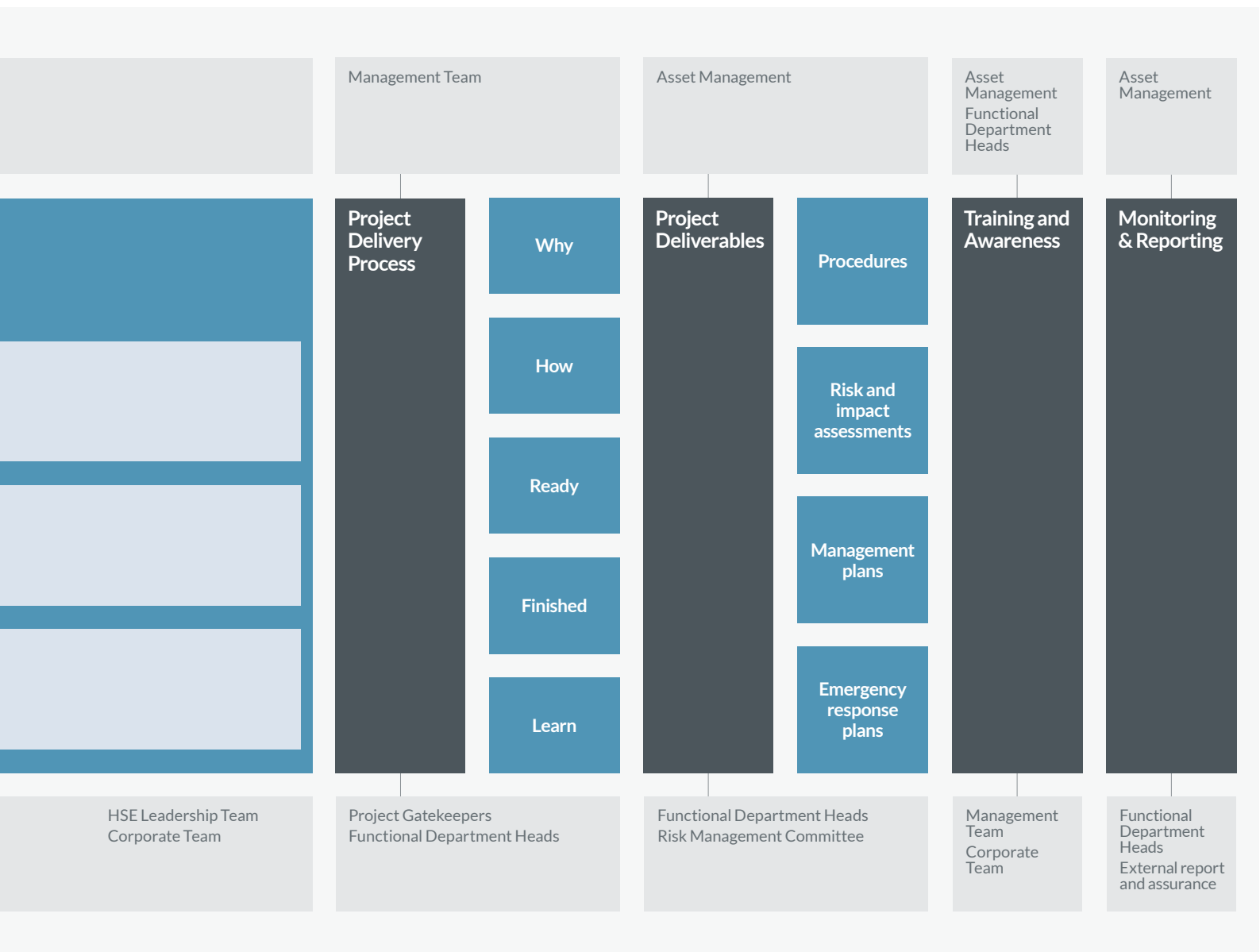
The graphic below shows how the Company's values, principles and management system embed good business practices to deliver safe and responsible operations. It also identifies responsibilities for each element and for assurance that the processes have been applied effectively. This approach helps equip us to respond to developing our business, while looking to meet expectations of our stakeholders for sustainable development.

In 2012, Cairn adopted an HSE Culture Framework, which defines the types of behaviours to be adopted by everyone to ensure a healthy and safe working environment. During 2013, it was rolled out to staff in the Edinburgh, Stavanger and London offices through a series of 15 interactive workshops, through which each team identified their plans for further strengthening their approach to HSE behaviours.

Our Project Delivery Process (PDP) ensures that the Company's Business Model and Business Principles work on the ground in our projects and activities. It comprises a five stage gated approach in which, at each stage, the progress of a project is assessed and, if set criteria are met, a decision is made whether to move on to the next stage. In common with Cairn's entire CR Management System (CRMS), the PDP is designed to reduce risks to acceptable levels.

Reflecting our commitment to prioritise HSE throughout the business, the HSE Leadership Team chaired by Jann Brown, the Managing Director & Chief Financial Officer (CFO), and comprising key managers continued to provide oversight on the Company's approach and performance on all health, safety, environmental, security and human rights matters during 2013.

Our Business Principles and CR policies define the Company's approach towards people, the environment, local communities and wider society.



## How We Nurture Our People

# People at Cairn are a priority

We operate in an increasingly competitive and global industry which requires people who are skilled and experienced in many different disciplines. This demand for talented people in the oil and gas industry will continue for years to come as the industry continues to develop

It is against this backdrop that we are looking to recruit talented people with the required technical capability in the areas where they are needed most. As part of our aim to retain this talent we look to create a vibrant working environment and culture which engages and retains our talent and to provide the appropriate experience and training to allow staff to perform to the best of their abilities.

The recruitment and retention of this skilled talent is one of the challenges facing the oil and gas industry. In 2013, Cairn increased its staff headcount by 13.7% globally. A quarter of these new roles were in geo-science and engineering and were mainly filled by experienced professionals with many years of experience. Throughout our recruitment process, the Employee Value Proposition (EVP), which outlines Cairn's culture and commitment to our people, is well communicated to candidates.

Cairn continues to ensure that the Company has a steady pipeline of young talent coming into the organisation by maintaining strong relationships with a number of schools and universities in addition to offering summer internships. In 2013, Cairn partnered with Career Academies, a national organisation which aims to increase social mobility and raise the aspirations of 16-to-19-year-olds, providing them with real-life experiences of the workplace and thereby boosting their employability skills. In 2013, Cairn provided work placements for six Career Academies students, providing them with an insight into the oil and gas industry and mentoring by a staff member.

### Learning and Development

Having recruited good people, the Company also invests in them by ensuring that they have the appropriate training and experience required to perform their jobs effectively in the delivery of the Company's strategy and business plan. Cairn continues to be very active in providing staff with development opportunities through a variety of means (internal and external courses, conferences, executive coaching, mentoring, on-the-job training, projects, etc.) to enhance their skills and capabilities.

In 2013, a total of 1,214 training days were undertaken by staff. This represents on average 5.8 days per employee compared to 5.5 days in 2012, and a national average of 3.57 days (source: CIPD Learning and Development Report 2013).

As an international company, we are able to offer overseas development opportunities for selected individuals. An example of this is our Deputy Head of Legal who expressed an interest in working overseas and was provided with the opportunity to work in Morocco during our drilling campaign. As he noted:

"I believe that my secondment to Morocco as General Manager has been of huge benefit, from the perspective of both my career and personal development. It has given me the opportunity to take on a different role from my normal duties in the legal department in Edinburgh, including acting as the Company's liaison with the Moroccan Government departments before and during our first drilling campaign in the country."





In 2013, Cairn was once again successfully accredited as an Investor in People (IIP), having been accredited for the first time in 2004. Investors in People is a UK accreditation body which helps employers to realise the potential of their people and improve standards.

The assessor commented:

"Learning and development, including giving members of staff regular feedback on their performance, both formally and informally, is another key strength in your company and the standard of on-the-job training and informal coaching and mentoring for all members of staff is very high." (IIP Scotland Report, April 2013)

The performance appraisal process was identified by the IIP audit process as an area for improvement and this is now one of the HR 2014 objectives.

### Succession Planning

To address risks associated with the potential loss of key personnel in a competitive labour marketplace, we undertook a study into succession planning, the results of which were shared with the Board of Directors in 2013. Our latest review of the talent pipeline demonstrates that in addition to the people who are ready now to be successors for key roles, our succession planning work also confirmed that 64% of key roles potentially have at least one successor ready in 24+ months. Plans are now being made to develop the identified talent to ensure that they are capable of fulfilling key roles when required, in addition to planning how best to address gaps identified where no potential successor has been identified.

### Culture and Engagement

The maintenance of our culture is an important factor in differentiating us from other exploration and production companies. The Cairn values of Respect, Relationship and Responsibility (the three Rs) are well understood by our employees and as part of our aim to further integrate these core values into all aspects of our business, in 2013 we undertook a 360-degree appraisal on all members of staff. In 2013, we also started the process of reviewing our performance management practices. This review is aimed at ensuring a clear line of sight between Company, team and individual objectives in addition to recognising and rewarding behaviours which are consistent with our Company values and culture.

### Diversity

Diversity is about valuing variety and individual differences and creating a working culture, environment and practices which respect these differences. As research indicates, a diverse workforce can improve creativity and problem solving resulting in better decisions.

- 50% of Cairn staff are women
- 10% of Cairn staff work part-time
- 100% of parents return to work following maternity/adoption/paternity leave
- 21 different nationalities are employed at Cairn
- 3.4% of the workforce are disabled
- Average age at Cairn is 42.

Currently, 28% of management roles at Cairn are held by women and 20% of the PLC Board is composed of women. In addition, Cairn is actively participating in a major piece of industry research aimed at encouraging more women onto boards. The 30% Club is a group of chairmen and organisations committed to promoting more women onto boards. Cairn is actively participating in their "Balancing the Pyramid" project which is exploring the behavioural differences between men and women and what makes women successful leaders in the corporate environment. Cairn's Managing Director & Chief Financial Officer, Jann Brown, is a committee member of the 30% Club.

### HSE Culture Framework

In June 2013, Cairn commenced the roll-out of its HSE culture framework to maintain and strengthen our existing HSE culture and performance and to engage our staff and contractors in that process. The HSE culture framework identifies and reinforces the HSE behaviours that Cairn needs to support excellent HSE performance. The framework was rolled out to our people via workshops which were facilitated by the Keil Centre, who are experts in the human and organisational factors which impact on health and safety. In total, 15 workshops were held in the UK and our overseas offices to ensure that everyone had an opportunity to attend.

To continue the process of embedding the HSE culture framework at Cairn, a number of further developments are planned for 2014 including:

- incorporating an HSE objective into every senior manager's Performance Review;
- using the framework in the investigation of incidents; and
- a follow-up survey in 2015 to measure how we have performed in strengthening the visibility of our existing HSE culture.



#### Edinburgh Headquarters

Jean Bernard Houssin, Geoscientist and Laura Bornatici, Geophysicist.



#### Edinburgh Headquarters

Natalie Adams in the Exploration department.

## How We Monitor Performance

# Key Performance Indicators play a key role in delivering strategy

Cairn has in place both financial and non-financial key performance indicators (KPIs) which are used to monitor progress in delivering the Group's strategy

The 2013 KPIs, which were set out on page 29 of the Annual Report and Accounts 2012, related to delivering a sustainable business, maintaining a balanced portfolio and achieving operational excellence.

The Group's 2013 KPIs were reflective of the early stage in the value creation cycle, rather than the more traditional KPIs for oil and gas E&P companies (such as production or operating cost targets), which the Board currently considers are not relevant as a measure of the Group's performance.

Good progress has been made across the 2013 KPIs and a brief update on progress is presented in the table below.

The final decision on the overall achievement of the KPI's was made at the Remuneration Committee meeting on 3 December 2013.

## 2013 KPIs

# Delivering a Sustainable Business

### Purpose

Preserve cash for investment

2013 KPI	Measurement	2013 Performance	KPI Remuneration Committee Decision
<b>Conclude asset swap or divestment of asset(s) that do not fit with the strategy</b>	Conclude an asset swap or divestment of the 6% interest in Mariner at a price no less than the acquisition value.	<p>The Group successfully completed the divestment of the Mariner asset during the year with the sale to Dyas. Cairn held a 6% interest in the Mariner asset based in the UK. The relatively low working interest and the high capital cost of the development project and the expected returns did not make this a core asset.</p> <p>On disposal, Cairn realised an accounting loss of US\$25m. Consideration received of US\$72m, included cash payment of US\$43m and a refund of the 2013 exploration costs incurred by Cairn of US\$29m.</p> <p><b>30</b> Discover more: <i>Operational Review</i> P30-37</p>	<b>Partially achieved</b>
<b>Maintain access to liquid reserves, including a contingency at all times, to meet planned funding</b>	Actual and forecast expenditures, together with expected bank lending for developments, are monitored and reported on a monthly basis to the Management and Executive Teams and Board.	<p>The Group continues to closely monitor its liquid resources and during the year maintained the required amounts to meet this KPI. At appropriate times, Cairn will look to introduce debt into its liquidity portfolio to part-fund planned North Sea developments.</p> <p><b>38</b> Discover more: <i>Financial Review</i> P38-41</p>	<b>Achieved</b>
<b>Ensure that overheads remain within the approved 2013 budget</b>	Actual and forecast expenditures on office related costs are monitored and reported on a monthly basis to the Management and Executive Teams and Board.	<p>Cairn controls its overhead costs by monitoring gross controllable costs against the approved Group budget, where controllable costs are all administrative and office costs excluding depreciation and amortisation, share-based payment charges and performance related bonus payments prior to directly attributable costs being recharged to assets. Performance targets are set at threshold, base and stretch target levels where actual costs are between 110% and 100%, 100% and 90% or less than 90% respectively of the approved budget.</p> <p>During the year, the Group achieved the base target level.</p> <p><b>38</b> Discover more: <i>Financial Review</i> P38-41</p>	<b>Achieved</b>

# Maintaining a Balanced Portfolio

## Purpose

Grow the reserves and resources base to provide the funding for future growth and cash-flow

2013 KPI	Measurement	2013 Performance	KPI Remuneration Committee Decision
<b>Progress exploration and appraisal activities in the UK and Norway sectors of the North Sea that will add net 2C resources in excess of 30 mmb/annum</b>	Resources and reserves figures evaluated by internal technical specialists and verified by independent consultants.	<p>The Group participated in four exploration wells and three appraisal wells in the UK/Norway region during 2013. The Bonneville exploration well and its sidetrack in the Catcher licence discovered oil and the appraisal wells were successful in providing information towards delineating the fields.</p> <p>Although relative performance was good, the absolute performance of adding 30 mmb discovered resources was not achieved from these wells.</p> <p> Discover more: <a href="#">Operational Review P30-37</a></p>	<b>Not achieved</b>
<b>Progress four or more independent high impact exploration prospects with overall target risked net resource &gt;100 mmb, approved for drilling in 2013/2014</b>	The outcome of technical and commercial evaluations of exploration opportunities are documented in a prospect and lead inventory, which is verified by independent consultants. The potential values of these prospects are also included in the Company valuation reports.	<p>Mapping of prospects has progressed in 2013 and there are now four drill-ready (but subject to final regulatory approval) prospects in Senegal, the Republic of Ireland and Morocco which will test &gt;120 mmb of risked resources. The first of these prospects will be drilled by the Cajun Express rig in Senegal in Q2 2014.</p> <p> Discover more: <a href="#">Operational Review P30-37</a></p>	<b>Achieved</b>
<b>Work with the operator and other JV partners to progress Catcher and Kraken developments to FDPs thereby moving 2C resources to 2P reserves</b>	The outcome of Cairn's technical and commercial evaluation of development projects is included in an Investment Proposal, an internal document, which requires sign-off by appropriate regional, asset and functional department heads. Estimates for the associated reserves figures are also verified by independent consultants. The potential values of these developments are also included in the Company valuation reports.	<p>Board sanction and DECC approval were received for the development of the Kraken Field with first oil scheduled for H2 2016/H1 2017.</p> <p>Development studies on the Premier operated Catcher field delayed the FDP submission to DECC until Q1 2014 (by the operator). Therefore, the KPI was only partially achieved.</p> <p>It is expected that 60 mmb 2P reserves will be booked in relation to the two development projects.</p> <p> Discover more: <a href="#">Operational Review P30-37</a></p>	<b>Partially achieved</b>
<b>Discover potentially commercial hydrocarbon resources through drilling high potential operated exploration or appraisal well(s) in 2013</b>	The outcome of technical and commercial evaluations of exploration opportunities are documented in a prospect and lead inventory, which is verified by independent consultants. The potential value of these prospects in the event of success is also included in the Company valuation reports.	<p>Operated drilling on the Foun Draa prospect in Morocco did not commence until late October 2013 and commercial hydrocarbons were not discovered. The Foun Draa well was in the progress of being drilled when the Remuneration Committee reviewed the final KPI results. The KPI, therefore, was deemed not applicable.</p> <p> Discover more: <a href="#">Operational Review P30-37</a></p>	<b>Not applicable as drilling was still in progress when the Remuneration Committee reviewed the final KPI results on 3 December 2013</b>

## How We Monitor Performance

Continued

# Seeking Operational Excellence

### Purpose

Successfully complete operated 2013 work programmes

2013 KPI	Measurement	2013 Performance	KPI Remuneration Committee Decision
<p><b>Complete 2013 operational activities on schedule, under budget, to the desired quality</b></p>	<p>Progress against project plans and budgets are closely monitored by regional management and reported to the Management and Executive Teams and Board.</p>	<p>Operated activities, for the most part, were successfully completed on budget and on schedule in 2013 in Greenland (including the environmental baseline and site surveys), Morocco (3D seismic and site surveys) and Senegal (site surveys). There were some slight delays to the permanent abandonment of four exploration wells drilled in Greenland due to unfavourable weather which had a small impact on the budget. Operated drilling commenced in Q4 2013 with the Cajun Express on the Fourn Draa prospect in Morocco and due to delays, the projected budget has increased.</p> <p><b>30</b> Discover more: <i>Operational Review</i> P30-37</p>	<p><b>Partially achieved</b></p>
<p><b>To minimise injuries and environmental incidents on 2013 operated activities:</b></p> <ul style="list-style-type: none"> <li>- Total Recordable Injuries Rate (TRIR) target of less than 2.0 TRI/million hours</li> <li>- No oil spills</li> </ul>	<p>HSE performance is monitored through a range of performance measures. A rigorous approach is taken to identifying, reporting and investigating safety and environmental incidents and the outcomes are recorded in an audited database.</p> <p>Performance is closely monitored by the Management and HSE Leadership Teams and reported regularly to the Executive Team and Board.</p>	<p>There have been two LTIs and three medical treatment cases during the 2013 operated activities and as a result the TRIR was 6.3 TRIR/million hours which was disappointing given the Company's historical performance in the HSE area. There were no oil spills to the environment in 2013.</p> <p><b>50</b> Discover more: <i>Working Responsibly</i> P50-61</p>	<p><b>Partially achieved</b></p>



An FPSO and flow line

## Purpose

## Continue to enhance the Group's approach to HSE risk identification and management

KPI Remuneration  
Committee Decision

## 2013 KPI

## Measurement

## 2013 Performance

Achieved

**Achieve targets for 10 HSE leading performance indicators across the areas of:**

- Awareness raising of HSE management systems and procedures
- Engagement with contractors
- Communication of HSE approach and performance
- Risk assessment and management

Progress made on delivery of the HSE leading performance indicators is regularly monitored by the HSE Leadership Team.

Good progress was made during 2013 on 9 out of 10 of the HSE leading performance indicators, which included:

- Roll-out of the updated Group CR Management System and new HSE Culture Framework
- Implementing new approach to travel risk assessments
- Enhancements to the procedures for managing contractor HSE through the tender and operational phases, and increased senior management engagement

The HSE LPI relating to the completion of lessons learned from previous projects was not formally achieved. However, there is a process which is strictly applied for ensuring lessons from previous projects are considered in future projects. Therefore, it was agreed that this KPI had been achieved.

50 Discover more: *Working Responsibly*  
P50-61

## Case Study

## Development of the Kraken field

Cairn has a 25% WI in the Kraken field, with JV partners EnQuest (operator, 60% WI) and First Oil (15% WI). The Kraken field is located in the UK North Sea and is currently under development with first oil expected in H2 2016/ 2017.

To progress the project and ensure that all partners are comfortable with the activity, Cairn and the other JV partners meet at least once a month. In addition, specialist working groups meet to discuss and agree specific areas, e.g. well locations. The team at Cairn who are working on Kraken involves individuals from various departments including Engineering (Reservoir and Facilities), Exploration (Geologists and Geophysicists), HSE, Legal and Finance. This ensures that Cairn has the right team with the right experience and skills to review and give input to proposals from the operator regarding the project and ensure that any plans meet with Cairn's technical, HSE and commercial standards.

The Kraken field received DECC approval at the end of 2013. When on stream, forecast production is 50,000 bopd, 12,500 of which is net to Cairn. This and other development projects will provide the future free cash flow to deliver Cairn's longer term exploration programme.



## How We Monitor Performance

Continued





# 2014 KPIs

The 2014 Group KPIs in the table below have been set by the Board on 3 December 2013 based on the Group's current portfolio and prospects and objectives as set out in the Business Plan and 2014 Work Programme and Budget:

### Maintaining a Balanced Portfolio

Purpose	Objective	2014 KPI	Risks to the achievement of KPI
<b>Grow the reserves and resources base to provide a basis for future growth</b>	Achieve exploration and appraisal success through discovery of commercial hydrocarbons in 2014	<b>Mature Basin:</b> Invest in exploration and appraisal activities in the UK and Norway sectors of the North Sea which will add net 2C resources in excess of 10 mmboe	<ul style="list-style-type: none"> <li>- Lack of exploration success</li> <li>- Reliance on JV operators for asset performance</li> </ul> <p> See: <i>How We Manage Risk</i> P42-49 for mitigants</p>
		<b>Frontier Basin:</b> Invest in exploration and appraisal activities in Morocco, Senegal and Republic of Ireland which will add net 2C resources in excess of 40 mmboe	<ul style="list-style-type: none"> <li>- Lack of exploration success</li> </ul> <p> See: <i>How We Manage Risk</i> P42-49 for mitigants</p>
		Mature high impact exploration prospects ready for drilling in 2015 or 2016	Mature a minimum of six new independent "drill-ready" prospects in each category (mature /frontier basin) which meet our investment criteria and which could be considered for drilling in 2015 or 2016

### Seeking Operational Excellence

Purpose	Objective	2014 KPI	Risks to the achievement of KPI
<b>Deliver operational excellence in all 2014 activities and maintain licence to operate</b>	Successfully complete operated and non-operated 2014 work programmes	Deliver all operated and non-operated asset projects (technical studies, surveys, seismic and drilling programmes) on schedule and budget (including manpower costs), with full data recovery	<ul style="list-style-type: none"> <li>- Operated exploration work programmes not executed on schedule and budget</li> <li>- Reliance on JV operators for asset performance</li> </ul> <p> See: <i>How We Manage Risk</i> P42-49 for mitigants</p>
		Progress North Sea development projects, remaining within 10% of capital guidance and first oil dates scheduled within 6 months of project sanctioned base case estimates	<ul style="list-style-type: none"> <li>- Kraken and Catcher development projects not executed on schedule and budget</li> <li>- Reliance on JV operators for asset performance</li> </ul> <p> See: <i>How We Manage Risk</i> P42-49 for mitigants</p>
		Minimise injuries and environmental incidents in 2014 operated activities: <ul style="list-style-type: none"> <li>- TRIR target of less than 2.0 TRIR/million hours</li> <li>- No oil spills to the environment</li> </ul>	<ul style="list-style-type: none"> <li>- Health, safety, environment and security incidents</li> </ul> <p> See: <i>How We Manage Risk</i> P42-49 for mitigants</p>
		Achieve targets for ten HSES leading performance indicators across the areas of: <ul style="list-style-type: none"> <li>- Knowledge of HSES procedures</li> <li>- Engagement with contractors regarding safety standards</li> <li>- Communication of HSES approach and performance</li> <li>- HSES risk assessment and management</li> </ul>	<ul style="list-style-type: none"> <li>- Health, safety, environment and security incidents</li> </ul> <p> See: <i>How We Manage Risk</i> P42-49 for mitigants</p>

## Delivering a Sustainable Business

Purpose	Objective	2014 KPI	Risks to the achievement of KPI
<b>Preserve cash for investment</b>	Retain balance sheet strength	Maintain liquid reserves including undrawn committed banking facilities to meet planned funding commitments plus a cushion at all times	<ul style="list-style-type: none"> <li>- Restriction on ability to sell CIL shareholding</li> <li>- Potential tax liabilities relating to Indian Income Tax Department enquiry</li> <li>- Cost pressures in the industry</li> <li>- Uncertainty in fiscal regimes</li> <li>- Operated exploration work programmes not executed on schedule and budget</li> <li>- Kraken and Catcher development projects not executed on schedule and budget</li> </ul>

**42** See: *How We Manage Risk*  
P42-49 for mitigants

## Operational Review

Dr Mike Watts

Cairn has a balanced portfolio of exploration and development assets.

Our exploration strategy is to focus on frontier or overlooked basins where we identify geological potential and a suitable acreage position can be secured on appropriate commercial terms.

Cajun Express drilling unit, offshore Morocco




## Overview

Cairn has a balanced portfolio of exploration and development assets.

Our exploration strategy is to focus on frontier or overlooked basins where we identify geological potential and a suitable acreage position can be secured on appropriate commercial terms. Our current target areas focus on building positions of medium risk/high reward exploration potential along the Atlantic Margin and the Mediterranean, complemented by lower risk/medium reward positions in the UK/Norwegian North Sea. We seek to participate in assets at equity levels appropriate to the overall scale and capital resources of the Group, either as operator or as non-operator in like-minded joint venture groups where we can still exert influence.

Our non-operated pre-development and future production interests in the North Sea provide balance to our exploration portfolio. At present these projects comprise Kraken (where we have booked 2P reserves of 30 mmboe) and Catcher (2C resources of 30 mmboe net to Cairn) in the UK and the Skarvfjell and Grosbeak fields in Norway.

We continually evaluate the entire asset base to ensure that our equity is at appropriate levels to offer potential growth opportunities, allied with appropriate financial risk exposure.



**Dr Mike Watts**

Deputy CEO

17 March 2014



## Frontier basins

### Atlantic Margin

Cairn's frontier Atlantic Margin exploration strategy is focused along the multiple play types related to the break up of the supercontinent Pangea.

Discover more: *Operational Review*  
P32-34

32

### Mediterranean

Cairn has interests offshore Spain and has entered into an ESA with the Government of Malta.

Discover more: *Operational Review*  
P35

35

## Mature basins

### UK and Norway

Over the last two years, the Group has built an attractive business and acreage position in the North Sea.

Discover more: *Operational Review*  
P36-37

36

### Group Booked 2P Reserves

A total of 30.1 mmboe were booked as 2P Reserves at 31 December 2013 on a net working interest basis.

2P	Reserves 31.12.12 mmboe	Produced in 2013 mmboe	Additions in 2013 mmboe	Revisions in 2013 mmboe	Reserves 31.12.13 mmboe
Kraken	0.0	(0.0)	0.0	30.0	30.0
Keddington	0.053	(0.002)	0.0	0.0	0.050
Mariner 9/11a	15.9	(0.0)	(15.9)	0.0	0.0
Total	16.0	(0.002)	(15.9)	30.0	30.1

- The Group's 2P Reserves increased by 14.1 mmboe during 2013 due to the net impact of the Kraken project FDP and Mariner asset divestment.
- Further reserves additions are expected when the Catcher field achieves FDP approval.

## Operational Review Continued

### Atlantic Margin

#### Frontier Basin Exploration – Atlantic Margin

We currently have interests in the following areas along the Atlantic Margin:

##### Morocco

Cairn has established a position in both the Jurassic carbonate shelf and the emerging deep-water Mesozoic clastic exploration plays. The region is attracting industry interest, with other operators taking licences in the area and the industry targeting up to 10 wells over the next three years.

The FD-1 exploration well located in 1,500m of water approximately 120km offshore Morocco in the Fom Draa block (Cairn 50% WI, Operator) was plugged and abandoned. The primary target of the well was a Late Jurassic/Early Cretaceous deep-water turbidite slope fan and channel complex. While gas shows confirmed an active thermogenic petroleum system, the well did not encounter clastic reservoirs.

The JM-1 well (Cairn WI 37.5%, Operator) drilled to evaluate Upper Jurassic and Middle Jurassic objectives reached a total depth of 3,711m TVDSS and has been plugged and abandoned without testing.

In the Upper Jurassic section, the well has confirmed the presence of heavy oil over a gross interval of 110m as originally tested in the 1968 MO-2 well,

some 2km from the JM-1 well. Reservoir quality and the oil gravity in the Upper Jurassic across the Cap Juby structure require further evaluation by Cairn and its joint venture partners (ONHYM and Genel Energy). Work is ongoing to correlate the core and log data from JM-1 with other wells on Cap Juby to evaluate the extent of moveable hydrocarbons and how any further assessment should be conducted.

The Middle Jurassic objective was encountered with limited primary porosity and evaluation of well logs and side wall cores continues.

Cairn farmed-in (20% WI non-operator) to the Cap Boujdour Permit operated by Kosmos Energy and partnered by ONHYM, subject to Government of Morocco approval. Located ~50km offshore, the permit covers an area of 29,740km<sup>2</sup> in the Aaiun Basin in water depths of 1,000 – 3,000m. The permit is covered by a regional 2D grid and 2,000km<sup>2</sup> of 3D seismic surveys.

Kosmos has identified several prospects within the 3D area, with the largest of these, Gargaa, to be drilled, in water depths of ~2,135m. The gross mean unrisks prospective resource is ~1 bn boe. The Atwood Achiever, a 6th generation drillship, is being mobilised for the drilling planned to commence Q4 2014 while final preparations are being made for a further exploration 3D survey that is due to commence later this year.

#### Cajun Express

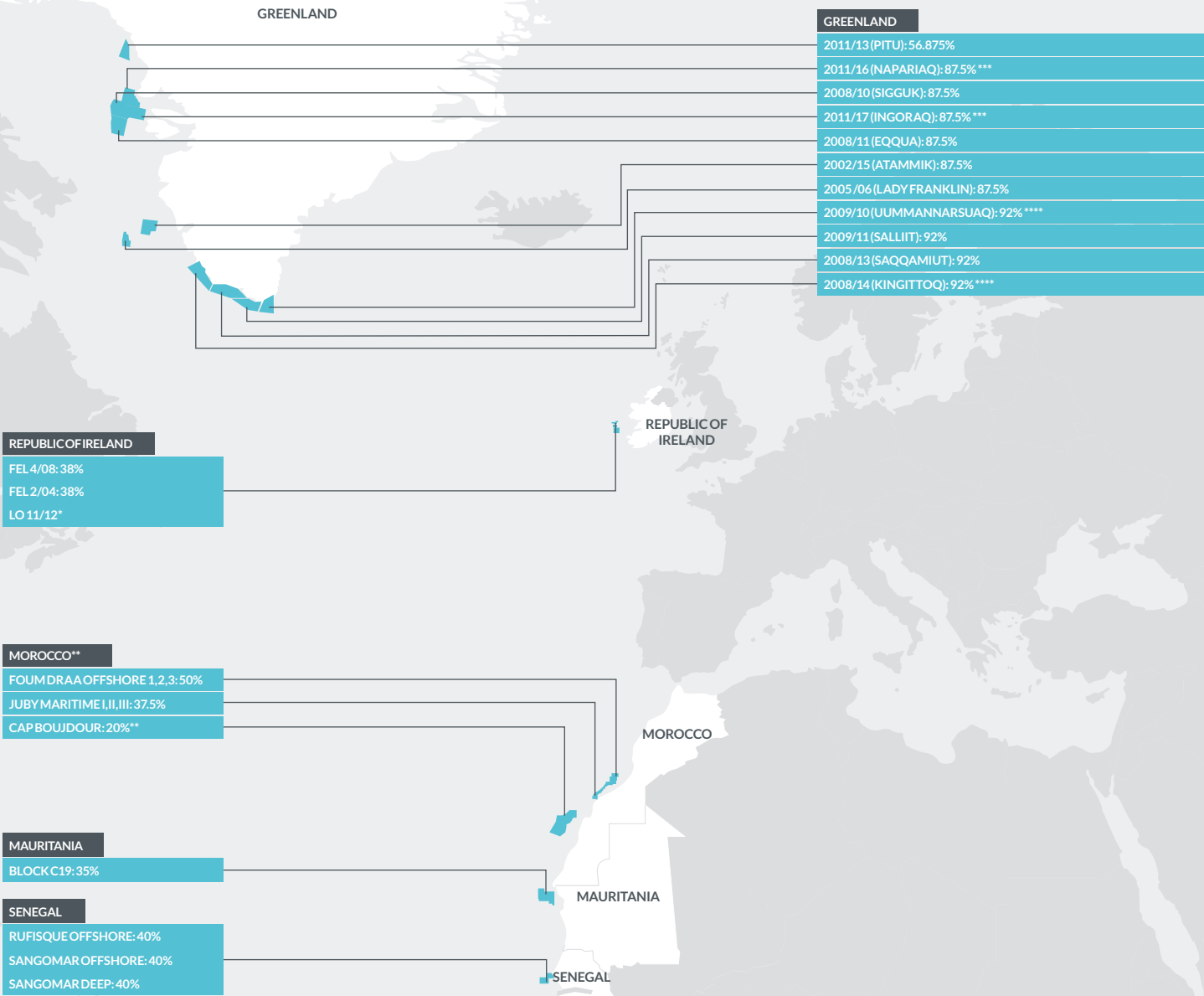
In April 2013 Cairn contracted the 'Cajun Express' drilling unit from Transocean for Cairn's planned multi-well frontier exploration programme in Morocco and Senegal.

#### Management visit

Senior management, including Simon Thomson, CEO visited the Cajun Express offshore Morocco in November 2013.



Atlantic Margin



\* The Irish Government has accepted an application to convert licence option 11/2 to an exploration licence (FEL 1/14) (Cairn has a 38% WI and will be Operator).

\*\* Cairn has entered into a farm-in agreement with Kosmos Energy and the Moroccan National Oil Company ('ONHYM') for a 20% non-operated interest in the Cap Boujdour block offshore North West Africa which is scheduled for drilling in H2 2014. This is now subject to government approval.

\*\*\* Cairn has issued a relinquishment notice in respect of Greenland Licences 2011/16 (Napariaq) and 2011/17 (Ingoraq) and these relinquishments are currently being considered by the regulatory authorities.

\*\*\*\* Cairn has issued a relinquishment notice in respect of Greenland Licences 2008/14 (Kingittoq) and 2009/10 (Uummannarsuaq) and these relinquishments are currently being considered by the regulatory authorities.

## Operational Review Continued

### Atlantic Margin

#### Senegal

Cairn's planned two well exploration programme offshore Senegal is due to commence in April.

The three exploration blocks (Sangomar Offshore, Sangomar Deep and the Rufisque Offshore blocks) cover an area of ~7,490km<sup>2</sup> near shore to deep water exploration over the shelf, slope and basin floor of the Senegalese portion of the prospective Mauritania-Senegal-Guinea-Bissau Basin. The deeper water western portion of the acreage is covered by a 2,050km<sup>2</sup> 3D seismic survey.

The initial exploration well, known as 'FAN-1' will be located on the North Fan Prospect in 1,427m water depth. This well will target multiple stacked deepwater fans interpreted as potentially thick, high quality clastic reservoirs, the two largest of which Cairn currently estimates to have gross mean unrisks prospective resource of 282 mmbbls and 535 mmbbls respectively. Other prospects and leads of this type provide follow up potential in the case of success at FAN-1.

The second exploration well, called 'SNE-1' is planned to be drilled after operations on FAN-1 are complete and will be located on the Shelf Edge Prospect in 1,100m of water. This dual objective prospect targets stacked Cretaceous clastics and a deeper target of karstified and fractured Lower Cretaceous shelf carbonates. The two prospect targets are estimated by Cairn to have a gross mean unrisks prospective resource of 182 mmbbls and 256 mmbbls respectively. There are several other shelf edge anomalies that provide follow-up potential in the success case.

#### ESIA, Senegal

In November 2013, Cairn presented the findings of its ESIA to the National Technical Committee in Senegal as part of the process to seek approval to drill.



Cairn estimates the block-wide "Yet to Find" gross unrisks prospective resource is currently more than 3 bn boe.

#### Mauritania

Interpretation and mapping of the 3,500km<sup>2</sup> 3D seismic on block C19 offshore Mauritania, which Cairn farmed into in H2 2013 with Chariot Oil and Gas, is ongoing.

#### Ireland

The Blackford Dolphin drilling rig is currently undergoing preparations in readiness for the proposed Spanish Point appraisal/exploration well on Frontier Exploration Licence (FEL) 2/04 offshore West of Republic of Ireland, due to commence in Q2/Q3 2014 (Cairn 38% WI, Operator). Meanwhile, contracts for support services are progressing and the approval process, including environmental assessments, is underway.

Tenders have been submitted and planning is underway for a 500km<sup>2</sup> 3D seismic survey to begin in Q2 2014 on acreage adjacent to the Spanish Point discovery on exploration licence FEL 1/14 (Cairn 38% WI, Operator).

#### Greenland

Cairn remains encouraged by the opportunity in the Pitu exploration block (Cairn 56.875% WI, Operator), with combined prospects within the 3D area confirming a potential multi-billion boe prospective resource, and is targeting a drilling decision in 2015. The mapping and evaluation of the 3D seismic on Pitu has identified a number of prospects.

#### Ilulissat Activity Park, Greenland

In 2011 Cairn established a Community Development fund in Greenland to support local projects including the building of this activity park in Ilulissat.



## Operational Review Continued

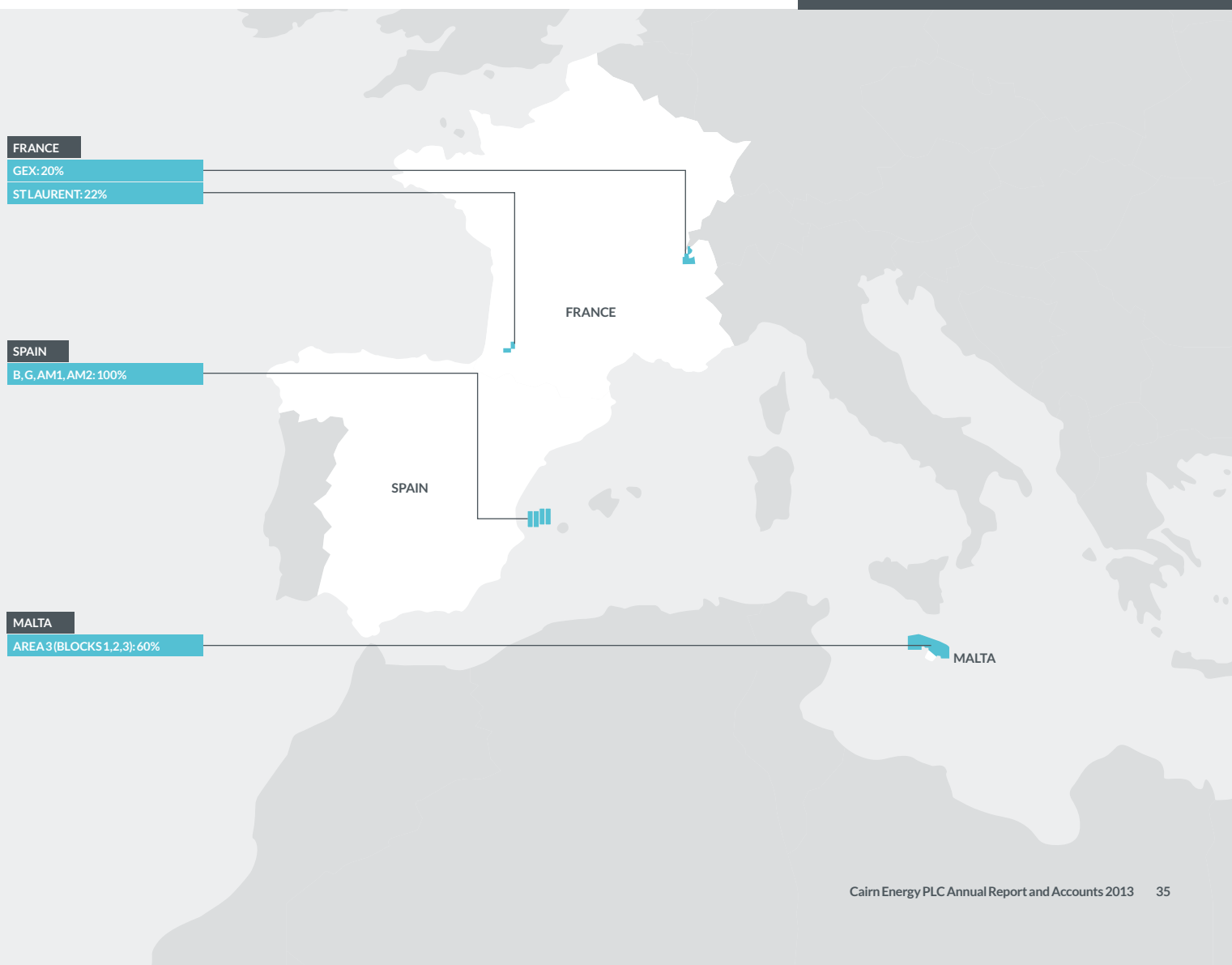
### Mediterranean

#### Frontier Basin Exploration – Mediterranean

Applications for further acreage offshore Spain (in the Gulf of Lion off the North East coast) have been submitted (Cairn 100% WI). Cairn holds licences of approximately 3,175km<sup>2</sup> in the Valencia Basin, offshore Spain and is in the early stages of its exploration programme. The authorisation for acquiring potential 3D seismic is underway.

Cairn (60% WI, Operator) has an Exploration Study Agreement (ESA) over Area 3 – Blocks 1, 2 and 3 offshore Malta. Cairn with its JV partner, Mediterranean Oil and Gas Plc, are currently mobilising to acquire approximately 1,500km of broadband 2D seismic.

#### Mediterranean



## Operational Review Continued

### UK and Norwegian North Sea

#### Mature Basin Exploration and Development – UK and Norwegian North Sea

Work is continuing on the Kraken development targeting first oil in H2 2016/H1 2017 with EnQuest as operator. Following the Kraken FDP approval, 30 mmbbl were booked as Proven plus Probable (2P) Reserves at 31 December 2013 on a net working interest basis. The detailed locations for the initial development wells from the first two drill centres (DC1 and DC2) are being finalised. BUMI are currently carrying out detailed engineering of the FPSO and work on christmas trees, templates and manifolds is progressing with first drilling templates expected later this year prior to drilling starting in H1 2015.

Considerable progress has been achieved on the Premier-operated Catcher area project since the development concept (a subsea tie-back of the Catcher, Varadero and Burgman fields to a FPSO) was agreed in December 2012. Reservoir modelling has been completed and well locations and sequencing have also been optimised. It is envisaged that development drilling will commence in 2015 and continue beyond first oil. Subsea FEED for the Catcher area project has also been completed. A draft FDP has been submitted to DECC, initiating the process to target project sanction by the operator in Q2 2014. More details on Catcher and its impairment are in the Financial Review. Gross 2C resources under the initial development scheme are 96 mmbbl although the development scheme makes provision for the tie-back of additional discoveries.

Following the results from the second Skarfjell appraisal well, which successfully delineated the field, the partners are now examining possible development concepts for Skarfjell for both oil and gas, together with undeveloped fields in the surrounding area.

Cairn has built a strong exploration position in the UK and Norway through a combination of acquisitions, farm-ins and licence rounds, most recently boosting its presence in the Quadrant 35 area in Norway, around the Skarfjell field.

Two firm non-operated exploration wells are currently planned to be drilled in the UK sector in 2014 and one in 2015:

- Aragon (UK Continental Shelf (UKCS), MPX operator during exploration phase, Cairn 30% WI and has agreed to acquire a further 2.5% WI from MPX) due to commence Q2 2014
- West of Kraken (UKCS, EnQuest operator, Cairn 25% WI) due to commence Q3 2014
- Tulla (UKCS, TAQA operator, Cairn 50% WI) due to commence Q1 2015

The wells planned for 2014 are targeting 13 mmbbl mean net risked resources (37 mmbbl mean net unrisked resources).

In Q1 2014, Cairn was awarded interests in all three licences applied for in the Norwegian Awards in Predefined Areas (APA) licence round and is currently reviewing this acreage, with a view to making drilling decisions over the forthcoming years.

Cairn presently holds interests in a total of 36 North Sea licences and is actively maturing new near term drilling opportunities from this acreage portfolio. The Group will also participate in the recently announced 28th UK Licensing Round.

#### Health and Safety

In all our activities, the Group is focused on seeking operational excellence. Given our focus on safety, we were concerned that following the start of operations offshore Morocco in 2013, two LTIs occurred. A thorough review has been undertaken to ensure any lessons learnt are captured from these incidents and to improve our forward operational safety performance.

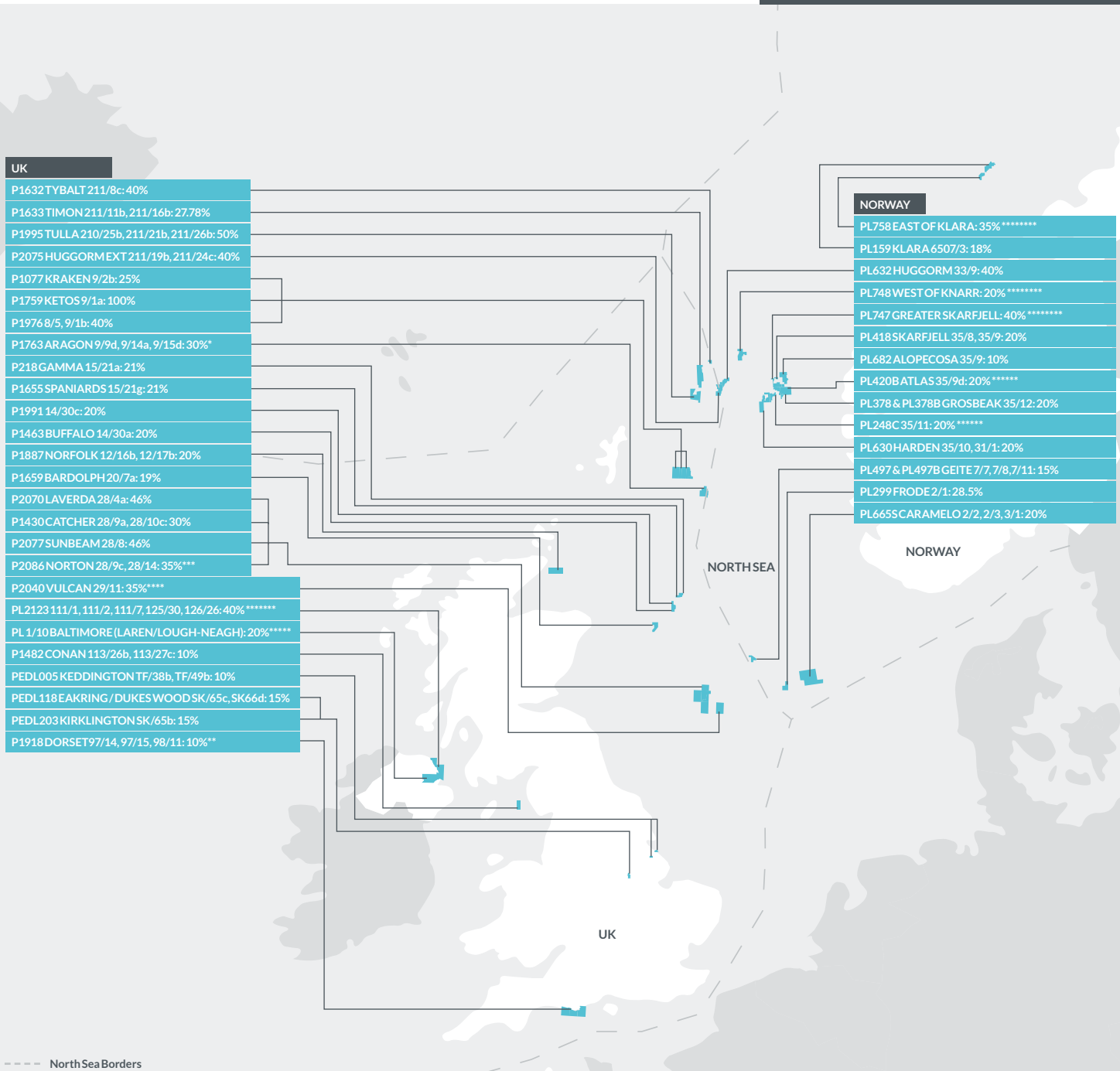
#### Skarfjell

Cairn has a 20% non-operated WI in the Skarfjell licence in the Norwegian North Sea. Discovered in 2012 Cairn participated in the drilling of two appraisal wells, with operator Wintershall Norge AS, in 2013.



In Q1 2014, Cairn was awarded interests in all three licences applied for in the Norwegian APA licence round and is currently reviewing this acreage, with a view to making drilling decisions over the forthcoming years.

UK and Norwegian North Sea



--- North Sea Borders

\* Cairn has agreed to acquire a 2.5% working interest in Licence P1763 on the United Kingdom Continental Shelf from MPX.  
 \*\* Cairn completed the transfer of this 10% interest in P1918 to InfraStrata on 28 February 2014.  
 \*\*\* Cairn has agreed to transfer a 25% of its working interest in UKCS Licence P2086 to Statoil, this is subject to partner and government approval.  
 \*\*\*\* Cairn has agreed to transfer a 25% of its working interest in UKCS Licence P2040 to Statoil, this is subject to partner and government approval.  
 \*\*\*\*\* Cairn has entered into an agreement to transfer this 20% interest in PL1/10 to InfraStrata, this is subject to government approval.  
 \*\*\*\*\* Cairn has agreed to acquire 20% working interest from Statoil, this is subject to partner and government approval.  
 \*\*\*\*\* Cairn has reached an agreement to transfer 40% working interest and operatorship to InfraStrata, this is subject to government approval.  
 \*\*\*\*\* Cairn has successfully received three awards from three applications in the 2013 APA licensing rounds in the Norwegian North Sea.

## Financial Review

Jann Brown

The existing portfolio provides many opportunities and we are looking closely at the allocation of capital for the programme beyond 2014, which will be guided by three core principles:

- creating value through exploration;
- maintaining a balanced portfolio, with a strong operating cash flow in the future; and
- capital discipline.

Cajun Express drilling unit, offshore Morocco



## Overview

The most significant event occurred post the Balance Sheet date, when, in January 2014, Cairn received a request from the Indian Income Tax Department for information relating to a group reorganisation completed in 2006.

This reorganisation was compliant with tax legislation in place at the time in each relevant jurisdiction, including India.

The Indian Income Tax Department has cited legislation introduced in 2012 as the reason for these enquiries.

While this information request is being dealt with, Cairn is unable to access the value of its shareholding in CIL (US\$1bn at the Balance Sheet date), either through disposal or future dividend income. As the restriction was not effective at the year end, no adjustment is made to the fair value reflected in the Group's 31 December 2013 Balance Sheet.

The current year's programme is funded fully from the cash on the Balance Sheet and we have moved quickly to review the capital allocation for 2015 and beyond and will keep this under review.

## Oil and gas assets, goodwill and related deferred tax liabilities

### Exploration and development additions and disposals

#### Frontier Exploration

#### Atlantic Margin – Africa

Cairn completed the first exploration well on the Fom Draa block, offshore Morocco in early January 2014. The Cajun Express rig subsequently moved to the Jubu Maritime block, also offshore Morocco to drill the JM-1 exploration well, which completed in March 2014. As neither well encountered commercial hydrocarbon reservoirs both were plugged and abandoned. Costs incurred to 31 December 2013 of US\$107m were expensed as unsuccessful exploration costs.

2013 movements in oil and gas assets, goodwill and related deferred tax liabilities are:

	Frontier exploration US\$m	Mature-Basin US\$m	Total US\$m
Asset carrying value	50	1,406	1,456
Deferred tax liabilities	–	(412)	(412)
<b>Net book value at 31 December 2012</b>	<b>50</b>	<b>994</b>	<b>1,044</b>
Exploration and development additions	200	204	404
Exploration and development disposals	–	(121)	(121)
Unsuccessful exploration costs	(132)	(81)	(213)
Impairment – exploration assets	–	(251)	(251)
Impairment – goodwill	–	(324)	(324)
Deferred tax credit	–	387	387
Foreign exchange differences	–	17	17
<b>Net book value at 31 December 2013</b>	<b>118</b>	<b>825</b>	<b>943</b>
Being:			
Asset carrying value	118	844	962
Net deferred tax liability	–	(19)	(19)

During 2013, Cairn completed the farm-in to three blocks offshore Senegal. Cairn subsequently agreed to farm-down a 25% WI to ConocoPhillips, which leaves the Group with a revised working interest of 40%. In the event of a commercial hydrocarbon discovery, ConocoPhillips will have the option to assume operatorship of the development project.

This farm-down completed on approval from the Government of Senegal in January 2014. Costs to date of US\$42m carried in the Balance Sheet include seismic and rig mobilisation costs. Following approval of the farm-down agreement subsequent to the year end, US\$17m of costs were recovered from ConocoPhillips in 2014.

Building on the Group's Atlantic Margin portfolio, Cairn farmed-in to the C19 block offshore Mauritania, paying US\$27m to the operator for seismic and other back costs.

#### Atlantic Margin – North Atlantic

Following approval by the Government of the Republic of Ireland, Cairn acquired a 38% WI as Operator of two licences offshore Republic of Ireland for back costs of US\$4m plus a promoted share of future exploration and appraisal costs, up to a maximum of two wells and a monetary cap. At the year end, the Group held US\$9m within exploration costs in the Balance Sheet in respect of these licences.

Building on the Group's Atlantic Margin portfolio, Cairn farmed-in to the C19 block offshore Mauritania, paying US\$27m to the operator for seismic and other back costs.



## Financial Review

### Continued

#### Mature Basin

##### UK and Norwegian North Sea

Cairn's interests in the UK and Norwegian North Sea were added following two corporate acquisitions in 2012. The portfolio at the year end consists of one development asset (Kraken), one near term development asset (Catcher), one recent exploration success currently under appraisal (Skarfjell) and several exploration prospects. During the year, the Group completed the disposal of its interests in the Mariner field.

The UK Kraken field (Cairn non-operated WI 25%) received DECC approval for the FDP in November 2013. Cairn is carried through the development phase costs up to a maximum between US\$150m-US\$240m dependent on reserve volumes with the current estimate at ~US\$200m. Total capitalised costs of Kraken in the Balance Sheet at 31 December 2013 were US\$300m.

On the Catcher asset (Cairn 30% non-operated WI), work has continued among partners to finalise the FDP.

Two successful appraisal wells were drilled on the Skarfjell discovery in the Norwegian North Sea during 2013 (Cairn 20% non-operated WI). Costs in the year relating to the two wells were US\$36m, with a related Norwegian tax refund receivable of US\$28m.

In December 2013, Cairn concluded the sale of its interest in the UK Mariner field, partially meeting one of the Group KPIs identified for the business of delivering a balanced sustainable business and preserving cash for investment. Though the disposal resulted in an accounting loss before tax of US\$25m, the sale of the asset frees the Group from ~US\$300m of future capital expenditure.

#### Impairment of exploration assets and goodwill

##### Catcher asset impairment

Revised economics, including resource downgrades and increased cost assumptions based on the latest operator estimates, resulted in impairment of the Catcher asset carrying value by US\$251m (see section 2.1 to the Financial Statements for further information). The impact of this impairment in the Income Statement is partially offset by a reduction in the provision for deferred tax of US\$152m that was initially recognised on acquisition of the assets in 2012.

Cairn's Balance Sheet is underpinned by its cash balances which are available to fund the current exploration programme and contribute towards future development projects.

#### Goodwill impairment

Following the corporate acquisitions in 2012, Cairn recognised goodwill of US\$474m, which was fully allocated to the North Sea operating segment. The goodwill largely arose from deferred tax liabilities that were recognised on the fair value of the assets acquired. Goodwill is tested annually for impairment by comparing the net carrying value of the goodwill, the North Sea exploration, appraisal and development assets and the deferred tax liabilities related to those assets to the fair value less costs of disposal of the underlying assets in the segment based on discounted cash flow models.

During 2013, there were two significant reductions to the deferred tax liabilities that are included within the UK and Norwegian North Sea cash generating unit. Firstly, the deferred tax credit on the Catcher asset impairment reduced the deferred tax liability by US\$152m. Secondly, the approval of the Kraken FDP triggered the recognition of heavy oil field allowances which eliminated the remaining deferred tax liability relating to UK North Sea assets and led to the recognition of a deferred tax asset of US\$59m. As a result, the increased carrying value of the cash generating unit was no longer supported by the fair

value less cost of disposal of the underlying assets, giving rise to a US\$324m impairment of goodwill.

#### Available-for-sale financial asset

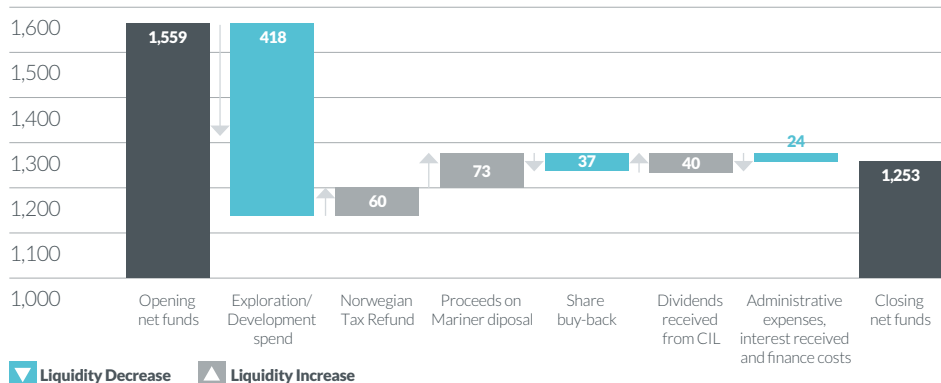
At the year end, Cairn's remaining ~10% holding in CIL was valued at ~US\$1.0 billion. Following an impairment of US\$268m at 30 June 2013, the value recovered by US\$72m in the second half. Under IFRS, there is no reversal in impairment in the Income Statement; the mark-to-market gains are instead reflected in Other Comprehensive Income.

As the restriction on further sales of the CIL shares did not exist at 31 December 2013, the holding in CIL is measured at the fair value on the Balance Sheet date reflecting the closing market value of US\$1.0bn. At the Group's next reporting date, the carrying value of the Group's financial assets will be assessed for impairment which will reflect the circumstances that exist at that time.

#### Cash and working capital

Cairn's Balance Sheet is underpinned by its cash balances which are available to fund the current exploration programme and contribute towards future development projects.

#### Movement in net funds over period (US\$m)



The Group's net funds (cash at bank less bank borrowings) were US\$1.25bn (31 December 2012: US\$1.56bn). This includes US\$100m of restricted cash.

Bank loans in Norway increased to US\$55m, up US\$26m year-on-year. These short term loans were drawn against future tax refunds receivable

in Norway on qualifying exploration expenditure incurred in the year. Subsequent to the year end, this loan was repaid in full and the facility cancelled.

### Results for the year

With no revenue currently recorded in the Income Statement, the Group reported a loss after tax for the year of US\$556m, analysed as follows:

		2013 US\$m	2012 US\$m
<b>Operational and administrative activities:</b>	Pre-award costs	(24)	(18)
	Unsuccessful exploration costs	(213)	(159)
	Administrative and other costs	(42)	(64)
	Related tax credits	86	122
		<b>(193)</b>	<b>(119)</b>
<b>Impairment and loss on sale of oil and gas assets:</b>	Impairment of exploration assets	(251)	(6)
	Impairment of goodwill	(324)	-
	Loss on sale of oil and gas assets	(25)	-
	Related tax credits	382	-
		<b>(218)</b>	<b>(6)</b>
<b>Finance income</b>	Net finance income	<b>48</b>	135
<b>Impairment and disposal of investment in CIL:</b>	Impairment	(268)	-
	Loss on sale	-	(82)
	Related tax credit	75	145
		<b>(193)</b>	<b>63</b>
<b>Total (loss)/profit after tax</b>		<b>(556)</b>	<b>73</b>

#### Operational and administrative expenses

Unsuccessful exploration costs of US\$213m include US\$107m relating to the Foum Draa and Jubu Maritime wells offshore Morocco, US\$81m relating to North Sea exploration wells drilled include Frode and Klara in the Norwegian North Sea and Timon in the UK North Sea and a further US\$25m written off assets elsewhere.

The fall in administration and other costs from US\$64m in 2012 to US\$42m for the current year reflect non-recurring expenses incurred acquiring and subsequently integrating the new subsidiaries in 2012 and Cairn's increased operational focus in 2013 with a greater portion of costs directly attributable to the Group's oil and gas assets. Controlling administrative cost levels remains a priority for the Group.

#### Finance income

Net finance income of US\$48m includes US\$40m of dividends received from CIL. Restructuring and capitalisation of inter-company group debt early in 2013 has eliminated much of Cairn's Income Statement exposure to foreign exchange movements.

The Group will continue to be entitled to dividend income declared by CIL going forward, however while the Indian Income Tax department restriction remains, dividend proceeds will be held in India.

#### Impairment of investment in Cairn India

The impairment recognised at 30 June 2013 of US\$268m includes mark-to-market deficits of US\$85m recognised in equity in prior years. The impairment is offset by related tax credits of US\$75m. Deferred tax of US\$70m remains provided at the year end on the assumption that a future sale of the remaining holding would be liable to Indian capital gains tax.

### Principal risks and uncertainties

In 2013, Cairn delivered on its priorities, creating a business offering multiple opportunities for growth within a coherent strategy and sustainable business model. This included frontier opportunities in the Atlantic Margin and Mediterranean basins and non-operated mature basin exploration and development projects in the North Sea. There are a number of risks linked to these opportunities which the Group is actively managing. Following year end, in January 2014, Cairn received a request from the Indian Income Tax Department to provide information in relation to the year ended 31 March 2007. The correspondence indicates that the request for information is in respect of amendments introduced in the 2012 Indian Finance Act which seek to tax prior year transactions under legislation applied retrospectively. While the interactions with the Indian Income Tax Department continue, Cairn has been restricted from selling its shares in CIL (valued at US\$1.0bn as at 31 December 2013). The Group will take whatever steps are necessary to protect its interests. The actions of the Indian Income Tax Department were taken without any prior discussion with Cairn and could not have been anticipated. It is therefore not possible at this stage to predict the course of any future action it might take.

The principal risks in relation to the Group's financial and operational performance are as follows:

- Lack of exploration success
- Continued restriction on the ability to sell CIL shareholding
- Health, safety, environmental and security incidents
- Kraken and Catcher development projects not executed on schedule and budget

### Outlook

Following the restriction imposed on our ability to access the value of our shareholding in CIL, we have moved quickly to ensure that all of our commitments in 2014 are fully covered. Capital allocation for future programmes will depend primarily on three things:

- the progress of Catcher through to project sanction;
- the conclusion of debt facilities for both Catcher and Kraken; and
- the results of our 2014 drilling programme.

The existing portfolio provides many opportunities and we are looking closely at the allocation of capital for the programme beyond 2014, which will be guided by three core principles:

- creating value through exploration;
- maintaining a balanced portfolio, with a strong operating cash flow in the future; and
- capital discipline.



**Jann Brown**

Managing Director & CFO  
17 March 2014

## How We Manage Risk

# Cairn has robust risk management processes to manage its business

### Managing Business Risks

Managing the risks to the business is essential to the long-term success and sustainability of the Group. There are inherent dangers associated with oil and gas exploration and development operations. Therefore, the Group's approach to risk is to actively seek out investment opportunities which provide the right balance of political, commercial and technical risks and manage these risks to an acceptable level. The Group's robust risk management framework is supported from the top down and is embedded throughout the organisation in all activities. It supports Cairn's entrepreneurial approach to business and this enhances the chances of safely engaging in successful business opportunities and delivering value to shareholders and other stakeholders.

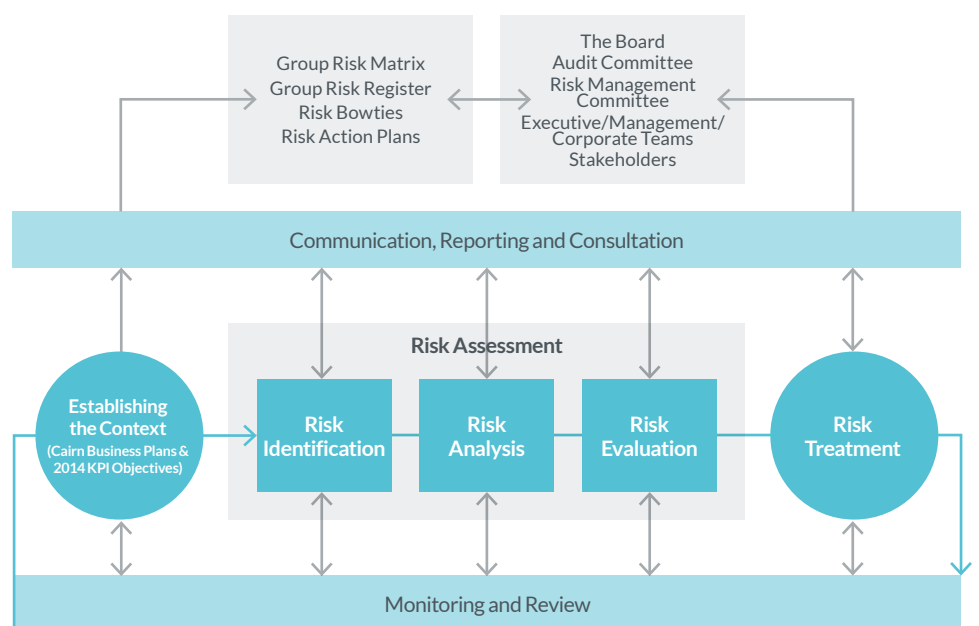
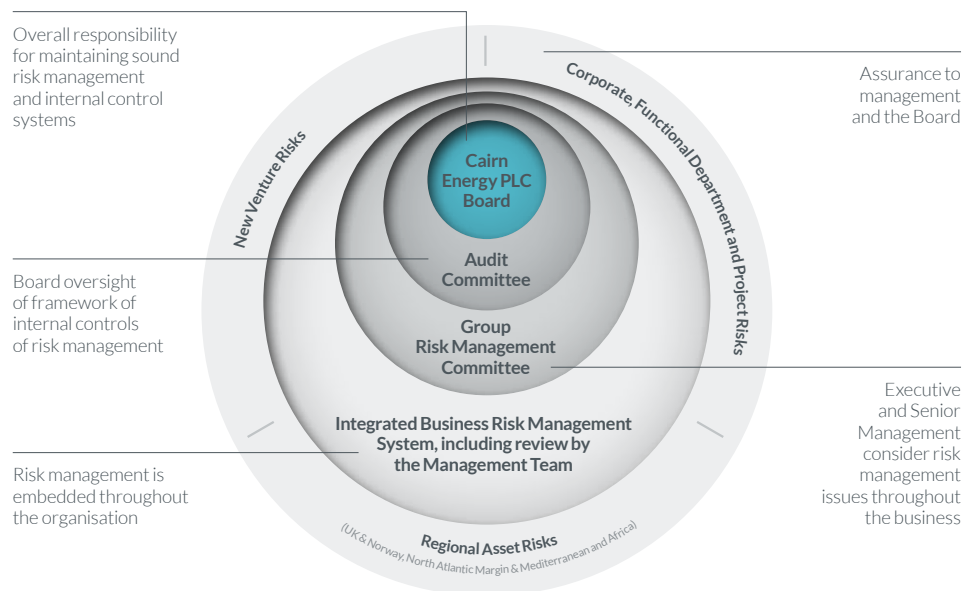
### Risk Identification and Management

Cairn's system for identifying and managing risks is embedded in its organisational structure, operations and management systems and accords with the risk management guidelines and principles set out in ISO 31000, the International Standard for Risk Management. Business risks across the Group are addressed in a systematic and consistent way through the risk management structure shown adjacent. This ensures the Board's assessment of risk is informed by risk factors and mitigating controls originating from and identified by the Group's regional assets, functional departments and in-country operations. The structure also allows the Board and various committees to assess and treat retained risks which fall outside the agreed tolerance levels of the Company Risk Appetite Statement.

Cairn has a robust risk management system in place to support risk identification, analysis, evaluation, treatment and ongoing monitoring of risks across the Group – shown in the diagram adjacent.

The risks associated with the delivery of the strategy, business plan, annual work programme and the associated mitigation measures and action plans are maintained in a series of risk registers at group, regional, asset, department and project levels. Assessment of the potential risks plays a key role in the evaluation of each new investment opportunity and all Investment Proposals require a risk register to be included.

Business Risk Management and Risk Management System at Cairn



The risks and mitigating actions from all of these sources are consolidated into the Group risk matrix and register which is regularly reviewed by the Executive, Management and Corporate Teams before being presented at the Group Risk Management Committee (GRMC), which is currently chaired by the Managing Director & CFO, Jann Brown. Risk management updates are provided at each Audit Committee and Board meeting.

### Responding to the Changing Risk Environment in 2013

The Group operates in a dynamic environment where the risks associated with internal and external developments are regularly reviewed to ensure their potential impact on the delivery of the Group's business strategy and objectives are assessed and mitigated. As part of steps to seek continual improvement of the Group Business Risk Management System (GBRMS), the following enhancements were made in 2013:

- Workshops were held with all areas of the business to undertake an assessment of the gross versus net risks and to map out the key controls currently in place to mitigate these risks. This process helped identify potential areas of control weakness requiring further action;
- The risk management approach to reporting risks to the GRMC was updated, with a particular focus on differentiating between the risks that are tolerated (with existing controls) and those that need to be treated (with additional actions); and
- Risk 'bowties' were completed for all high category risks to define interdependencies, pre and post controls, causes and consequences.

The internal audit service provider completed a review of the Group's approach to risk management in Q4 2013, which included benchmarking against other peer companies. The review confirmed that the current approach to risk management is effective and compares well to the peer group. The audit identified the following actions for implementation in 2014 to further improve risk management in Cairn:

- Further strengthen risk governance and oversight and refine the roles and responsibilities for risk management at senior levels and at the various risk management committees;
- Review and update the risk appetite statement to ensure it remains aligned to strategy and is clearly communicated and understood across the business;
- Increase the focus on the status of risk mitigations and monitoring the closure of actions; and
- Further embed the risk culture across the Group by including risk management responsibilities in induction programmes, performance appraisals and more regular training for appropriate staff.

## Principal Risks and Uncertainties

As described in the Financial Review, as the Group continues its strategy of targeting and realising value for stakeholders from exploration success, the principal risks and uncertainties facing the Group are as follows:

### Principal Risks and Uncertainties

#### Lack of exploration success

Once acreage has been secured, the challenge is to discover a hydrocarbon resource in commercial quantities. In 2014, operated wells are due to be drilled in Morocco, Senegal and the Republic of Ireland and four non-operated wells are also anticipated to be drilled in the UK and Norway. The Group continues to actively evaluate a number of potential new exploration investment opportunities for 2014 and further ahead which are all subject to extensive external and internal peer review.

#### Health, safety, environment and security incidents

Health, safety, environment and security (HSES) incidents can occur if potential risks are not properly identified and managed. Executing operations safely and securely is the Group's number one priority. To help mitigate HSES risks, a comprehensive CR Management System is embedded throughout the organisation which ensures all HSES risks are identified, evaluated and treated during project screening, planning and execution. In the unlikely event of an incident occurring, robust plans exist to ensure it is managed effectively.

#### Restriction on ability to sell CIL shareholding

In January 2014, Cairn received a request from the Indian Income Tax Department to provide information regarding a transaction which took place during the fiscal year ended 31 March 2007. The correspondence indicates that this enquiry stems from amendments introduced in the 2012 Indian Finance Act with retrospective effect which seek to tax prior year transactions. While the interactions with the Indian Income Tax Department continue, Cairn has been restricted from selling its shares in CIL (valued at US\$1.0bn as at 31 December 2013). The actions of the Indian Income Tax Department were taken without any prior discussion with Cairn and could not have been anticipated. It is therefore not possible at this stage to predict the course of any future action it might take. The Group will take whatever steps are necessary to protect its interests. This matter is addressed further in the Financial Review on page 39.

#### Kraken and Catcher development projects not executed on schedule and budget

The Kraken and Catcher development projects are part of the mature basin North Sea portfolio which provides balance to the frontier exploration programme as well as the future cash flow to fund exploration activity. Development projects of this nature can be susceptible to delays and budget increases for a variety of reasons and to mitigate against this, the Group works closely with the partners to support and/or influence key decisions. The Kraken FDP was submitted and received DECC approval in 2013 and the first draft of the Catcher FDP has been submitted to DECC by the operator.

# How We Manage Risk

Continued

## Principal Risks to the Group in 2013/14

In our 2012 Annual Report & Accounts, we presented the risks which we believed could adversely impact our business at the time. During 2013, we regularly reviewed these risks and the diagram (below) and table (adjacent) update these key risks, their potential impacts, the mitigation measures that we have in place and the KPI the risk impacts upon. The list is not exhaustive or set out in any order of priority and is likely to change at any time.



The closer to the centre of the circle the more significant the risk to the business.



### Look for this symbol

Throughout this section this symbol is used to code risk types.

# Strategic Risks



Risk Description	Impact	Mitigation	2013 Movement	2014 KPI Objective	Mature or Frontier
<b>Lack of exploration success</b>	<ul style="list-style-type: none"> <li>Loss of investor confidence</li> <li>Limited or no value creation</li> <li>Failure of the business</li> </ul>	<ul style="list-style-type: none"> <li>An active programme is in place for high-grading new areas through licence rounds, farm-ins and other transactions</li> <li>An inventory of prospects and leads has been developed that offer opportunities which provide a balance of geological and technical risks</li> <li>Highly competent team applying a thorough review process of prospects and development opportunities and a team of geoscientists with a track record of delivering exploration success</li> <li>Continue to seek out the right personnel who can add value, knowledge and experience to the Group</li> </ul>	This risk remains at the same level as last year. Cairn's multi-year, multi-well frontier exploration campaign has commenced with a series of wells along the Atlantic Margin. The Group's frontier operated exploration programme will target prospects in Morocco, Senegal and the Republic of Ireland, with a series of high-impact exploration opportunities in the region over the next year. Four non-operated wells are also anticipated to be drilled in the UK and Norway and one in the Cap Boujdour permit, Morocco. A number of potential follow up exploration prospects have also been identified.	Achieve exploration and appraisal success through discovery of commercial hydrocarbons in 2014	Mature and Frontier Exploration
<b>Kraken and Catcher development projects not executed on schedule and budget</b>	<ul style="list-style-type: none"> <li>Increased costs</li> <li>Delay in future cash flow</li> <li>Adverse influence on future Business Plan</li> </ul>	<ul style="list-style-type: none"> <li>Actively engage with all our JV partners early to establish good trusting, working relationships</li> <li>Actively participate in technical meetings to challenge, apply influence and/or support our partners to establish a cohesive joint venture view and ensure operational activity is executed in a safe and secure manner</li> <li>Work closely with the Kraken operator to monitor and review BUMI-Subsea, the FPSO contractor</li> </ul>	This risk has been added in 2013. The successful delivery of the Kraken and Catcher developments is fundamental to the future funding of exploration and therefore the Group continues to work closely with all JV partners to challenge, apply influence and/or support key decisions. The Kraken FDP was submitted and received DECC approval in 2013 and the first draft of the Catcher FDP has been submitted to DECC by the operator.	Successfully complete operated and non-operated 2014 work programmes	Mature Development
<b>Inability to identify or secure prospective acreage at a cost which can generate reasonable returns</b>	<ul style="list-style-type: none"> <li>Loss of investor confidence</li> <li>Loss of competitive edge</li> </ul>	<ul style="list-style-type: none"> <li>Exploration Director, with the support of the technical and commercial teams, continue to identify and review a number of prospects</li> <li>Experience and knowledge throughout the organisation in recognising prospective opportunities</li> </ul>	This risk remains unmoved. In 2013, Cairn successfully farmed-in to opportunities in Mauritania, Senegal, Morocco, the Republic of Ireland and the North Sea. The Group participated in the Norwegian APA 2013 licensing round and successfully received three awards from three applications. Looking ahead, the Group continues to identify and analyse potential prospective opportunities.	Mature high impact exploration prospects ready for drilling in 2015 or 2016	Mature and Frontier Exploration

## How We Manage Risk

Continued

# Health, Safety, Environment and Security Risks



Risk Description	Impact	Mitigation	2013 Movement	2014 KPI Objective	Mature or Frontier
<b>Health, safety, environment and security incidents (HSES)</b>	<ul style="list-style-type: none"> <li>- Serious injury or death</li> <li>- Environmental impacts</li> <li>- Loss of reputation</li> <li>- Regulatory penalties</li> </ul>	<ul style="list-style-type: none"> <li>- Effectively managing HSES risk exposures is the number one priority for the Board, Executive Team, Management Team and Corporate Team</li> <li>- HSE Leadership Team, under the Chair of the Managing Director &amp; CFO, Jann Brown, meets monthly to review and provide direction on HSES matters</li> <li>- CR Management System processes and procedures are embedded throughout the organisation and all potential health, safety, security, environment and societal impacts are proactively identified, evaluated and treated during project screening processes</li> <li>- Robust internal and external assurance and review processes covering the design and operation of producing facilities</li> <li>- Process in place for assessing an operator's operating and HSES capabilities, including undertaking JV audits to determine the level of oversight required</li> <li>- Emergency organisation procedures and equipment are maintained and regularly tested to ensure the Group is able to respond to an emergency quickly, safely and effectively</li> </ul>	<p>This risk has been moved to a higher category due to the increase in the intensity and volume of operations in 2013/14 in comparison to 2012. The Group continues to execute all projects with a focus on managing HSES exposures.</p>	<p>Deliver our activities with a strong focus on not hurting people or damaging the environment.</p> <p>Continue to enhance the Group's HSES culture, behaviours and approach</p>	Mature and Frontier Exploration

# Operational Risks



Risk Description	Impact	Mitigation	2013 Movement	2014 KPI Objective	Mature or Frontier
<b>Reliance on JV operators for asset performance</b>	<ul style="list-style-type: none"> <li>- Cost/schedule overruns</li> <li>- Poor performance of assets</li> <li>- HSE performance</li> </ul>	<ul style="list-style-type: none"> <li>- Actively engage with all JV partners early to establish good, trusting, working relationships</li> <li>- Actively participate in technical meetings to challenge, apply influence and/or support partners to establish a cohesive JV view</li> </ul>	<p>This risk has moved to a higher category due to the increase in the level of work being executed in a non-operator role. This includes the Kraken and Catcher development projects, interests in offshore North West Africa and non-operated exploration and appraisal in the UK and Norway.</p>	<p>Successfully complete operated and non-operated 2014 work programmes</p>	Mature and Frontier Exploration and Development
<b>Operated exploration work programmes not executed on schedule and budget</b>	<ul style="list-style-type: none"> <li>- Increased well costs</li> <li>- Incomplete well programme</li> </ul>	<ul style="list-style-type: none"> <li>- Comprehensive set of criteria that must be met before contracting and accepting any rig</li> <li>- Work very closely with the rig contractors to exert influence and impose our performance expectations</li> </ul>	<p>This risk has been added to reflect the schedule and cost pressures of the Group's current drilling campaign. The Group is currently contracted to the Cajun Express rig and the Blackford Dolphin rig.</p>	<p>Successfully complete operated and non-operated 2014 work programmes</p>	Frontier Exploration



# Financial Risks



Risk Description	Impact	Mitigation	2013 Movement	2014 KPI Objective	Mature or Frontier
<b>Restriction on ability to sell CIL shareholding</b>	<ul style="list-style-type: none"> <li>Outcome of Indian Income Tax Department enquiry</li> </ul>	<ul style="list-style-type: none"> <li>The Group will take whatever steps are necessary to protect its interests</li> </ul>	<p>This risk has been added in 2014. In January 2014, Cairn received a request from the Indian Income Tax Department to provide information in relation to the fiscal year ended 31 March 2007. The correspondence indicates that this enquiry stems from amendments introduced in the 2012 Indian Finance Act with retrospective effect which seek to tax prior year transactions. While the interactions with the Indian Income Tax Department continue, Cairn has been restricted from selling its shares in CIL (valued at US\$1.0bn as at 31 December 2013). The actions of the Indian Income Tax Department were taken without any prior discussion with Cairn and could not have been anticipated. It is therefore not possible at this stage to predict the course of any future action it might take. This matter is addressed further in the Financial Review.</p>	Retain balance sheet strength	N/A
<b>Potential tax liabilities relating to Indian Income Tax Department enquiry</b>	<ul style="list-style-type: none"> <li>Outcome of Indian Income Tax Department enquiry</li> </ul>	<ul style="list-style-type: none"> <li>The Group will take whatever steps are necessary to protect its interests</li> </ul>	<p>This risk has been added in 2014. In January 2014, Cairn received a request from the Indian Income Tax Department to provide information in relation to the fiscal year ended 31 March 2007. The correspondence indicates that this enquiry stems from amendments introduced in the 2012 Indian Finance Act with retrospective effect which seek to tax prior year transactions. While the interactions with the Indian Income Tax Department continue, Cairn has been restricted from selling its shares in CIL (valued at US\$1.0bn as at 31 December 2013). The actions of the Indian Income Tax Department were taken without any prior discussion with Cairn and could not have been anticipated. It is therefore not possible at this stage to predict the course of any future action it might take. This matter is addressed further in the Financial Review.</p>	Retain balance sheet strength	N/A
<b>Cost pressures in the industry</b>	<ul style="list-style-type: none"> <li>Sub-optimal investment decisions</li> <li>Increased costs</li> <li>Value erosion</li> </ul>	<ul style="list-style-type: none"> <li>Wide range of scenarios run to assess robustness of projects and development decisions</li> </ul>	<p>This risk has been added in 2013 to capture the industry wide cost pressures attached to exploration and development projects. The Group undertakes a robust commercial assessment of all exploration and development projects to ensure they are viable.</p>	Retain balance sheet strength	Mature and Frontier Exploration and Development
<b>Uncertainty in fiscal regimes</b>	<ul style="list-style-type: none"> <li>Loss of value</li> <li>Uncertain financial outcomes</li> </ul>	<ul style="list-style-type: none"> <li>Engage closely with regulators in all jurisdictions where the Group has activities</li> <li>Legal agreements in place to protect interests</li> <li>Seek appropriate legal and tax advice</li> </ul>	<p>This risk has increased in 2013/14 due to the enquiry from the Indian Income Tax Department to provide information in relation to the fiscal year ended 31 March 2007. The actions of the Indian Income Tax Department were taken without any prior discussion with Cairn and could not have been anticipated. It is therefore not possible at this stage to predict the course of any future action it might take. Elsewhere, the Group has assets in a number of different geographies and is potentially exposed to sudden or unplanned changes in tariffs or taxes.</p>	Retain balance sheet strength	Mature and Frontier Exploration and Development

## How We Manage Risk

Continued

# Reputational Risks



Risk Description	Impact	Mitigation	2013 Movement	2014 KPI Objective	Mature or Frontier
<b>Negative stakeholder reaction to our operations</b>	<ul style="list-style-type: none"> <li>- Reputational damage</li> <li>- Loss of investor confidence</li> <li>- Loss of Licence to Operate</li> </ul>	<ul style="list-style-type: none"> <li>- Asset level stakeholder management and communication plans have been developed</li> <li>- Proactively engage with key stakeholders at all levels to build strong relationships to understand possible impacts</li> <li>- Actively monitor steps being taken by regulators and industry through participation in industry bodies such as OGP and Oil &amp; Gas UK</li> </ul>	This risk has increased due to the increase in activity levels both as operator and non-operator. The Group now has assets in a number of different geographies, which has increased the number of stakeholders and, therefore, the potential for stakeholder opposition.	Deliver our activities with a strong focus on not hurting people or damaging the environment	Frontier Exploration
<b>Escalating discussions regarding the future of oil and gas exploration in the Arctic</b>	<ul style="list-style-type: none"> <li>- NGO pressures</li> <li>- Government and regulatory interest</li> </ul>	<ul style="list-style-type: none"> <li>- Established a comprehensive programme of stakeholder engagement with communities in Greenland</li> <li>- Established an active engagement programme with a variety of stakeholders in key areas, including politicians, other operators, environmental experts and journalists</li> </ul>	This risk remains unchanged. The Group is not planning to drill in the Arctic in 2014 and even though the level of commentary regarding Arctic oil and gas exploration appeared to increase during 2013, this did not directly affect Cairn. The Group is targeting a drilling decision in 2015.	Deliver our activities with a strong focus on not hurting people or damaging the environment	Frontier Exploration



Simon Thomson, CEO (centre) and Craig McGregor (right), drilling manager on the Cajun Express drilling unit, offshore Morocco

# Organisational Risks



Risk Description	Impact	Mitigation	2013 Movement	2014 KPI Objective	Mature or Frontier
<b>Staff recruitment and retention</b>	<ul style="list-style-type: none"> <li>Disruptions to business ambitions</li> <li>Loss of key knowledge and experience</li> </ul>	<ul style="list-style-type: none"> <li>Regional Directors and Departmental Heads agree resource requirements as part of the annual work programme and budget processes</li> <li>As an accredited Investor in People, we support continuous professional development through technical, professional, management and behavioural skills courses as well as mentoring and educational assistance schemes</li> <li>Succession planning is in place for all areas of the business</li> </ul>	This risk has decreased due to the extensive recruitment plan which was completed in 2013. Total headcount increased by 13.7% through new recruits; staff turnover was 4.66%. There has been a focus on getting the right people, with the right skills in order to be adequately resourced to successfully deliver the work programme.	Successfully complete operated and non-operated 2014 work programmes	Mature and Frontier Exploration and Development

## Case Study

# Managing Risk During Drilling Offshore Morocco

Before committing to an investment in any new country we carefully consider the risk associated with operating in that country through comprehensive due diligence by both ourselves and third party experts. This risk assessment process includes assessing the technical risk associated with drilling in the country as well as political and commercial risk.

In advance of submitting our drilling plans to the Moroccan National Oil Company (ONHYM), and consistently with how we approach drilling wherever we operate, we contracted several third party technical experts, including a nominated UK well examiner, to review our well designs and drilling plans and provide feedback. We also carried out an internal exercise to assess any risks associated with the rig whilst on location and in transit to the drilling sites. This Major Hazard Identification Exercise which was facilitated by Det Norske Veritas, a global provider of services for managing risk with expertise in oil and gas, involved key managers from Cairn including our Drilling and HSE Manager and contractors including Transocean, the rig provider, and Marex, specialist marine risk consultancy.

During the one day workshop, the team reviewed a series of scenarios and their possible causes and consequences, developing plans to avoid them as well as safeguards to manage them, should they occur.

Throughout the process of drilling, we continue to identify, monitor and treat any new or emerging risks through our risk management procedure.

Working Responsibly

Operating  
with integrity



Cairn

## Working Responsibly Mapping our priorities

# A robust process helps Cairn to identify the topics that matter most to the business and its stakeholders

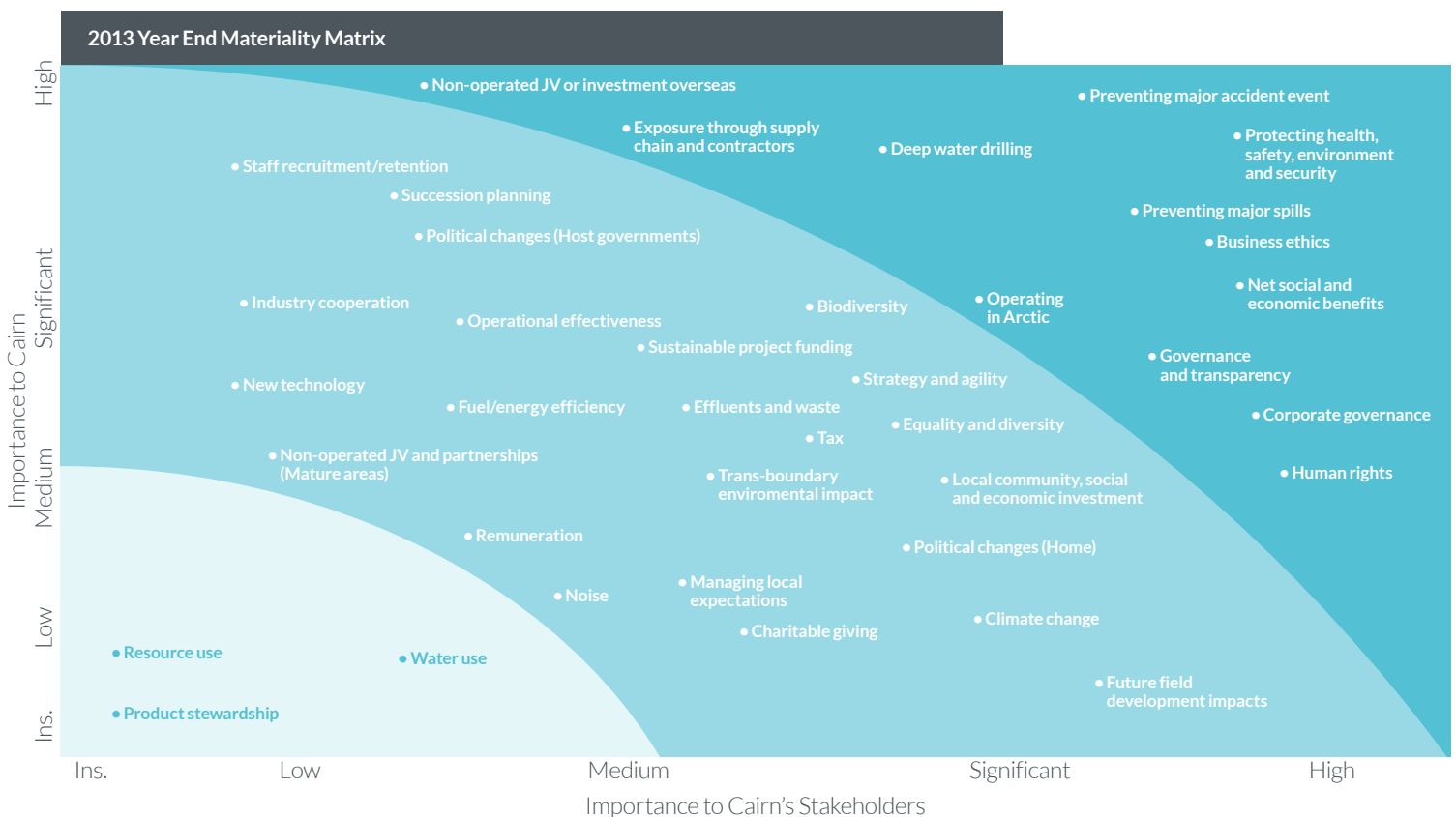
### Identifying Cairn's Most Important Topics

Cairn's strategy is to provide investors with exposure to material growth potential alongside mature basin development and pre-development assets, all against a backdrop of balance sheet strength. So we are continually looking at new business opportunities for which the associated impacts may vary. It is therefore essential that CR priorities are assessed at the start of reviewing the opportunity and at regular intervals thereafter to reflect this. Cairn uses a method called a 'materiality process' to identify the issues most important to the Company's stakeholders and business. The process is based on the AccountAbility AA1000APS model, an internationally recognised framework which involves establishing a range of relevant existing and emerging topics, which are then assessed and prioritised according to their significance to the business and to stakeholders.

In 2013, the prioritisation of Cairn's most important issues was carried out during a materiality workshop attended by senior management, facilitated by a third party and monitored by an external CR expert. The outcomes and their importance to Cairn and its stakeholders were mapped onto the materiality matrix shown below.

### Cairn's key issues inform CR strategy, objectives, risk management and how we communicate performance

Based on the materiality process at the end of 2013, the twelve areas identified to be most 'significant' (of high importance to our stakeholders and of high importance to Cairn) are described on the following pages. Further information on how we identify, assess and manage these CR topics as well as the majority of those identified as 'significant' is available in our summary CR report. More detail is also available on the Cairn website at [www.cairnenergy.com/responsibility](http://www.cairnenergy.com/responsibility).



# 1. Preventing a major accident event

## Overview

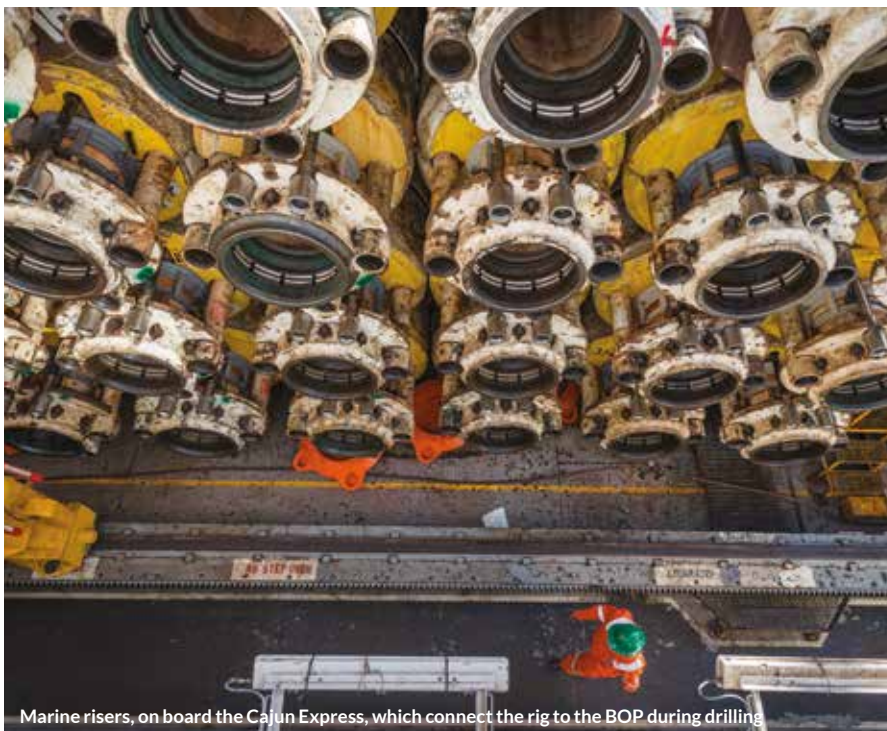
The prevention of any accident is a key focus of the oil and gas industry. At Cairn, rigorous procedures are followed to identify, assess and manage potential risks and impacts in line with the ALARP principle. Risks are managed and accidents prevented through safe design, review and assessment of equipment, defined operating procedures, training and performance monitoring. Contingency plans, equipment and trained staff are ready to respond in the unlikely event of a major accident. For more information on risk management please see page 44.

### HSE leadership

Cairn recognises that systems are not enough and that HSE leadership and culture are also critical. During 2013 therefore, we rolled out the new HSE Culture Framework and trained 79% of staff, as described in the 'How we nurture our

people' section of this report. During the year, the HSE Leadership Team has also been raising HSES awareness both internally and amongst those we work with by enhancing the contractor management process, including engaging with key contractors at a senior level. Further information about how we prevent major accidents is available in 'Responsible exploration' in our CR Summary Report.

In recognition of the importance given to HSE management and performance, the Remuneration Committee has assigned a 10% weighting in the Group 2014 KPIs to delivery of steps to further embed our HSE approach and an additional 5% weighting to delivery of safety and environmental performance targets.



Marine risers, on board the Cairn Express, which connect the rig to the BOP during drilling

# 2. Protecting health, safety, environment and security

## Overview

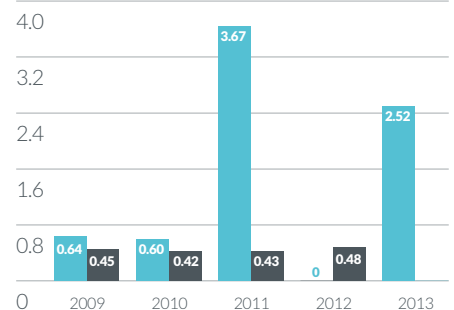
In Cairn's business, protecting the health, safety, security and wellbeing of people and the environment is emphasised in all day-to-day activities.

In early 2013, a series of workshops were held with senior management to refresh their knowledge of the CRMS. Particular focus was placed on their role in the delivery of operations that adhere to the Company's HSE standards and procedures. Cairn's safety performance over five years is illustrated in the graphs, and our performance explained, below. There have been no fatalities of Cairn staff or contractors during 2013 and for over five years.

### Health and safety

Over the last year, while there have been a number of marine surveys, Cairn's main operated activity has been the commencement of the drilling programme in Morocco in Q4 2013. Given the Company's focus on safety, Cairn was concerned that a number of incidents occurred during early shore base operations for the Morocco drilling programme. Many of these involved lifting operations. Together with the contractor companies we undertook detailed investigations of the potential causes of the incidents. One, which occurred at the Agadir shore base, resulted in a LTI when a contractor's employee trapped his finger

Lost Time Injury Frequency (LTIF)  
(Lost time injuries per million hours worked)



■ Cairn total for employees and contractors  
■ OGP Benchmark

between the tail and side gates of a truck. Lessons learned from this investigation include the importance of a 'One Task One Talk' culture that ensures that staff can concentrate on managing the risks for the task in hand rather than being overwhelmed by many instructions for a number of tasks.

As a result of our investigations, additional HSE resources were made available, procedures strengthened and specific training provided for local shore base workers, and this provision has been included in the preparations for our future shore base operations in Senegal and Republic of Ireland in 2014.

Regrettably, despite working closely with the rig operator, Transocean, ahead of the start of operations, there was also a LTI during the early stages of the drilling operations offshore Morocco. A member of the rig crew was injured whilst carrying out planned preventative maintenance to a lift. In this case, a detailed investigation led to the conclusion that improvements to risk assessment processes and work procedures were required. As a result, Transocean conducted a thorough review and developed a detailed corrective action plan. This included specific requirements relating to the maintenance system and improvements to comprehensive risk assessment, job procedures, training and communication. To address Cairn's safety concerns the CEO, Simon Thomson, visited

the Cajun Express with senior management from Transocean to re-emphasise the importance of learning from such incidents and minimising the chance of them reoccurring (see the case study on page 61).

### Security

Cairn recorded no security incidents during 2013 but recognises that with expansion into new countries, the risks to the security of our people and assets have increased. Following a tender process, we appointed Drum Cussac in March 2013 to provide external security advice and support to our activities. One particular area of concern was the security of business travellers to these new countries and, to mitigate this risk, an updated travel procedure was also issued in May 2013 requiring travel risk assessments to be completed and travel management plans issued for trips to locations deemed to have heightened health, safety or security risks.

### Environment

Governments award exploration and development opportunities knowing that our licence to operate and track record depends on delivering value creation for all stakeholders while taking rigorous care for the environment. Cairn takes a precautionary approach and avoids, wherever possible, negative impacts to the environment and biodiversity and looks to prevent or minimise emissions to air, land and water.

Our CRMS stipulates that environmental aspects must be managed at every stage of the exploration, drilling or development programme. Possible environmental impacts and their management are evaluated at every decision point in the five-stage PDP process. Environmental Impact Assessments (EIAs) completed by external experts are the main means by which these potential environmental impacts are determined and steps identified to minimise them. During 2013, we completed a total of three EIAs and a number of other studies including an Environmental Baseline survey and an Environmental Area Assessment ahead of our operated activities in 2013 and those being planned for 2014. These play a key role in gaining consents from governments to conduct seismic surveys and drilling operations. The permits to proceed with the drilling programme in Senegal and Republic of Ireland are subject to suitable applications and mitigation measures being in place. Cairn is working to meet these requirements in early 2014.

### Climate change

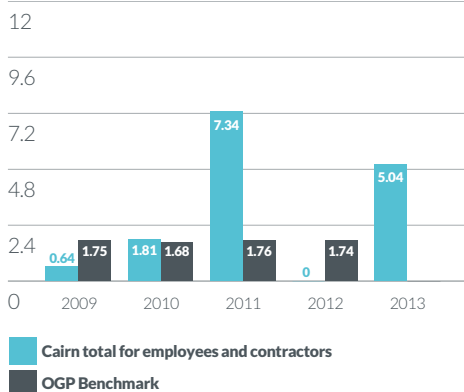
Energy is essential to social and economic progress. We recognise that we have a responsibility to take a precautionary approach to the causes of climate change and seek to minimise our own emissions of greenhouse gases. We reviewed our approach to climate change in 2013 in the light of external developments and updated our Business Principles to reflect our findings.

### Our approach

Our approach to climate change includes:

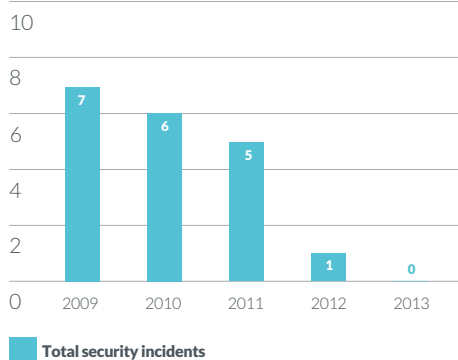
- Measuring, verifying and reporting on greenhouse gas emissions;
- Considering the risks and opportunities associated with climate change in our projects;
- Promoting efficient use of energy in our activities and wherever possible, establishing objectives and targets for energy efficiency;
- Integrating climate change considerations and potential costs into investment decisions;
- Engaging with stakeholders, for example, through participating in industry associations, on mitigation and adaptation to climate change; and
- Looking to contribute to local programmes that address environmental and social impacts of climate change within our sphere of control and reasonable influence.

### Total Recordable Injury Rate (TRIR) (Total recordable injuries per million hours worked)



Notes: OGP is the International Association of Oil and Gas Producers. Cairn TRIR and LTIIF statistics can be higher than the OGP benchmark after only one incident, or a small number of incidents, because our exploration activities often last for only a short time period so there are relatively few hours worked compared with ongoing production and other long term operations.

### Total security incidents (number)



## 2. Protecting health, safety, environment and security continued

We monitor and manage the greenhouse gases (GHGs) emitted during our activities. Our report covers Cairn's global operations from 1 January to 31 December each year. We disclose on an 'operational control' basis which means that we report on those operated assets over which we have control in terms of CR policies and practices during 2013.

### How we report

We disclose our GHG emissions in accordance with the GHG Protocol Corporate Accounting and Reporting Standard (revised edition) and use emission factors that are appropriate to Cairn for our scope 1, 2 and 3 GHG emissions. Scope 1 emissions arise from fuel combustion during offshore rig, marine vessel and aircraft operations and from the use of land-based vehicles (99.9%), and include the incineration of waste on marine vessels / rigs (<0.01%). Our scope 2 emissions derive from the use of electricity in our offices and shore bases. Scope 3 emissions are emitted during business travel, including by air and rail.

More information on our GHG accounting and reporting methodologies can be found on our website at [www.cairnenergy.com](http://www.cairnenergy.com)

### Emissions and level of activity

The graph below of our GHG emissions over five years show that they are heavily dependent on the level of operational activity in any given period. In 2010 and 2011 Cairn's major drilling programme offshore Greenland involved drilling eight wells and resulted in higher emissions than in 2012, when there was a limited amount of survey activity. Emissions rose in 2013 when we carried out surveys and commenced drilling offshore Morocco.

The varying levels of operational activity make it very difficult to identify a baseline and set targets for total GHG reduction over time.

Our GHG emissions intensity is calculated per thousand hours worked, as this provides a direct relationship with our activity. Factors such as the nature of the work in hand (i.e. drilling or survey), environmental conditions and distances between operations and logistic support bases have further significant influences on the intensity of GHG emissions.

### Case Study:

## An invitation to participate in Senegal

### Responding to stakeholders: Cairn's Environmental and Social Impact Assessment

As part of our application to carry out exploration drilling offshore Senegal, we undertook an Environmental and Social Impact Assessment (ESIA). The aim was to identify the potential impacts exploration drilling could have on the local population and habitats. A consultation process with local stakeholders was arranged in accordance with local and our own requirements. Possible effects on plants and animals in marine, coastal and wetland areas were assessed so that we could respond appropriately.

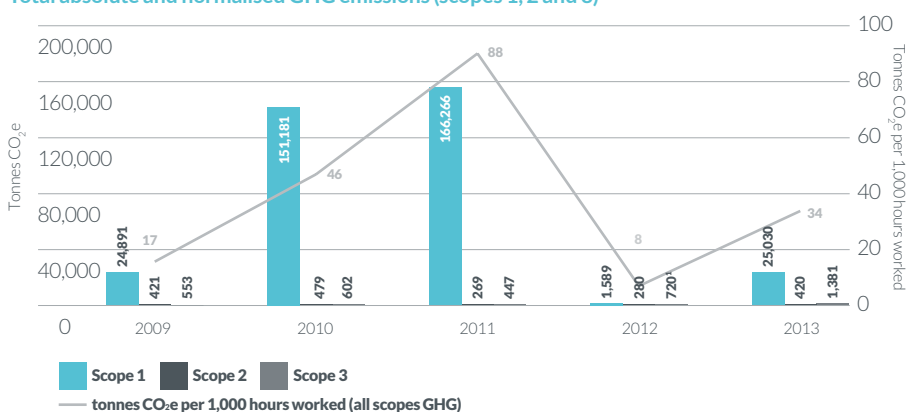
### Identifying stakeholders

To help identify stakeholders, we undertook in-country scouting trips, engaged with partners and consultants based in Senegal, used indigenous and corporate media monitors and internet sources and commissioned an external agency to carry out a stakeholder mapping exercise. Amongst others, Cairn held meetings with national and regional government bodies, industry associations, fishermen's organisations, public research centres, supply chain representatives and the NGOs WWF and Oceania. The engagement helped us to understand the representative groups' key concerns, consider appropriate responses and gauge the level of support for exploration drilling.

### Responsiveness

The reaction of the majority of stakeholders towards exploration during the research and consultation period was positive. However, a key issue raised was a concern over the potential impacts on fishing. The fishing sector in Senegal is vital both socially and economically, providing a major food source, 63,000 jobs and over 12% of the country's exports by value. Responding to this stakeholder concern, we were able to present mitigation measures for noise, vibration and vessel movement, and share study findings showing that exploration drilling activities have a low impact on marine fauna. Cairn was also able to address concerns about an oil spill by explaining our Oil Spill Prevention and Contingency Plan.

Total absolute and normalised GHG emissions (scopes 1, 2 and 3)



1 2012 air travel figures have been re-stated due to miscalculations being identified in the database.

Notes: We use emission factors from the API Compendium 2009 and also from EEMS 2008 (UK Environmental and Emissions Monitoring System for the Department of Energy and Climate Change (DECC)).

For calculating Scope 2 Emissions we use emission factors from the IEA (International Energy Agency) report 'CO<sub>2</sub> Emissions from Fuel Combustion Highlights' (2013 Edition).

For calculating air travel emissions we use journey type (domestic, short haul, long haul), seat class (economy, premium economy, business, first), distance, and an uplift factor. For some flights, where the seat class is not known, or data is not available broken into flight sectors with the associated seat class, applicable average emission factors may be used. For rail travel emissions we use rail type (national rail, eurostar) and distance. We use emission factors from '2012 Guidelines to Defra/DECC's GHG Conversion Factors for Company Reporting'.

For further details about our GHG emissions' calculations, please see our website.



### 3. Preventing major spills

#### Overview

A primary focus for the oil and gas industry and a material issue for Cairn is prevention of major accidents and hydrocarbon spills. Cairn actively supports the International Association of Oil & Gas Producers (IOGP) initiatives in these areas. Most notably, we are participating in the Joint Industry Project (JIP) for enhancing the industry's approach to oil spill prevention and response.

#### Risk assessment and response planning

One of the key outcomes from the JIP is a new approach to oil spill risk assessment and response planning which includes a structured and detailed analysis of oil spill risk, including development of potential spill scenarios, likelihood and consequence analysis, detailed modelling and development of credible response capability. Cairn has applied this new approach in developing its oil spill response plans for the Morocco, Senegal and Republic of Ireland offshore drilling programmes.

To complement this initiative we invested heavily in securing access to the Capping Stack System, the Subsea Incident Response Toolkit and the Global Dispersant Stockpile, all of which are managed by Oil Spill Response Limited (OSRL) – see the case study adjacent for more information. As shown in the tables below, there were no oil or fuel spills to the environment in 2013.

#### Total spills (number)

	2009	2010	2011	2012	2013
Oil	0	0	0	0	0
Fuel	1	1	1	0	0
Chemical	0	3	0	1	0
Waste	1	0	0	0	0
Other	0	0	2	0	0

#### Total spills (barrels)

	2009	2010	2011	2012	2013
Oil	0	0	0	0	0
Fuel	0.01	28.3	0.06	0	0
Chemical	0	56.85	0	2.20	0
Waste	0.06	0	0	0	0
Other	0	0	9.44	0	0

#### Case study:

### Oil spill prevention and contingency planning in Morocco



Offshore Cairn HSE adviser on board the Cajun Express drilling unit offshore Morocco

#### Meticulously designed and extensively examined wells are supported by comprehensive contingency plans

Oil spill prevention in Morocco, and all locations where Cairn operates, starts with well designs that exceed requirements for the expected characteristics of the geological formations to be encountered. Primary and secondary well control is built into the design as described on page 59.

#### Tertiary well control

In the very unlikely event that both primary and secondary well control barriers are breached, tertiary controls to regain well control and collect or disperse spilled oil are deployed. A series of scenarios are identified which define possible blow-out sizes irrespective of their probability. These are modelled to identify the 'worst credible case discharge' (WCCD). The WCCD is used for detailed oil spill modelling in conjunction with information gathered via the EIA to ensure that an appropriate oil spill contingency plan is developed. The plan is based on a widely used three tiered response system. Tier 1 is the response to a localised spill close to the operation. Equipment and personnel to respond to a localised spill are located on the rig and support vessels. Should the incident prove beyond this local capability or affect a larger area, resources for an enhanced response (Tier 2) are provided from the shore base. Tier 3 response resources are located internationally and can be mobilised through Cairn's membership of OSRL.

OSRL membership gives Cairn access to:

- A substantial supply of mechanical equipment including booms, skimmers and collection equipment for offshore and near shore response;
- Specialist fire-resistant booms for application of in-situ burning techniques;

- A supply of equipment and aircraft for the aerial application of dispersant to the water surface;
- The Sub-sea Incident Response Toolkit (SIRT), which enables dispersant to be applied at a sub-sea level, subject to government approval. This reduces the amount of oil reaching the surface or the shore, and increases its amenability to biodegradation;
- The Global Dispersant Stockpile, which provides a stockpile of dispersants with the widest worldwide approvals, large enough to provide for serious incidents; and
- The Capping Stack System (CSS), which can be deployed to shut-in the well and prevent oil from escaping to sea, at which point subsea dispersant is no longer needed.

In addition, Cairn has carried out training and practical exercises to ensure that priority actions are understood, equipment handling is mastered and appropriate logistics are in place.

In Morocco this specifically included:

- Oil Spill Contingency Plan and Emergency Response Procedure completed in August and October 2013 for the Foum Draa and Juby Maritime exploration wells;
- Oil Spill Contingency Plan Logistics workshop held in July 2013;
- Oil Spill Response certified training and practical training in equipment deployment provided by OSRL in July and October 2013;
- A series of desk-top exercises and focused training sessions in Q4 2013; and
- An emergency response real-time exercise – carried out in October 2013.

## 4. Business ethics

### Overview

Cairn's ability to secure licences and deliver operations effectively depends on robust business ethics and transparent relationships with governments, communities, partners and suppliers globally.

#### Zero tolerance for bribery and corruption

Cairn operates with integrity and has a zero tolerance approach to bribery and corruption. Country and Group level anti-bribery and corruption risk screening forms an integral part of the decision making process when entering new countries or negotiating with potential partners and major suppliers. If concerns arise, a third party anti-bribery and corruption review is undertaken. The purpose of this research and assessment is to establish whether potential issues should result in Cairn declining the opportunity or, if concerns are identified, whether they are manageable. The outcome of the anti-bribery and corruption assessments is included in the investment proposals. While this is a legal requirement, we believe it is also critical to our reputation as a well run business.

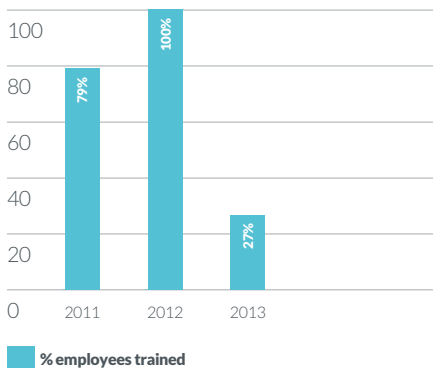
Activities during 2013 to enhance our approach to anti-bribery and corruption included:

- Conducting an external review of the anti-bribery and corruption practices employed on several transactions. This led to enhancements to our approach to assessing potential business partners, which were rolled out to senior management through a workshop run by an external expert;
- Reviewing supply chain anti-bribery and corruption practices with those responsible for tendering and evaluating bids for services; and
- Working with Good Corporation to put in place local anti-bribery and corruption procedures for use in Senegal.

Further information about our approach to business ethics can be found in our CR report in 'Ethical business practices'.

As shown in the graph below, all staff were trained in our updated anti-corruption policies and procedures when they were rolled out in 2012. In 2013 new staff were trained.

Employees trained in Cairn's anti-corruption policies and procedures (%)



Note: All Cairn employees have been trained in Cairn's anti-corruption policies and procedures. These are the figures for employees who received training in the reporting year.

## 5. Net social and economic benefit

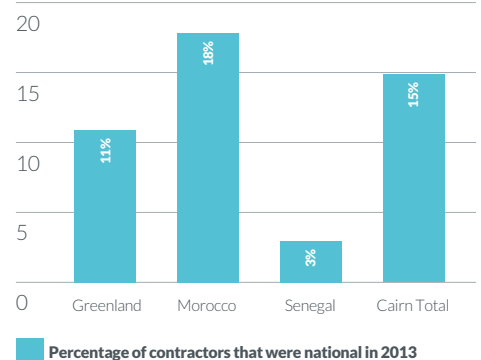
### Overview

In delivering our strategy we regularly operate in countries with no or relatively little oil and gas activity. We use a range of environmental, social and human rights assessments and baseline surveys to assess the potential effects of operations, tailoring them to meet government requirements. ESAs and social baseline studies are designed as participatory processes in which the research and discussion often include environmental issues, employment and livelihoods, economy, local business participation, education and training, community health, infrastructure, culture and heritage.

#### Using local suppliers

Our activities such as surveying and drilling in the exploration phase tend to be short term and temporary with future activity dependent on success. As such, the Company's procurement policy is an important opportunity to create social and economic benefit for host communities during these activities; however, these can be limited in exploration. Cairn encourages the use of local suppliers wherever the right expertise is available, or can be developed, without compromising the standards and principles required in the industry. We include local companies with the required competence in bid lists and we ask international contractors to consider the use of local sub-contractors where possible. The graphs below

Contractors that are national (%)



Percentage of contractors that were national in 2013

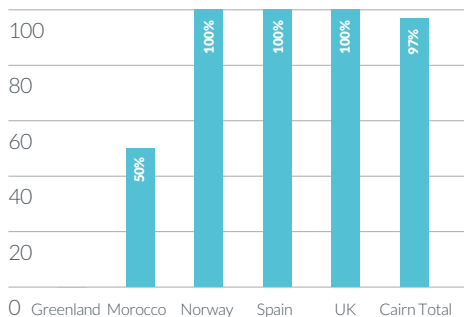
show that an average of 15% of contractors used by Cairn in 2013 were national and that the percentage of managers we hired from the local population in 2013 varied with the expertise available in the country of operation.

Cairn is committed to supporting skills development in local communities as well as using local labour. By organising seminars, sharing information with local enterprises and encouraging alliances between local contractors and international companies, the Company seeks to drive continuous improvement of local workforce skills, including skills that are transferable to industries other than the oil and gas sector.

In Morocco, Cairn is currently working with a number of local suppliers including the offshore base logistics agent, the port authority, the airport authority, helicopter operations handling services, waste management contractors, security services, accommodation provider, office services and a consultancy offering environmental and social impact assessments.

For more detail about how Cairn delivers net social and economic benefit, please see 'Engaging for the long term' and 'Partners in excellence' in our CR Summary Report, and our website at [www.cairnenergy.com/responsibility](http://www.cairnenergy.com/responsibility).

#### Managers hired from the local population (%)



Percentage managerial employees hired from the local population in 2013

#### Case Study:

### Giving people time

**In preparation for possible drilling, subject to approvals, Cairn invested in two rounds of stakeholder engagement in the Baffin Bay area of Greenland.**

Greenlandic regulations require oil companies to carry out a Social Impact Assessment (SIA) before undertaking exploration drilling.

The SIA must be a participatory process and Cairn followed up its SIA scoping consultation tour in 2012 with a consultation tour in the Baffin Bay area of North West Greenland regarding plans for potential future exploration drilling in the Pitu block. Three key findings emerged:

- A high proportion of the residents in this North Western part of Greenland are hunters and fishermen, and their central concern was the effect drilling could have on marine mammals;
- The second major discussion topic was the potential impact of an oil spill on the local environment, upon which they rely for their livelihoods; and

- Finally an underlying anxiety was identified about skills development in the area, as it is recognised that opportunities for young people are limited, which is also true of the small towns nearby.

#### Applying outcomes

The outcomes of this consultation will be included in Cairn's future SIA submission which will provide the basis for developing an Impact Benefit Agreement between the Company and the Government of Greenland in any future operations. In 2010 and 2011, Impact Benefit Agreements between Cairn and the Government of Greenland provided support to education and community development initiatives; training opportunities within operations; local business opportunities; and institutional capacity building.



In 2011 Cairn established a community development fund in Greenland to support local projects including the building of this activity park in Ilulissat

Greenlandic regulations require oil companies to carry out a Social Impact Assessment (SIA) before undertaking exploration drilling.

## 6. Governance and transparency

### Overview

Cairn's reputation for sound governance rests on making well informed and carefully considered decisions wherever we operate. When entering into a new country, our due diligence process starts with a thorough country risk assessment. We evaluate the commercial, legal, political, regulatory, health, safety, environmental, security and human rights issues and how best to manage these. In addition, technical and economic challenges and potential business partners involved in an investment opportunity are assessed.

### Engaging with stakeholders

The development and maintenance of good relationships with Cairn's stakeholders is essential to the success of the business. We maintain transparent and open channels to engage with stakeholders throughout the lifecycle of our business activities. We communicate regularly and transparently on economic, social, and environmental impact as well as changes in operations that may affect employees, customers, investors, partners, the environment, the community or other stakeholders.

We believe it is important to discuss issues affecting the business with government. All relations with public bodies are consistent with the Code of Business Ethics.

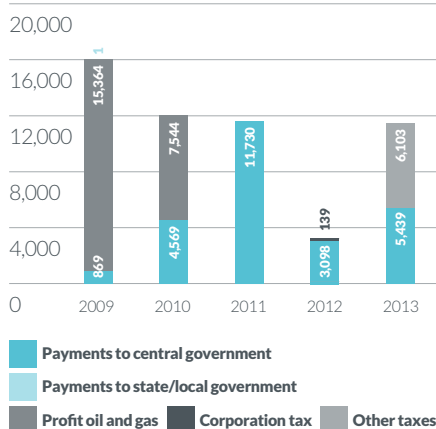
### Tax transparency

Transparency about tax contributions and other payments to Governments are two specific areas of interest to stakeholders. Cairn operates in various different territories with diverse tax obligations and requirements and the Group ensures that in every territory it is committed to complying fully with local tax rules and regulations. Additionally, the Group has adopted a policy to ensure that any tax planning activity is always aligned with the commercial reality. We have also been explicit since 2005 in our support for the

principles of the EITI, a multi-stakeholder initiative aimed at bringing transparency to payments to Governments from mineral or oil and gas extraction, and we have voluntarily disclosed payments to Governments in annual CR Reports. The Company strengthened and formalised its commitment to transparency of payments by becoming a Participating Company in the EITI in September 2013.

In January 2014, Cairn received a request from the Indian Income Tax Department to provide information in relation to the year ended 31 March 2007. The correspondence indicates that the enquiry stems from amendments introduced in the 2012 Indian Finance Act with retrospective effect which seek to tax prior year transactions. While the interactions with the Indian Income Tax Department continue, Cairn has been restricted from selling its shares in CIL (valued at US\$1.0bn as at 31 December 2013). This matter is addressed further in the Financial Review on pages 38 to 41.

Total payments to governments (US\$'000)



## 7. Corporate governance

### Overview

Cairn's licence to operate depends on transparent relationships with governments, communities, partners, shareholders and suppliers globally. Therefore commitment to high standards of corporate governance, and living by them, is critical.

As a Company, Cairn empowers management and teams to make decisions, yet has in place policies and procedures to escalate decisions to the Management Team, Executive Team or Board level as appropriate.

Risk management is a guiding theme for every decision we make and is comprehensively applied across the business. The Board sets the Group Risk Appetite and monitors the effectiveness of our risk management process.

### CR at Board level

The Board takes ultimate responsibility for Cairn's Group Business Principles and CR management, while the Management Team ensures that all work programmes are executed responsibly and that risk management is fully integrated. CR performance is a standing agenda item at 100% of Board meetings and CR considerations through the due diligence process are integrated into 100% of investment proposals submitted for a Board decision. In addition, key or emerging issues may merit particular consideration. In 2013, specific presentations were made to the Board regarding Cairn's approach to well control, an update on anti-bribery and corruption, governance, the OSRL Cap and Secure Services and the Cajun Express rig acceptance criteria. Findings from the investigation into the November 2013 lost time injury on the Cajun Express, the rig engaged for our operated well programme in Morocco, were shared. Senior management from Transocean, the Cajun Express contractor, presented their approach to managing HSE on the rig.

The HSE Leadership Team is chaired by Jann Brown, the Managing Director & CFO. It provides oversight on our approach and performance on all health, safety, environmental, security and human rights matters. Its members include a number of senior managers from across the business representing Executive, Corporate and operational responsibilities.

## 8. Human rights

### Overview

Cairn supports the principles in the United Nations Global Compact and applies a 'rights aware' approach to managing human rights aligned with the 'Guiding Principles on Business and Human Rights'. Respecting human rights is critical to the development and maintenance of effective relationships with the communities where we operate. Cairn's Human Rights procedures were updated in 2012, and in March 2013 we provided human rights training on these policies and procedures to 50% of CR and HR practitioners. This updated guidance aims to provide an effective approach to considering and managing human rights issues that may arise.

### Human rights due diligence

Cairn applies human rights screening as part of the due diligence process before entering a new country. This identifies and checks any human rights issues that arise through the investment proposal due diligence and establishes any risks requiring management by the Operator (be that Cairn or another) before proceeding. We also use the results of human rights screening assessments to decide whether ESAs require human rights elements. For example in 2013, human rights screening assessments were carried out to inform the ESAs completed for our drilling programmes in Morocco and Senegal. Prior to farming in to the Cap Boujdour permit we undertook a detailed review of Kosmos' Business Principles and the extensive analysis carried out by Kosmos and its advisers of the political, legal and human rights situation. Kosmos has signed a joint declaration of principles with Morocco's Office National des Hydrocarbures et des Mines (ONHYM) stating that exploration and production will comply with the principles of the Moroccan constitution and international standards, including the United Nations Charter. This requires local populations to be involved and consulted and stipulates that they will benefit equitably from exploration and production. Kosmos also stated its commitment to protecting the environment and complying with sustainable development requirements.



United Nations Global Compact

## 9. Deep-water drilling

### Overview

Cairn's reputation for responsible exploration in shallow or deep-water rests upon a rigorous approach to well design, well control and blow-out prevention in drilling operations. Cairn applies the same uncompromising well design approach, with an emphasis on prevention, to all categories of water, whether shallow or deep.

### Well design

Wells are designed to exceed the expected characteristics of the formations to be encountered and are assessed by an independent external expert well examiner who verifies that the design complies with the stated standards. The requirements of the Cairn Well Engineering and Construction (WEC) and CR Management Systems are translated into specific well designs, project plans and procedures. These are independently verified through a series of reviews from an expert, regulators and partners. An independent expert assesses critical equipment and systems before drilling can commence.

### Primary well control

In any well design, the primary well control barrier is provided by the weight of the drilling fluid column acting on the hole, or wellbore, created by the drill in the rock formation. This barrier is sustained by maintaining a wellbore fluid column with a higher pressure inside the wellbore than the fluid pressure in the pore spaces of the rock formation itself.

### Secondary well control

Secondary well control is provided by high specification blow-out preventers (BOPs). The BOP consists of a series of mechanical sealing devices called 'rams' with associated back-up systems. If the primary drilling fluid barrier is lost, the blow-out preventer rams and valves are operated to close the well, regain control and stop any fluid flow to the external environment. We recognise that in deep-water wells, the complexity of these secondary well control devices increases due to the need to rely upon dynamic positioning systems to keep the drilling rig on location.

### Tertiary well control

In the very rare event that both primary and secondary well control barriers are breached, tertiary controls to regain well control and collect or disperse spilled oil are deployed. These are described in the case study 'Oil spill prevention and contingency planning in Morocco' on page 55.

The Cajun Express drilling unit



## 10. Operating in the Arctic

### Overview

Exploration in the wider Arctic region, beyond the High Arctic, is not new and began onshore in the 1920s and offshore in the 1970s, with a total of 10,000 wells drilled to date. Choosing to realise the value of its potential resources, the Government of Greenland has awarded Cairn and other companies, including Shell, Statoil ASA, ConocoPhillips and Maersk, licences to explore, drill and potentially develop hydrocarbon resources in its territory for the benefit of its people.

### Responsibility

Cairn is conscious of its responsibility when operating in frontier areas such as the Arctic and is highly informed about the risks of drilling in all conditions and develops plans to mitigate risks accordingly.

Cairn's track record and experience demonstrate that we are well equipped for the task of exploring for oil and gas. We completed a range of operations in Greenland since 2008/9, including drilling eight offshore wells, without any serious injuries or significant environmental incidents such as spills. We contributed a total benefit of £186m to the Greenland economy between 2010 and 2012.

### Activities in 2013

In 2013, Cairn completed a site survey and consultation in preparation for future drilling activities. In addition, four wells from our previous drilling campaigns offshore Greenland were permanently plugged and abandoned. Activities in Greenland in 2013 provided valuable information for future exploration.

Our detailed research into the impact of drilling on the marine environment, described in 'Monitoring drilling impacts' in our CR Summary Report, has helped to fine-tune modelling used in the preparation of further environmental impact assessments. To date, our findings show that drilling impacts on the marine environment are not significant, particularly when compared to some other types of marine activity, for instance trawling.

## 11. Exposure through supply chain and contractors

### Overview

The majority of man-hours worked in connection with Cairn's business are contracted out at times of significant operational activity. As shown in the adjacent graph, the number of hours worked by contractors rises and falls in line with our level of activity, while the number worked by employees remains relatively stable over time.

Cairn's relationships with suppliers are crucial. Our focus is on selecting the right partners, communicating expectations, ensuring effective policies and management processes, monitoring performance and sharing lessons learned.

### Choosing partners carefully

Experience, competence and responsibility are some of the key considerations when it comes to choosing the right people to supply the provisions, equipment and services needed to help run Cairn's business. We apply a rigorous selection process in choosing contractors, including plotting potential partners on an HSE contractor risk evaluation matrix. This is embedded in our Contractor Management Procedures, updated in 2013, and built into the PDP.

### Focus on HSE

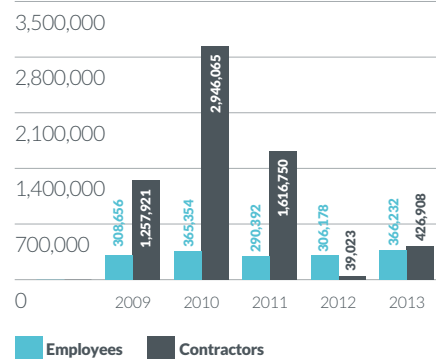
In a period of increasing activity in new countries, part of Cairn's HSE Leadership Team's drive has been to emphasise the importance of HSE considerations in 2013, and this has extended both to our activity and to contractor selection and management. During 2013 we put in place a Strategic Contractors Engagement Plan. We engaged pro-actively at the senior management level with 91% of the key contractors identified, and delivered a programme of briefings on HSE topics.

### Leading from the top

To ensure that key contractors take Cairn's HSE expectations on board and put safety first, a programme of senior management briefings to contractors on HSE topics has also been a priority in 2013. This has been supplemented by a senior management tour of activity, described in the adjacent case study.

For more information about how we work with contractors please read 'Partners in excellence' in our CR Summary Report.

### Total hours worked (hours)



## Case Study:

## Management visit to Cajun Express, offshore Morocco



### A senior management tour re-emphasised the importance of high HSE standards

Following a lost time injury onboard the Cajun Express during drilling of the first well offshore Morocco in November 2013, senior management, led by CEO Simon Thomson, visited the rig to re-emphasise the importance of learning from such incidents and promote practices to help minimise the chance of them occurring. The visit reflected management's commitment to ensuring Cairn's high standards of HSE management and performance are met and consistently maintained by contractors, one of the Group's 2013 CR objectives. Throughout the visit Simon reiterated the importance, above all else, of safety throughout our operations engaging with management and personnel involved in rig floor activities.

Simon was accompanied by a number of those responsible at Cairn for delivering a safe drilling campaign including the Director of Exploration, the Drilling Manager, the Morocco Asset Manager and the Morocco Country Manager. We also took this opportunity to invite our partner the Moroccan National Oil Company, ONHYM (Office National des Hydrocarbures et des Mines), to participate in the visit.

During the visit, safety was paramount. Two thorough safety briefings were conducted during the day: one before transferring by helicopter to the rig, conducted by Heliconia the helicopter contractor and one on arrival on the rig from Transocean personnel responsible for day-to-day management onboard the Cajun Express. This included encouraging the visitors to employ the 'Time Out' mechanism if they saw anything of concern at any time. 'Time out' is designed to transcend language and seniority barriers on board the rig so that at any time anyone can halt and question an activity by using the phrase 'Time Out'.

## 12. Non-operated joint venture and investment management overseas

### Overview

Due diligence is a key component of Cairn's approach to assessing investment opportunities. This involves carrying out our own assessments and checks on all aspects of CR and also commissioning third party and peer reviews where appropriate. Whether joint venture partners or suppliers are operating on Cairn's behalf, we review their CR approach and track record to ensure that they are meeting our criteria.

### Assessing CR in JV partners

Cairn counts both investments operated by the Company and joint ventures managed by business partners (i.e. operated and non-operated investments) in its portfolio of assets. Our acquisition and farm in activity in 2012/13 has given us access as non-operator to opportunities with other companies such as Statoil ASA, Premier Oil, Kosmos Energy, EnQuest and Chariot Oil & Gas. In addition to assessing partner principles and practices, we regularly assess the HSE standards of contractors selected by our operating partners. Cairn influences its partners by reviewing operator criteria for the HSE ranking of contractors, making HSE evaluations of development concepts and commenting on project risk matrices.

Cairn has a minority ~10% shareholding in CIL and as a consequence has limited opportunity to influence their strategy or approach to CR matters.

# Board of Directors

Executive Directors	Non-Executive Directors			
---------------------	-------------------------	--	--	--

## Simon Thomson

### Chief Executive (49)

Simon Thomson was appointed Chief Executive in July 2011. Prior to becoming Chief Executive, he had been Legal and Commercial Director since 2006. Simon originally joined Cairn in 1995 and holds an LLB (Hons) from Aberdeen University and a Diploma in Legal Practice from Glasgow University.

## Dr Mike Watts

### Deputy Chief Executive (58)

Mike Watts is Deputy CEO and has over 32 years' experience in the oil industry. He was formerly the CEO and Managing Director of the Amsterdam listed Holland Sea Search, which was acquired by Cairn in 1995, and where he was the architect of the South Asia strategy. Mike previously held senior technical and management roles with Premier, Burmah and Shell.

## Jann Brown

### Managing Director & CFO (58)

Jann Brown holds an MA from Edinburgh University and a diploma in accounting from Heriot-Watt University. Jann joined Cairn in 1998 after a career in the accountancy profession. Jann is Vice President of the Institute of Chartered Accountants of Scotland and a member of the Chartered Institute of Taxation.

## Sir Bill Gammell

### Non-Executive Chairman (61)

Sir Bill Gammell holds a BA in Economics and Accountancy from Stirling University and has over 30 years' experience in the international oil and gas industry. In 2006, he was awarded a knighthood for services to industry in Scotland.

## Todd Hunt

### Non-Executive Director (61)

Todd Hunt has 40 years' experience in the oil and gas industry. He is President and joint owner of Atropos Exploration Company and Atropos Production Company based in Dallas, Texas.

### Term of Office

Simon was appointed to the Board in November 2006 as Legal and Commercial Director and became Chief Executive in July 2011.

Mike was appointed to the Board in 1997 and became Deputy Chief Executive in March 2009.

Jann was appointed to the Board in November 2006 as Finance Director and became Managing Director & CFO in July 2011.

Sir Bill founded Cairn and was appointed to the Board as Chief Executive on its initial listing in 1988. In July 2011, he stood down from that role and became non-executive Chairman, following consultation with shareholders. He does not intend to seek re-election at the AGM.

Todd was appointed as an independent non-executive director in May 2003, however given his length of tenure he is no longer considered to be independent.

### Independent

Not applicable

Not applicable

Not applicable

Not applicable

No

### External Appointments

Simon is a non-executive director of Graham's The Family Dairy Limited.

Mike is a non-executive director of SOCO International plc.

Jann was appointed a non-executive director and chair of the Audit Committee of Troy Income & Growth Trust plc in January 2013. She is also a member of the 30% Executive Pipeline Action Group.

Sir Bill is a director of Glasgow 2014 Limited and was appointed chairman of Genius Foods Limited in March 2012.

Todd is President and joint owner of Atropos Exploration Company and Atropos Production Company.

### Committee Membership

Simon is a member of the Nomination Committee and attends meetings of the Remuneration Committee by invitation. He is also a member of the Group Risk Management Committee.

Mike is a member of the Group Risk Management Committee.

Jann is a member of the Governance Committee and attends meetings of the Audit Committee by invitation. She is also chair of the Group Risk Management Committee.

Sir Bill is chair of the Nomination Committee, and a member of the Governance Committee, and attends the Remuneration Committee by invitation.

Todd is a member of the Remuneration Committee, the Nomination Committee and the Governance Committee.





## Iain McLaren

### Non-Executive Director (63)

Iain McLaren has significant experience in the oil and gas sector. He is a Chartered Accountant and was formerly Senior Partner for KPMG in Scotland.

## Dr James Buckee

### Non-Executive Director (68)

Dr James Buckee (Jim Buckee) has more than 40 years' experience in the oil and gas industry, having gained extensive international experience with Shell, Burmah Oil and BP. He was appointed President of Talisman Energy Inc in 1991 and CEO in 1993 and held both posts until retiring from Talisman in 2007.

## M. Jacqueline Sheppard QC

### Non-Executive Director (58)

M. Jacqueline Sheppard QC (Jackie Sheppard) was previously Executive Vice President, Corporate and Legal at Talisman Energy Inc., a post she held for 15 years from 1993 to 2008. She holds a BA from the Memorial University of Newfoundland, BA and MA in Jurisprudence from Oxford University and LLB from McGill University. Jackie was admitted to the Law Society of Alberta (Canada) in 1982 and was appointed Queen's Counsel for the Province of Alberta in 2008.

## Alexander Berger

### Non-Executive Director (48)

Alexander Berger is Chief Executive Officer of Oranje-Nassau Energie B.V., a private Dutch exploration and production company based in Amsterdam. Alexander holds a Masters degree in Petroleum Engineering from Delft University and an MBA from Rotterdam School of Management.

## Ian Tyler

### Non-Executive Director (53)

Ian Tyler was Chief Executive of Balfour Beatty plc from 2005 until March 2013. During this time he took the company from being primarily a UK construction business, to a global infrastructure services business. Ian graduated with a first class degree in Commerce from Birmingham University. He then qualified as a Chartered Accountant with Arthur Andersen in 1987. Ian subsequently held a number of senior finance and operational positions within listed companies.

### Term of Office

Iain was appointed as an independent non-executive director in July 2008.

Jim was appointed as an independent non-executive director in January 2009. He does not intend to seek re-election at the AGM.

Jackie was appointed as an independent non-executive director in May 2010.

Alexander was appointed as an independent non-executive director in May 2010.

Ian was appointed as an independent non-executive director in June 2013. Ian will succeed Sir Bill as non-executive Chairman at the AGM.

### Independent

Yes

Yes

Yes

Yes

Yes

### External Appointments

Iain is chairman of Investors Capital Trust plc and a director of Baillie Gifford Shin Nippon plc, Scottish Enterprise and Mitra Energy Limited. He is also a past President of the Institute of Chartered Accountants of Scotland.

Jim is non-executive chairman of EnQuest PLC. He is also a director of Rodinia Oil Corp., PetroFrontier Corp., Black Swan Energy Inc., Magma Global Limited and KERN Partners Limited.

Jackie is a non-executive director and has been named as the successor chairperson of Emera Inc, a public Canada-based international energy generation, transportation and distribution company. She is also a director of the general partner of Pacific NorthWest LNG LP, which was formed for the purpose of constructing, owning and operating an LNG facility in British Columbia. She is a founder and director of two privately financed upstream oil and gas exploration companies.

Alexander is Chief Executive Officer of Oranje-Nassau Energie B.V.

Ian is non-executive chairman of Al Noor Hospitals Group plc, a non-executive director and chairman of the Audit Committee of Cable & Wireless Communications plc, a non-executive director of BAE Systems plc and non-executive Chairman of Bovis Homes Group PLC.

### Committee Membership

Iain is the chair of the Audit Committee and a member of the Nomination Committee and the Remuneration Committee.

Jim is a member of the Audit Committee and the Remuneration Committee.

Jackie is chair of both the Remuneration Committee and the Governance Committee.

Alexander is a member of the Audit Committee, the Nomination Committee and the Governance Committee.

Ian is a member of the Audit Committee and the Remuneration Committee.



# Directors' Report

## Directors' Report

The Directors of Cairn Energy PLC (registered in Scotland with Company Number SC226712) present their Annual Report for the year ended 31 December 2013 together with the audited consolidated financial statements of the Group and Company for the year. These will be laid before the shareholders at the AGM to be held on Thursday 15 May 2014.

## Results and Dividend

The Group made a loss after tax of US\$555.9m (2012 profit of US\$72.6m).

The Directors do not recommend the payment of a dividend for the year ended 31 December 2013.

Subsequent events that have occurred after the balance sheet date as at 31 December 2013 are included in Section 6 of the Notes to the Financial Statements.

## Strategic Review

Details of the Group's strategy and business model during the year and the information that fulfils the requirements of the Strategic Review can be found in the Strategic Review section on pages 2 to 61 of this document, which are deemed to form part of this report by reference.

Details of Cairn's offices and Cairn's advisers are given at the end of this report.

## Change of Control

All of the Company's share incentive plans contain provisions relating to a change of control and full details of these plans are provided in the Directors' Remuneration Report on pages 81 to 98. Generally, outstanding options and awards will vest and become exercisable on a change of control, subject to the satisfaction of performance conditions, if applicable, at that time.

On a change of control of the Company resulting in the termination of a director's employment, each of the Executive Directors is also entitled to compensation pursuant to their service contracts. Full details of the relevant provisions are set out in the Directors' Remuneration Report on page 89. There are no agreements providing for compensation to employees on a change of control.

There are no significant agreements to which the Company is a party that take effect, alter or terminate in the event of a change of control of the Company.

## Corporate Governance

The Company's Corporate Governance Statement is set out on pages 67 to 77 and is deemed to form part of this report by reference.

## Directors

The names and biographical details of the current Directors of the Company are given in the Board of Directors section on pages 62 and 63. The beneficial interests of the Directors in the ordinary shares of the Company are shown below:

	As at 31 December 2012	As at 31 December 2013	As at 17 March 2014
Simon Thomson	367,103	387,383	387,383
Dr Mike Watts	1,144,652	1,164,932	1,164,932
Jann Brown	284,088	295,550	295,550
Sir Bill Gammell	596,331	596,331	596,331
Todd Hunt	72,012	72,012	72,012
Iain McLaren	7,878	7,878	7,878
Dr James Buckee	34,636	37,788	37,788
Jackie Sheppard	0	0	0
Alexander Berger	0	10,979	16,498
Ian Tyler	0	0	0

Details of outstanding awards over ordinary shares in the Company held by the Directors (or any members of their families) are set out in the Directors' Remuneration Report on pages 81 to 98.

None of the Directors has a material interest in any contract, other than a service contract, with the Company or any of its subsidiary undertakings. Details of the Directors' service contracts are set out in the Directors' Remuneration Report on pages 81 to 98.

## Share Capital

The issued share capital of the Company is shown in Note 5.1 of the Notes to the Financial Statements. As at 17 March 2014, 578,189,219 ordinary shares of 231/169 pence each have been issued, are fully paid up and are quoted on the London Stock Exchange. The rights attaching to the ordinary shares are set out in the Company's Articles of Association. There are no special control rights in relation to the Company's shares and the Company is not aware of any agreements between holders of securities that may result in restrictions on the transfer of securities or on voting rights.

## Voting Rights

The following paragraph details the position in relation to voting rights set out in the Company's Articles of Association. However, the Company recognises that best practice is now to hold a poll on all shareholder resolutions. It is the Company's current practice, therefore, to hold a poll and it is committed to doing so going forward.

Subject to any special rights or restrictions attaching to any class of shares, at a general meeting or class meeting, on a show of hands, every member present in person and every duly appointed proxy entitled to vote shall have one vote and on a poll, every member present in person or by proxy and entitled to vote shall have one vote for every share held by him/her. In the case of joint holders of a share, the vote of the senior member who tenders a vote, whether in person or by proxy, shall be accepted to the exclusion of the votes of the other joint holders and for this purpose, seniority shall be determined by the order in which the names stand in the register of members in respect of the joint holding. Under the Companies Act 2006, members are entitled to appoint a proxy, who need not be a member of the Company, to exercise all or any of their rights to attend and to speak and vote on their behalf at a general meeting or class meeting. A member may appoint more than one proxy in relation to a general meeting or class meeting provided that each proxy is appointed to exercise the rights attached to a different share or shares held by that member. A corporation which is a member of the Company may authorise one or more individuals to act as its representative or representatives at any meeting of the Company, or at any separate meeting of the holders of any class of shares. A person so authorised shall be entitled to exercise the same powers on behalf of such corporation as the corporation could exercise if it were an individual member of the Company.

## Restrictions on Voting

No member shall, unless the directors of the Company otherwise determine, be entitled in respect of any share held by him/her to attend or vote at a general meeting of the Company either in person or by proxy if any call or other sum presently payable by him/her to the Company in respect of shares in the Company remains unpaid. Further, if a member has been served with a notice by the Company under the Companies Act 2006 requesting information concerning interests in shares and has failed in relation to any shares to provide the Company, within 14 days of the notice, with such information, the directors of the Company may determine that such member shall not be entitled in respect of such shares to attend or vote (either in person or by proxy) at any general meeting or at any separate general or class meeting of the holders of that class of shares. Proxy forms must be submitted not less than 48 hours (or such shorter time as the Board may determine) (excluding, at the Board's discretion, any part of any day that is not a working day) before the time appointed for the holding of the meeting or adjourned meeting or, in the case of a poll taken more than 48 hours after it was demanded, not less than 24 hours (or such shorter time as the Board may determine) before the time appointed for the taking of the poll at which it is to be used.

## Directors' Report

### Continued

#### Variation of Rights

Whenever the share capital of the Company is divided into different classes of shares, all or any of the special rights attached to any class may, subject to statute and unless otherwise expressly provided by the rights attached to the shares of that class, be varied or abrogated either with the consent in writing of the holders of not less than three-fourths in nominal value of the issued shares of that class or with the sanction of a special resolution passed at a separate general meeting of the holders of the shares of that class. At every such separate general meeting, the quorum shall be two persons holding or representing by proxy at least one-third in nominal value of the issued shares of the class. These provisions also apply to the variation or abrogation of the special rights attached to some only of the shares of any class as if the shares concerned and the remaining shares of such class formed separate classes. The rights attached to any class of shares shall, unless otherwise expressly provided by the terms of issue of such shares or the terms upon which such shares are for the time being held, be deemed not to be varied or abrogated by the creation or issue of further shares ranking *pari passu* with, or subsequent to, the first mentioned shares or by the purchase by the Company of its own shares.

#### Transfer of Shares

Subject to any procedures set out by the Directors in accordance with the Articles of Association, all transfers of shares shall be effected by instrument in writing in any usual or common form or in any other form acceptable to the Directors of the Company. The instrument of transfer shall be executed by, or on behalf of, the transferor and (except in the case of fully paid shares) by, or on behalf of, the transferee. The transferor shall be deemed to remain the holder of the shares concerned until the name of the transferee is entered in the register of members of the Company.

The Directors may, in their absolute discretion and without assigning any reason therefore refuse to register a transfer of any share which is not a fully paid share unless such share is listed on the Official List of the UK Listing Authority and traded on the London Stock Exchange's main market for listed securities. The Directors may also refuse to register a transfer of a share in uncertificated form where the Company is entitled to refuse (or is excepted from the requirement) under the Uncertificated Securities Regulations 2001 to register the transfer and they may refuse any such transfer in favour of more than four transferees. The Directors may also refuse to register any transfer of a share on which the Company has a lien.

The Directors may, in their absolute discretion and without assigning any reason therefore refuse to register a transfer of any share in certificated form unless the relevant instrument of transfer is in respect of only one class of share, is duly stamped or adjudged or certified as not chargeable to stamp duty, is lodged at the transfer office or at such other place as the directors may determine, is accompanied by the relevant share certificate(s) and such other evidence as the Directors may reasonably require to show the right of the transferor to make the transfer and is in favour of not more than four transferees jointly. If the Directors refuse to register a transfer, they shall, as soon as practicable and in any event within two months after the date on which the transfer was lodged with the Company (in the case of a share in certificated form) or the date on which the operator-instruction (as defined in the Uncertificated Securities Regulations 2001) was received by the Company (in the case of a share in uncertificated form) (or in either case such longer or shorter period (if any) as the Listing Rules may from time to time permit or require), send to the transferee notice of the refusal.

#### Major Interests in Share Capital

As at 31 December 2013 and 7 March 2014 (being the latest practicable date prior to the date of this report), the Company had received notification that shareholdings of 3% and over were as set out in the table below.

	As at 31 December 2013	% Share Capital	As at 7 March 2014	% Share Capital
MFS Investment Management	67,043,739	11.27	68,378,709	11.75
BlackRock	57,417,635	9.65	54,646,739	9.39
Franklin Templeton	26,107,583	4.39	27,830,128	4.78
Oppenheimer Funds	24,907,487	4.19	24,693,307	4.24
Aviva Investors	24,297,430	4.08	23,287,544	4
Legal & General Investment Management	23,205,272	3.90	19,335,873	3.32
Greenlight Capital	18,738,588	3.15	20,486,812	3.52
Merrill Lynch International Collateral a/c	-	-	21,449,809	3.69
Schroder Investment Management	-	-	19,211,833	3.3

#### Political Donations

No political donations were made and no political expenditure was incurred during the year.

#### Greenhouse Gas Emissions

Details of the Group's greenhouse gas emissions can be found in the Strategic Review section on pages 2 to 61 of this document, which are deemed to form part of this report by reference.

#### Financial Instruments

The financial risk management objectives and policies of the Company are detailed in Appendix 3 of the Financial Statements.

#### Acquisition of Own Shares

On 25 October 2013, with its focus on capital discipline, the Company initiated a share buy-back programme with a view to maximising shareholder value and optimising capital allocation. The Board considered that the share buy-back programme would maximise shareholder value by increasing the capital gain per share that would be expected in the event of a successful hydrocarbon discovery and that it would be in the best interests of shareholders generally. Therefore, the Company entered into an irrevocable and non-discretionary agreement with its brokers, Morgan Stanley and Jefferies, to repurchase on the Company's behalf and within certain pre-set parameters up to US\$300m of ordinary shares in the Company for cancellation. As at 31 December 2013, 8,217,615 ordinary shares have been repurchased and cancelled, which represents 1.38% of the called-up share capital of the Company as at that date. The nominal value of the shares purchased at that date is US\$181,466 and the aggregate amount of consideration paid by the Company for those shares is US\$36,293,629.63. The Board has decided to suspend the share buy-back programme as of 21 March 2014.

#### Appointment and Replacement of Directors

The Company's Articles of Association provide that directors can be appointed by the Company by ordinary resolution, or by the Board. The Nomination Committee makes recommendations to the Board on the appointment and replacement of directors. Further details of the rules governing the appointment and replacement of directors are set out in the Corporate Governance Statement on pages 67 to 77 and in the Company's Articles of Association.

## Directors' Report

Continued

### Directors' Indemnities

As permitted by the Company's Articles of Association, the Directors have the benefit of an indemnity which is a qualifying third party indemnity provision as defined in Section 234 of the Companies Act 2006. The indemnity was in force throughout the last financial year and is currently in force. The Company also purchased and maintained throughout the financial year Directors' and Officers' liability insurance in respect of itself and its Directors.

### Powers of the Directors

Subject to the Company's Articles of Association, UK legislation and any directions given by special resolution, the business of the Company is managed by the Board. The directors currently have powers both in relation to the issuing and buying back of the Company's shares and are seeking renewal of these powers at the forthcoming AGM.

### Articles of Association

Unless expressly specified to the contrary therein, the Company's Articles of Association may be amended by a special resolution of the Company's shareholders. The Company adopted new Articles of Association following approval of these by shareholders at the AGM held on 17 May 2012.

### Disclosure of Information to Auditors

The directors of the Company who held office at 31 December 2013 confirm that, as far as they are aware, there is no relevant audit information of which the Company's auditors are unaware. In making this confirmation, the directors have taken appropriate steps to make themselves aware of the relevant audit information and to establish that the Company's auditors are aware of this information.

### AGM 2014

The AGM of the Company will be held in the Castle Suite of The Caledonian, a Waldorf Astoria Hotel, Princes Street, Edinburgh EH1 2AB at 11 am (UK time) on Thursday, 15 May 2014. The resolutions to be proposed at the AGM are set out and fully explained in the Notice of AGM which has been posted to shareholders together with this Annual Report.

### Recommendation

The Board considers that all of the resolutions to be considered at the AGM are in the best interests of the Company and its shareholders as a whole and unanimously recommends that you vote in favour of all of the proposed resolutions, as they intend to do in respect of their own beneficial shareholdings.

By order of the Board

### Duncan Wood

Company Secretary  
17 March 2014

## Corporate Governance Statement

### Dear Shareholder

Maintaining and promoting high standards of corporate governance is central to my role as Chairman and I firmly believe that this is an essential prerequisite to delivering sustainable business performance. At Cairn, to deliver our strategy, our mandate is to operate with integrity at all times, recognising that in doing so the Company will maintain the trust of investors, governments, local communities, JV partners and other stakeholders.

The Cairn Board is committed to promoting high standards of corporate governance and understands that an effective, challenging and diverse Board is essential to enable the Company to deliver its strategy and shareholders' long-term interests, whilst also generating investor confidence that the business is conducting itself in a responsible manner. Further information on our strategy, business model and approach to operating responsibly can be found in the Strategic Review section of this Annual Report and in our Corporate Responsibility Report.

As announced on 3 March 2014, I will be retiring as non-executive Chairman with effect from the conclusion of the Company's AGM on 15 May 2014 and I am delighted that Ian Tyler will succeed me in this role. Ian was appointed as a non-executive director in June 2013 at which time the Board recognised his very extensive listed company governance experience both as a chairman and non-executive director. The Board has therefore agreed that Ian's qualifications and experience make him ideal for the role of non-executive Chairman following my retirement.



Sir Bill Gammell

I am proud of Cairn's many achievements during my tenure as founder, Chief Executive and subsequently non-executive Chairman of the Company. After 25 years on the Board, I am pleased to be leaving in the knowledge that the Board and the Company will remain in highly capable hands with Ian as Chairman and Simon at the helm as Chief Executive. Under this leadership, shareholders and other stakeholders can be confident that governance will continue to be a high priority for the Board.

Dr James Buckee will also retire in May 2014 and as such will not seek re-election at the Company's AGM on 15 May 2014. Dr Buckee has served as a non-executive director on the Cairn Board for five years I would like to take this opportunity to thank him for his valuable contribution to the Board during this time.

I recognise that, in last year's annual report, we stated that Todd Hunt would retire from the Board within the next 12 months. However, in light of my retirement and that of Dr Buckee at the AGM, Todd has agreed to offer himself for re-election as a non-executive director to allow the Board to retain his valuable technical skills and extensive knowledge of the business. As Todd has served on the Board for more than nine years he will, however, no longer be considered to be an independent non-executive director. The Board intends to appoint a new non-executive director with relevant technical skills and experience during 2014.

Following these changes, the composition of the Board will continue to comply with the provisions of the UK Corporate Governance Code (other than in respect of Mr Hunt's independence).

### Compliance with the UK Corporate Governance Code

As a company incorporated in the UK with a Premium Listing on the London Stock Exchange, we are required to report against the UK Corporate Governance Code (as published by the Financial Reporting Council and available on its website at [www.frc.org.uk](http://www.frc.org.uk)). Cairn is fully committed to achieving compliance with the principles and provisions set out in the Code.

The Board continually reviews the provisions of the UK Corporate Governance Code and has amended or enhanced the Company's governance framework to ensure that the Company complies with the Code (otherwise than as detailed in this statement). Set out below is a statement of how the Company applied the principles in sections A to E of the UK Corporate Governance Code for the year ended 31 December 2013. This statement reports compliance with the current version of the Code published in September 2012.

#### Executives/Non-Executives



#### Directors that are UK/International



# Corporate Governance Statement

## Continued

### The Board

Cairn's business is international in scope and carries political, commercial and technical risks. Accordingly, particular attention is paid to the composition and balance of the Board to ensure that it has wide experience of the industry sector and regulatory environment in which Cairn operates, and appropriate financial, operational and risk management skills. In each Board appointment, whether executive or non-executive, objectivity and integrity, as well as skills, experience, ability and diversity, assist the Board in its key functions, and are prerequisites for appointment. This also applies to appointments to senior management positions below Board level and to our succession planning.

The Board currently comprises the Chairman, three executive directors (the Chief Executive, the Deputy Chief Executive, and the Managing Director & CFO) and six independent non-executive directors. The current directors' biographies are on pages 62 and 63. Following the Board changes explained above, the Board will comprise the Chairman, three executive directors and four non-executive directors.

The Company considers periodic refreshment of the Board to be positive as it brings new thinking to the Company as well as ensuring that the Board's collective experiences equip it to meet its business needs as they evolve over time as well as its strategy for offering material growth within a balanced sustainable portfolio. The Board is also mindful that an appropriate balance between directors who can bring a new perspective and those who provide continuity is essential for a business like Cairn's.

Diversity is a key element of the Cairn Board, with emphasis placed not only on gender but also on nationality and experience. The Board currently demonstrates balance across all these elements with 20% female representation (one executive director and one non-executive director) and directors from the Netherlands, the USA and Canada, as well as the UK, adding international experience to the Board. The Board members' diverse range of experience and expertise covers not only a wealth of experience of operating in the oil and gas industry but also extensive technical, operational, financial, governance, legal and commercial expertise. Further information on diversity within Cairn is included in the report of the Nomination Committee on page 73 and in the Strategic Review section of this Annual Report.

### Division of Responsibilities between Chairman and Chief Executive

The Company has a clear division of responsibilities between the Chairman and the Chief Executive, which is set out in writing and agreed by the Board.

The Chairman's responsibilities include:

- the leadership and effective running of the Board;
- ensuring that the Board plays a full and constructive part in the determination and development of the Group's strategy;
- acting as guardian and facilitator of the Board's decision-making process;
- ensuring effective implementation of the Board's decisions; and
- ensuring open communications with shareholders and in particular, understanding their issues and concerns with regard to governance.

The Chief Executive's responsibilities include:

- managing the Group's business and proposing and developing the Company's strategy and overall commercial objectives in consultation with the Board;
- leading the Executive Team in implementing the decisions of the Board and its committees;
- ensuring the successful and efficient achievement of the Company's KPIs and objectives; and
- providing coherent leadership of the Company in representing the Company to its stakeholders including shareholders, financial institutions, employees, governments, the media, the wider community and the general public.

### Senior Independent Director

Iain McLaren continues to be Cairn's senior independent non-executive director. The main responsibilities of the senior independent non-executive director are as follows:

- to provide a sounding board for the Chairman and to serve as an intermediary with other directors when necessary;
- to be available to shareholders if they have concerns which contact through the normal channels of Chairman, Chief Executive or other executive directors has failed to resolve or for which such contact is inappropriate; and
- to meet with the other non-executive directors without the Chairman present, at least annually, in order to appraise the Chairman's performance.

### Re-election of Directors

In accordance with the UK Corporate Governance Code, all of the Company's directors are subject to annual re-election by shareholders. As such, each of the directors (with the exception of Sir Bill Gammell and Dr James Buckee) will seek re-election at the AGM to be held on 15 May 2014. Full biographical details of the current directors can be found in the Board of Directors section on pages 62 and 63.

### Performance Evaluation

The Board continually strives to improve its effectiveness and recognises that the performance evaluation process represents an annual opportunity to enhance overall Board effectiveness. In 2012, the Company conducted an externally facilitated Board evaluation for the first time and fully explained the process and outcomes for this in last year's Annual Report.

The 2012 evaluation resulted in some important recommendations for improving the Board's effectiveness and the table below sets out our progress in seeking to implement those recommendations.

Key actions	Progress
Board composition: the main priority should be to appoint up to two new non-executive directors.	Ian Tyler appointed as new independent non-executive director in June 2013 (and as a member of the Audit and Remuneration Committees).
Clearer role of the Chairman: it was recommended that the role of the Chairman should have increased focus on Board leadership, governance and effectiveness. It was also decided that the Corporate Governance and Nomination Committee should be split and that the Chairman should assume the role of chair of the Nomination Committee.	Sir Bill Gammell significantly increased his focus on these areas throughout 2013. In addition, he held meetings with investors in relation to corporate governance matters.  The Corporate Governance and Nomination Committee was split into two separate committees in March 2013, at which time the Chairman also became chair of the Nomination Committee.
Non-executive-director-only meetings: it was recommended that the Chairman should hold more regular meetings with the non-executive directors without the executive directors present.	Immediately following each scheduled Board meeting throughout the year, the Chairman meets with the non-executives only.

## Corporate Governance Statement

### Continued

This year, in view of the 2012 evaluation and given the changes to the Board during the review period, it was agreed that an internal rather than external board performance evaluation would be most beneficial to the Company. The Chairman and Company Secretary discussed how best to facilitate this and undertook a review of products from external providers suitable for internal board performance evaluations. Following an online demonstration to the Chairman and Company Secretary, Independent Audit's 'Thinking Board' software package was recommended and subsequently selected. Independent Audit has no other connection with the Company.

The Governance Committee discussed and approved the use of this software at its meeting in October 2013 and thereafter specific online questionnaires were developed and were then completed by all Board members to evaluate the performance of the Board, each of its committees and the Chairman. This year, members of the senior management team were also invited to complete an online questionnaire focusing on Board performance. Following completion of the various questionnaires, the Chairman held a series of one-to-one meetings with each of the directors in December 2013 in order to discuss the answers to the questionnaires. The Chairman's own appraisal was conducted by the Senior Independent Director who did this through a series of one-to-one meetings with the other directors before meeting with the Chairman to present feedback.

The findings of the internal evaluation were then discussed with the Board in December 2013 and a number of action points agreed, including the following:

Key actions	Progress
Board composition: it was agreed that the composition of the Board should be revisited following the appointment/retiral of non-executive directors.	The Board and Nomination Committee have been actively considering Board composition throughout 2013 and 2014 to date. This matter is ongoing in view of the Board changes which will take effect at the AGM.
Board dynamics: it was identified that dynamics between executive and non-executive directors had on occasion been more complex than was necessary.	The Chairman provided feedback to the whole Board on specific examples of this and clarified the approach to be taken by all directors going forward.
Strategy setting: it was identified that senior management members beneath Board level involved in strategy setting may in certain instances require more support from the Board.	The Chairman provided feedback to the whole Board on specific examples of this and it was agreed that a better balance could be struck between challenge and approval of forward strategy.

Following the internal performance evaluation process conducted in 2013, the Board and the Board committees are satisfied that they are operating effectively and that each Director has performed well in respect of their individual roles on the Board. As explained above, some improvements have been identified and have already been or will be addressed during 2014. Following the results of the individual performance evaluations, the Board believes that all of the directors' performances continue to be effective and that they each demonstrate commitment to their role.

The executive directors also have their performance individually reviewed by the remuneration committee against KPIs and objectives which are set annually. Further details of the KPIs can be found in the KPI section on pages 26 to 29. The bonuses payable to the executive directors under the Company's cash bonus scheme (described further in the Directors' Remuneration Report on pages 81 to 98) are linked directly to the results of these reviews.

### Independence of Non-Executive Directors

The Board evaluation and review process covered the independence of each of the non-executive directors, taking into account their integrity, their objectivity and their contribution to the Board and its committees. The Board is of the view that the following behaviours are essential for a director to be considered independent:

- provides an objective, robust and consistent challenge to the assumptions, beliefs and views of senior management and the other directors;
- questions intelligently, debates constructively and challenges rigorously and dispassionately;
- acts at all times in the best interests of the Company and its shareholders;
- has a detailed and extensive knowledge of the Company's business and of the market as a whole which provides a solid background in which they can consider the Company's strategy objectively and help the executive directors develop proposals on strategy; and
- has no close ties or material relationships with the Company, either directly or indirectly.

Having reviewed the independence of each of the non-executive directors (excluding the Chairman) against these criteria, the Board concluded that all non-executive directors (excluding the Chairman) demonstrated each of the required competencies to a high level and are, therefore, each considered independent. The Company does however recognise that in view of the characteristics of independence set out in the UK Corporate Governance Code, including if a director has served on the Board for more than nine years, that Todd Hunt will no longer be considered to be an independent non-executive director.

### Induction and Development

New directors receive a full and appropriate induction on joining the Board. This involves meetings with other Board members (in particular the Chairman), senior management and the Company's principal advisers. In addition, any new director is provided with a comprehensive induction pack which contains a wide range of materials shown in more detail in the table on page 70.

The Company also provides on an ongoing basis the necessary resources for developing and updating its directors' knowledge and capabilities. In particular, the Company is committed to the provision of continuing professional development training to its directors. In 2013 the Company continued with its practice of providing a Directors' Education Programme consisting of a number of seminars for Board members, which are presented by the Company's external advisers/guest speakers/members of senior management, on subjects appropriate to the Company's business, including changes to legislation, regulation and market practice. During 2013 the subjects covered by these seminars included:

- tertiary well control management;
- Cairn and the Scottish independence referendum;
- Spanish assets and doing business in Spain;
- anti bribery and corruption update;
- revised directors' remuneration reporting regulations and changes in narrative reporting regulations; and
- group insurances (including directors' and officers' liability cover).

These seminars are held prior to Board meetings and are attended by all directors present at such meetings (the Company keeps a record of attendance). This process was reviewed during 2013 and the Board approved the proposed Directors' Education Programme for 2014 at its meeting in October 2013. Any director may request that a particular subject is covered in a seminar. In addition, all media articles relating to the Company and all brokers' and analysts' reports on the Company are distributed to all directors.

# Corporate Governance Statement

Continued

New directors' induction	
<b>Board</b>	Directors' and Company Secretary's contact details; list of Board and committee members and dates of appointment; schedule of matters reserved to the Board; financial delegations of authority; Board papers and minutes of previous meetings; schedule of dates for Board and committee meetings; current directors' education programme.
<b>Committees</b>	Terms of reference for all Board committees.
<b>Risk</b>	Terms of reference for Risk Management Committee and minutes of last meeting; current Group Risk Matrix.
<b>Key policies</b>	Group Corporate Responsibility Business Principles; Group Code of Business Ethics; Anti Bribery and Corruption (ABC) Management System; ABC Business Partner Due Diligence Procedure; Dealing Rules and Model Code; Procedures, Systems and Controls for Compliance with the Listing Rules and Disclosure Rules.
<b>Organisation</b>	Group Structure Chart, current Annual Report and Accounts, and Corporate Responsibility Summary Report.
<b>Governance</b>	UK Corporate Governance Code; FRC Guidance on Board Effectiveness and Audit Committees; ICSA Guidance on Liability of Non-Executive Directors; and GC100 Directors' Remuneration Reporting Guidance.
<b>Legal/regulatory</b>	Memorandum for directors on their responsibilities and obligations as directors.
<b>Insurance</b>	Full details of Directors' and Officers' Liability cover.

## Information and Support

The Board has full and timely access to all relevant information to enable it to perform its duties. The Company Secretary ensures the presentation of high quality information to the Board and its committees and that all papers and information are delivered in a timely fashion. Board and committee papers are delivered securely through an electronic platform.

The Company Secretary and Deputy Company Secretary are responsible for advising the Board, through the Chairman, on all corporate governance matters and each director has access to the advice and services of the Company Secretary and Deputy Company Secretary. There is also a procedure agreed by the Board for directors, in furtherance of their duties, to take independent professional advice if necessary, at the Company's expense.

## Directors' and Officers' Liability Insurance

The Company has directors' and officers' liability insurance in place.

## Conflicts of Interest

The Board has in place a procedure for the consideration and authorisation of conflicts or possible conflicts with the Company's interests. All directors are aware of the requirement to submit details to the Company Secretary or Deputy Company Secretary of any current situations (appointments or otherwise) which may give rise to a conflict, or potential conflict, of interest. Notifications have been received from all of the current directors and there are no conflict matters which require to be authorised. The Board will continue to monitor and review potential conflicts of interest on a regular basis.

## Matters Reserved to the Board and Delegation of Authority

The Board has a formal schedule of matters specifically reserved to it for decision. These reserved matters include determination of the overall strategy of the Company and approval of the annual report and accounts, the Company's annual budget and amendments to that budget over a particular amount, borrowing and security, acquisitions and disposals, capital expenditure over a specified amount, amendments to the organisational structure of the Company and Board, approval of significant changes to accounting policies and approval of management incentive schemes and Company policy on pensions.

By way of example, some of the matters which the Board considered and approved during 2013 were:

- the Company's five-year business plan and annual budget;
- the frontier exploration drilling programme in North West Africa and West of Ireland and the contracting of two rigs for this;
- the Field Development Plan for the Kraken Field in the UK North Sea;
- the initial farm-in to and subsequent farm-out of part interests in three blocks in Senegal;
- the farm-in to block C19 offshore Mauritania;
- the divestment of Cairn's interest in the Mariner Field and surrounding acreage in the UK North Sea; and
- the share buy-back programme to repurchase up to US\$300m of ordinary shares in the Company.

During 2013, the Board comprehensively reviewed and approved revised financial delegations of authority to ensure clarity throughout the business concerning the distinction between financial matters which require Board approval and those that can be delegated to senior management.

The Management Team and the Corporate Team continue to support the Board and Executive Team in the day-to-day operational management of the Company.

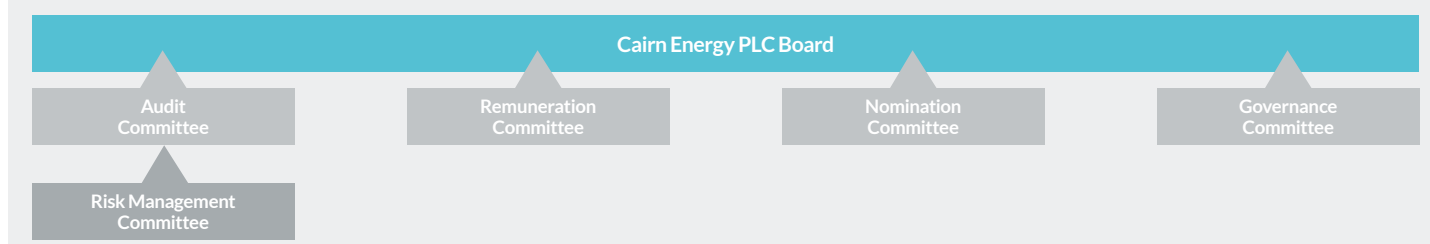
The Management Team comprises nine members of the senior management team and is chaired by the Chief Operating Officer. The role of the Management Team continues to be to lead the delivery of the Company's strategic objectives, including creating and updating the business plan to be recommended to the Board and ensuring that all work programmes are executed, managed and reported while mitigating and managing any operational and business risks.



## Corporate Governance Statement

### Continued

#### Board and Committee Structure



The Management Team meets formally on a regular basis (with a fixed schedule of dates which are normally close to the timing of Board meetings).

The Corporate Team comprises four members of the senior management team and is responsible for enabling and maintaining the Company's access to the capital markets in line with the Company's strategic objectives and is charged with promoting and protecting the Company's reputation as a well run organisation focused on delivering value through a sustainable business. The Corporate Team meets regularly to discuss specific projects. In 2013 and 2014 to date, the Corporate Team has focused on the following key areas: statutory reporting; adherence to governance procedures; implementation of new remuneration reporting requirements; new ventures and stakeholder management; access to capital; business and CR management systems; and effectiveness of internal control.

During 2013, the Management Team and Corporate Team undertook joint quarterly performance reviews to review their progress and to plan ahead on key events, projects and risks. The Executive Team, the Management Team and the Corporate Team have regular joint meetings focusing solely on risk.

The HSE Leadership Team, which is chaired by the Managing Director & CFO and comprises key managers across the business, has continued its work in 2013 with the aim of providing leadership on health, safety and environmental issues and driving initiatives to maintain standards and to focus on HSE performance. During 2013, this included providing externally facilitated training to all staff on the Company's HSE Culture Framework (further information in relation to this can be found in the Operating Responsibly section of this Annual Report).

#### Board Meetings

During 2013, six scheduled meetings of the Board were held, with all but one of these meetings taking place over two consecutive days. The majority of the Board meetings were held at the Company's registered office in Edinburgh with one meeting held at the Company's office in Madrid. Details of attendance at each of those Board meetings, and at meetings of each of the Board committees, are set out in the table opposite.

Given the level of portfolio management and operational activity undertaken by the Company during the year, a number of other meetings took place to deal with specific matters that required to be considered at short notice. When a specific matter requires consideration at short notice, there is a procedure that sets out when those matters must be considered at a short-notice Board meeting and when they may be dealt with by a committee of the Board.

Any director who is physically unable to attend Board and committee meetings is given the opportunity to be consulted and comment in advance of the meeting by telephone or in writing. Video and telephone conferencing facilities are used when directors are not able to attend meetings in person.

The formal agenda for each scheduled Board meeting, which regularly includes presentations from senior operational management, is set by the Chairman in consultation with the Chief Executive and the Company Secretary. Formal minutes of all Board and committee meetings are circulated to all directors prior to the next Board meeting and are considered for approval at that Board meeting. In addition, the members of the Board are in frequent contact between meetings to progress the Group's business. The non-executive directors meet after every Board meeting, without any executives present, to discuss matters in respect of the business.

#### Directors' Attendance at Board and Board Committee Meetings

The table below sets out the attendance record of each director at scheduled Board and Board committee meetings during 2013:

	Board	Audit Committee	Remuneration Committee	Nomination Committee	Governance Committee
Meetings held during 2013	6	5	6	5	4
	Meetings attended	Meetings attended	Meetings attended	Meetings attended	Meetings attended
<b>Executive Directors</b>					
Simon Thomson (Chief Executive)	6	n/a	n/a <sup>3</sup>	5	n/a
Dr Mike Watts (Deputy Chief Executive)	5	n/a	n/a	n/a	n/a
Jann Brown (Managing Director & CFO)	6	n/a <sup>4</sup>	n/a	n/a	4
<b>Non-Executive Directors</b>					
Sir Bill Gammell (Chairman)	6	n/a	n/a <sup>5</sup>	5	4
Iain McLaren (SID)	6	5	6	4	n/a
Todd Hunt	6	n/a	5	3	2
Dr James Buckee	5	5	6	n/a	n/a
Alexander Berger	6	4	n/a	5	4
Jackie Sheppard	6	n/a	6	n/a	4
Ian Tyler <sup>6</sup>	3	3	2	n/a	n/a

#### Notes:

n/a not applicable (where a director is not a member of the committee).

- (1) During 2013, certain directors who were not committee members attended meetings of the Audit Committee, Remuneration Committee, Nomination Committee and Governance Committee by invitation. These details have not been included in the table.
- (2) Where a director was unable to attend meetings of the Board or of Board committees, they reviewed the relevant papers for the meetings and provided their comments to the Board or the Board committees in advance of such meetings.
- (3) Simon Thomson is not a member of the Remuneration Committee but attends its meetings by invitation.
- (4) Jann Brown is not a member of the Audit Committee but attends its meetings by invitation.
- (5) Sir Bill Gammell is not a member of the Remuneration Committee but attends its meetings by invitation.
- (6) Ian Tyler was appointed a member of the Board and of the Audit and Remuneration committees on 28 June 2013. The number of meetings he attended is stated from that date.

#### Board Committees

The Board has established an Audit Committee, a Remuneration Committee, a Nomination Committee and a Governance Committee, each of which has formal terms of reference approved by the Board.

The terms of reference for each of the Board committees satisfy the requirements of the UK Corporate Governance Code and are reviewed internally on an ongoing basis by the Board. Copies of the terms of reference are available on the Company's website.

# Corporate Governance Statement

## Continued

The committees are provided with all necessary resources to enable them to undertake their duties in an effective manner. The Company Secretary acts as secretary to all Board committees with the exception of the Audit Committee, where the Deputy Company Secretary undertakes this role. The minutes of all committee meetings are circulated to all directors.

Set out below are reports from each of the Board Committees. This year, in line with the latest regulatory guidance, the Audit Committee Report is presented as a separate report (on pages 78 to 80) rather than including this in the Corporate Governance Statement.

### Remuneration Committee Report

The Remuneration Committee currently comprises five non-executive directors, all of whom were considered by the Board to be independent throughout the year ending 31 December 2013.

The members of the Remuneration Committee during the year were as follows:

- **Jackie Sheppard (chair);**
- Dr James Buckee;
- Todd Hunt;
- Iain McLaren; and
- Ian Tyler (appointed a member of the committee on 28 June 2013).



Jackie Sheppard

The Remuneration Committee met six times during 2013. The Chairman and Chief Executive of the Company are not members of the committee but attend its meetings by invitation. Certain other executive directors attended meetings of the committee as observers on being invited to do so by the committee. The Company's remuneration advisers, New Bridge Street, also attended some of the committee's meetings. None of the members of the committee, nor the Chief Executive nor the Chairman, participated in any meetings or discussions relating to their own remuneration.

The role of the committee includes:

- determining and agreeing with the Board the remuneration policy for all the executive directors, the Chairman, and the Company's Persons Discharging Managerial Responsibilities;
- within the terms of the agreed policy, determining the total individual remuneration package for each executive director;
- determining the level of awards made under the Company's share option plans and long-term incentive plans and the performance conditions which are to apply;
- determining bonuses payable under the Company's annual cash bonus scheme;
- determining the vesting of awards under the Company's long-term incentive plans and exercise of share options; and
- determining the policy for pension arrangements, service agreements and termination payments for executive directors.

During 2013, the Remuneration Committee also undertook a detailed early review and gap analysis of its reporting in the context of the new Directors' Remuneration Reporting Regulations.

Full details of the Company's policies on remuneration, service contracts and compensation payments are given in the Directors' Remuneration Report on pages 81 to 98, which has been prepared in accordance with the new Regulations.

### Nomination Committee Report

As disclosed in last year's corporate governance statement, it was agreed at the March 2013 Board meeting that the then existing Corporate Governance and Nomination Committee ("CGN") should be split into two separate committees – the Nomination Committee and the Governance Committee, with the Nomination Committee to be chaired by Sir Bill Gammell and the Governance Committee to be chaired by Jackie Sheppard. The membership of both committees was refreshed at that time.

The members of the Nomination Committee during the year were as follows:

- **Sir Bill Gammell (chair with effect from 13 March 2013);**
- Iain McLaren;
- Todd Hunt;
- Alexander Berger;
- Jackie Sheppard (stepped down as chair and member of CGN with effect from 13 March 2013);
- Simon Thomson (member with effect from 13 March 2013); and
- Jann Brown (stepped down as a member with effect from 13 March 2013).



Sir Bill Gammell

The Nomination Committee met five times in 2013. The Chairman and three of the Company's independent non-executive directors are members of the Committee. In addition, to ensure continuing executive input on nomination matters, Simon Thomson was appointed a member of the committee on 13 March 2013 (he was previously an invitee at meetings of the CGN). Jann Brown stepped down as a member following the split of the CGN and is now a member of the Governance Committee only.

## Corporate Governance Statement

### Continued

The role of the Nomination Committee includes:

- considering the composition, balance and skills of the Board and making recommendations to the Board on these matters, on the appointment of new directors and on the reappointment and orderly succession of existing directors; and
- facilitating an annual performance evaluation to ensure that all members of the Board are effectively discharging and devoting sufficient time to their duties and responsibilities.

The Committee considers, on an ongoing basis, the balance of skills, experience, independence and knowledge of the Company on the Board, its diversity (including gender), how the Board works together as a unit, and other factors relevant to the Board's effectiveness.

One of the main recommendations of the 2012 external board evaluation was to appoint up to two new non-executive directors. The Company publicly stated its aim to do this in last year's corporate governance statement and confirmed that external recruitment consultants Ridgeway Partners had been instructed in connection with the proposed appointments. Ridgeway Partners has no other connection with the Company.

The Company subsequently appointed Ian Tyler as a non-executive director. The process with regard to this appointment is described below.

#### Appointment of Ian Tyler

Ridgeway Partners was briefed regarding the proposed appointment in early 2013 and prepared a long-list by the end of February. The long-list was screened by Ridgeway and a number of candidates then short-listed for interview by them. Following these interviews Ridgeway put forward five candidates for consideration by the Company, all of whom met with the Chief Executive. Three candidates were subsequently short-listed by the Company and were interviewed by both the Chairman and Chief Executive, pursuant to which Ian Tyler was selected.

Following selection and prior to his appointment, Mr Tyler met with the other executive and non-executive directors, the Company Secretary and senior management. Mr Tyler was given the opportunity to, and subsequently carried out, due diligence on the Company. The Nomination Committee then recommended to the Board that Ian Tyler be appointed as a non-executive director of the Company and the proposed appointment was unanimously approved by the Board. Mr Tyler was appointed with effect from 28 June 2013 and was also appointed a member of the Audit and Remuneration committees with effect from that date.

As explained on page 67, the Board has subsequently agreed that Mr Tyler will become non-executive Chairman when Sir Bill Gammell retires from this role following the AGM on 15 May 2014.

#### Diversity

The Nomination Committee very much takes into account the benefits of diversity on the Board, including gender. Cairn currently has two women on its Board, one executive (Jann Brown, Managing Director & Chief Financial Officer) and one non-executive (Jackie Sheppard). The Board is also diverse in terms of the range of nationality and international experience of its members.

Cairn aspires to diversify its Board further as part of its succession planning policy, although in seeking to achieve this aspiration we will not appoint a woman to the Board unless she is the best candidate for the role. Whilst two women were short-listed and interviewed for the most recent NED appointment, the selection process identified a male as the best candidate for the role. When engaged in future searches for non-executive directors, the Company will continue to require search consultants to include female candidates on both the long and short lists.

Beneath Board level, we are seeking to develop and increase the number of women in senior management roles across the Group through a number of measures, including our succession planning, training and development and flexible working policies, which support diversity at Cairn. The pipeline of younger talent within the Group is also diverse and bodes well for the future.

#### Succession Planning

The Nomination Committee regularly reviews the structure, size and composition (including the skills, knowledge and experience) required of the Board and makes recommendations to the Board as appropriate. The Board has satisfied itself that the committee has in place appropriate plans for orderly succession to the Board and senior management positions as well as procedures to ensure an appropriate balance of skills within the Company and on the Board and its committees.

The Board and the Nomination Committee have regularly discussed and reviewed Board composition and succession planning throughout 2013 and this will continue in 2014 in view of the Board changes which will take effect following the AGM. The Board intends to appoint a new non-executive director with relevant technical skills and experience during 2014.

The Board and the Nomination Committee are satisfied that the individuals currently fulfilling key senior management positions in the organisation have the requisite depth and breadth of skills, knowledge and experience.

#### Governance Committee Report

As disclosed in last year's corporate governance statement, it was agreed at the March 2013 Board meeting that the then existing Corporate Governance and Nomination Committee ("CGN") should be split into two separate committees, the Nomination Committee and the Governance Committee. The membership of both committees was refreshed at that time.

The members of the Governance Committee during the year were as follows:

- **Jackie Sheppard (appointed chair with effect from 13 March 2013);**
- Todd Hunt;
- Alexander Berger;
- Sir Bill Gammell;
- Jann Brown (appointed a member of the committee on 13 March 2013); and
- Iain McLaren (stepped down as a member of the committee on 13 March 2013).



Jackie Sheppard

# Corporate Governance Statement

## Continued

The Governance Committee met four times in 2013. The Governance Committee is comprised of a majority of independent non-executive directors. In addition, to ensure continuing executive input on governance matters, the Managing Director & CFO was appointed a member of the committee on 13 March 2013 (having previously been a member of the CGN).

The role of the Governance Committee includes:

- reviewing and approving changes to the Board's corporate governance practices and policies;
- monitoring the Company's compliance with the UK Corporate Governance Code and with all applicable legal, regulatory and listing requirements; and
- reviewing developments in corporate governance generally and advising the Board periodically with respect to significant developments in the law and practice of corporate governance.

### Relations with Shareholders

Communications with shareholders are given high priority by the Board. The Company has implemented the provisions of the Companies Act 2006 regarding electronic communication with its shareholders, in order to give shareholders more choice and flexibility in how they receive information from the Company.

In order to ensure that the members of the Board develop an understanding of the views of major shareholders, there is regular dialogue with institutional shareholders, including meetings after the announcement of the year-end and half-yearly results. The Chairman is available to attend a number of these meetings. At the Board meeting immediately following these meetings, a detailed report is given to all directors who were not in attendance at those meetings. In addition, the Company maintains an external relations database which details all meetings attended by the directors with third party stakeholders. All analysts' and brokers' reports on the Company are also distributed to all directors. Cairn responds promptly to correspondence from shareholders and its website contains a wide range of information on the Company, including a dedicated investor relations section.

A list of the Company's major shareholders can be found in the Directors' Report on page 65.

The senior independent non-executive director is available to shareholders if they have concerns that contact through the normal channels of the Chairman, the Chief Executive or the Managing Director & CFO has failed to resolve or for which such contact is inappropriate.

Each of the non-executive directors is available to attend meetings with major shareholders (without the executive directors present), if requested by such major shareholders.

In April 2013, the Chairman and the Company Secretary met or held conference calls with a number of the Company's major shareholders and certain proxy voting agencies to discuss governance. The matters discussed included the following:

- an explanation of the main findings of the external Board performance evaluation and how the Company is implementing the recommendations (including Board composition, the role of the Chairman and changes to Board committees);
- the Company's Board meetings process (including pre-Board meetings followed by Board and committee meetings over two consecutive days)
- changes to advisers (particularly external and internal auditors);
- diversity; and
- the Company's risk management process (see pages 42 to 49 for more details of this process).

These meetings allowed major shareholders to express their views on the matters discussed in advance of the Company's AGM in May 2013 and for the Company to consider and respond to any other issues raised. At these meetings, a number of shareholders provided very positive feedback in relation to the Company's governance reporting.

The Company recognises that the success of the comply-or-explain approach under the UK Corporate Governance Code depends on an ongoing and open dialogue with shareholders, and remains committed to communicating with shareholders, as well as proxy voting agencies, on any matter which they wish to discuss in relation to the Company's governance.

### Annual General Meeting (AGM)

The Board uses the AGM to communicate with private and institutional investors and welcomes their participation. It is policy for all of the Company's directors to attend the AGM if possible. Whilst this may not always be possible for business or personal reasons, in normal circumstances the chair of each of the Board committees will be available to attend the AGM and be prepared to answer questions.

It is policy to involve shareholders fully in the affairs of the Company and to give them the opportunity at the AGM to ask questions about the Company's activities and prospects. Details of resolutions to be proposed at the AGM on 15 May 2014 can be found in the Notice of AGM posted with this Annual Report. Further explanation of each of the resolutions can also be found in the Notice of AGM.

The proxy votes for and against each resolution, as well as abstentions, will be counted before the AGM and the results will be made available at the meeting after the shareholders have voted in a poll on each resolution. Both the Form of Proxy and the poll card for the AGM include a "vote withheld" option in respect of each resolution, to enable shareholders to abstain on any particular resolution. It is explained on the Form of Proxy that a "vote withheld" is not a vote in law and will not be counted in the calculation of the proportion of the votes "for" or "against" a resolution.

The information required to be disclosed by DTR 7.2.6.R (in relation to securities and voting rights thereon) is set out in the Directors' Report on page 65.

### Directors' Responsibility Statement

The directors are responsible for preparing the annual report, the Directors' Remuneration Report and the financial statements in accordance with applicable laws and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law, the directors have prepared the Group and parent Company financial statements in accordance with International Financial Reporting Standards (IFRSs) issued by the International Accounting Standards Board (IASB) and as adopted by the European Union. Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and the Company and of the profit or loss of the Company and Group for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable IFRSs issued by the IASB and adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements;
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Group and Company and enable them to ensure that the financial statements and the Directors' Remuneration Report comply with the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the Company and Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

## Corporate Governance Statement Continued

The directors consider the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's performance, business model and strategy.

Each of the directors, whose names and functions are listed in the Board of Directors section on pages 62 and 63, confirm that, to the best of their knowledge:

- the Group financial statements, which have been prepared in accordance with IFRSs as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Group and Company; and
- the Strategic Review section of this Annual Report (which is cross referred to in the Directors' Report) includes a fair review of the development and performance of the business and the position of the Group, together with a description of the principal risks and uncertainties that it faces.

### Information pursuant to the Takeovers Directive

The Company has provided the additional information required by DTR 7.2.7 (directors' interests in shares; appointment and replacement of directors; powers of the directors; restrictions on voting rights and rights regarding control of the Company) in the Directors' Report.

### Going Concern

The directors have considered the factors relevant to support a statement on going concern. They have a reasonable expectation that the Group has adequate financial resources to continue in operational existence for the foreseeable future and have therefore continued to use the going concern basis in preparing the financial statements. In concluding that the going concern assumption is appropriate, the Board and Audit Committee considered the Group cash flow forecasts under various scenarios, and concluded that the Group has sufficient funding to meet its current commitments as and when they fall due.

### Internal Control

The Board is responsible for the Company's system of internal control and for regularly reviewing its effectiveness. The Company has in place an Integrated Internal Control and Assurance Framework (the "framework"), which plays a critical role in setting out how the Company manages and assures itself that the risks relating to the achievement of corporate vision, strategy and objectives are effectively controlled. The framework is based on the Committee of Sponsoring Organisations (COSO) framework and its five key components, which is the most commonly used and recognised framework for considering internal control systems. It is central to safeguarding shareholders' interests and Company assets. This system of internal control is in accordance with the UK Corporate Governance Code and is designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable but not absolute assurance against material misstatement or loss.

The framework has been in place in respect of the Company for the 2013 accounting period and up to the date of approval of the report and accounts. The Board has carried out a review of the effectiveness of the system of internal controls during 2013 and will ensure that such reviews are performed in 2014. In so doing, the Board has taken into account the assurance provided by the Chief Executive in respect of the effectiveness of the system of internal control within the Company. The Board is accordingly satisfied that effective controls are in place and that risks have been mitigated to an acceptable level.

The Company is subject to a variety of risks which derive from the nature of the oil and gas exploration and production business and relate to the countries in which it conducts its activities (see pages 42 to 49 of this Annual Report for more information on risks). The directors believe that Cairn derives its competitive edge by focusing resource in areas which offer potential for material growth, where the Company has a technical and commercial advantage. The Company's experience gained over many years enables risks to be managed effectively and appropriately.

Operations in any country are only possible when values are shared.

The directors believe that the values of integrity, social and environmental responsibility, teamwork and nurturing of individuals, creativity, risk management and alliances with key partners are ingredients that are central to the Company's success. Throughout the Company's work, Cairn considers all its stakeholders' interests and has a consultative engagement programme with host governments, joint venture partners, investors and local communities where it operates. The directors recognise the value of working as a partnership with host governments, both nationally and regionally, and believe this is a critical ingredient in delivering a successful business.

Particular attention has been placed by the Company's management during 2013 on ensuring that a robust system of internal control has been maintained during the year in relation to the key risks in the Company's business activities. The Company has undertaken a number of transactions during 2013 through which it has entered into new joint ventures in Senegal, the Republic of Ireland, Mauritania and Morocco. The system of internal controls will be applied in all of these new business locations.

During 2013, external specialists from Grant Thornton (GT) conducted a review of the Company's internal control framework documentation to determine whether it complied with all of the relevant corporate governance requirements, that it is in line with best practice and that it is understood within the business. This review concluded that while the framework document lays out all of the requirements, it is less effective in spelling out responsibilities and how the framework is implemented in the expanded business. The framework document will be updated based on the outcome of the review, and will be rolled out across the business in Q1 2014.

Additionally, enhancements have been made during 2013 to the following key controls, business processes and procedures:

- The technical, contractual and financial delegation of authority has been refreshed for the new regional organisation to ensure accountabilities and responsibilities are clearly defined.
- The Well Engineering and Construction Management System has been finalised and issued, including a new Cost Control and Budget Management Standard.
- The updated Company Corporate Responsibility Management System (CRMS) has been finalised and rolled out. A series of workshops has been held with all staff to raise awareness of the new Cairn HSE Cultural Framework and to further embed the desired behaviours towards HSE.
- A policy has been issued defining the Company's approach to communications using social media.
- The Company's Business Risk Management System has been updated for enhancements to the process over the last few years and to reflect the new regional organisation.
- The Management System (MS) in the Stavanger office has been updated to cover participation in non-operated developments as well as exploration and appraisal activities, to meet regulatory requirements.
- Following a treasury review by the internal auditor in late 2012, a follow-up review has been conducted by Deloitte of all the treasury policies, standards and procedures, including a comparison with best practice and industry peers. The review identified a number of additional policies which will be considered by the Treasury Sub-Committee.
- Business Continuity Plans have been updated across the Company to reflect the current business impacts and recovery strategies, including a change in disaster recovery provider.
- The anti bribery and corruption procedures covering the supply chain and the selection of new business partners have been updated for the "lessons learned" over the past year.

# Corporate Governance Statement

## Continued

The following describes the key elements of the framework and the processes used by the Board during 2013 to review the effectiveness of the system and the approach to be taken in 2014.

### 1. Strategic Direction

The Company's business model is that the strategy and business plan are proposed by the executive directors and approved by the Board. The Chief Executive is responsible for managing the Company's business and proposing and developing the Company's strategy and overall commercial objectives in consultation with the Board. As leader of the Executive Team, he is also responsible for implementing the decisions of the Board and its committees and ensuring successful and efficient achievement of the Company's objectives.

### 2. Operating Management

The Company operates three regional units covering different countries and with various partners on both an operated and non-operated basis. Supporting the strategy is a matrix organisation where the assets are the principal focus tasked with delivering objectives for their particular asset with functional departments providing support to the assets in delivering their objectives.

The Executive Team, which comprises the three executive directors, has the primary role of devising strategy (including new ventures) and sanctioning the business plan and work programmes and budget, and overall responsibility for investor relations, corporate governance matters and implementing the communications strategy. Reporting to the Executive Team are two teams: the Management Team, who are primarily responsible for day-to-day management of the delivery of the approved business plan and work programmes; and the Corporate Team, who are responsible for maintaining market reporting and communications and ensuring corporate governance processes are effectively implemented. Further information on the Management Team and the Corporate Team can be found earlier in this statement on pages 70 and 71. The directors have also appointed Functional Department Heads whose roles include providing expert input and challenge to the work programmes, budgets and business plans, supplying the relevant director with full and accurate information with which to make statements on the adequacy of internal control.

A business plan with a five-year outlook and annual work programmes and budgets are prepared annually to help ensure the Company meets its strategy. These start at asset level before being consolidated at Regional and Company levels. The business plan sets out detailed objectives and key performance indicators for each asset and supporting functional departments, and is consolidated into the Company's annual business plan. After an iterative process, the business plan and budget are presented to the Executive Team and the Board for approval.

The asset management teams then have the required authority to implement the business plan and to deliver the agreed work programmes within the approved budget and delegations of authority, and in accordance with the internal control framework.

### 3. Risk Management

The Risk Management Committee ("RMC"), established by the Board in 1999, continues to be responsible for the development of risk management strategy and processes within the Company and for overseeing the implementation of the requirements of this strategy. It does this by ensuring that the framework for the identification, assessment, mitigation and reporting on all areas of risk is fit for purpose and that appropriate assurance arrangements are in place in relation to these risks to bring them within the Risk Appetite agreed by the Board.

The Company's Business Risk Management System ("BRMS") defines the processes through which Cairn seeks to systematically identify, analyse, assess, treat and monitor the business risks faced by the Company. The BRMS also identifies the risk management organisational structure through which business risks are managed and regularly reviewed at operating, asset, country and Company levels. The BRMS was updated in 2013 to cover enhancements to the process over the last few years and to reflect the new regional organisation.

The RMC was chaired by Simon Thomson, the Chief Executive for the first six months of 2013 and then in accordance with a rotation policy, the chair was taken over by Jann Brown, Managing Director & CFO with effect from 1 July 2013. The RMC currently comprises executive directors and senior functional management. The Internal Auditor also attends RMC meetings, in order to ensure internal audit's integration with the risk management process. Regular joint Management and Corporate Team, and joint Management, Corporate and Executive Team risk meetings were also held to manage the assessment and treatment of business risks that may affect the Company's ability to deliver its strategy.

The RMC relies on the identification of business risks, together with the identified mitigating measures and responsibilities, which are recorded in asset, country, regional and departmental risk registers and then consolidated into the Company's risk register, which is regularly reviewed by the joint Management and Corporate Teams, joint Management, Corporate and Executive Teams and the RMC to ensure that the business understands the key risks it faces and that there is an embedded risk management approach in place across the Company.

Enhancements to our approach to risk management during 2013 included:

- holding a series of workshops to undertake an assessment of the gross versus net risks and to identify the key controls that are in place to mitigate these risks. The risk management approach and reporting of risks to the RMC were updated, in particular providing a more rigorous differentiation between the risks that we can tolerate (with existing controls) and those that need to be treated with additional controls;
- extensive use of bowties, a tool used by the Company to map out the key risk interdependencies, causes, consequences and mitigations for an identified risk.

The RMC reports on the Company's risk profile to both the Audit Committee and the Board. Additionally, the Audit Committee and the Board receive internal reviews of the effectiveness of internal controls relative to the key risks. The conclusion of the Board following these reviews during 2013 is that the internal controls in respect of key risks are effective.

## Corporate Governance Statement

### Continued

#### 4. Assurance

The framework adopted by the Board provides for the standard three levels of assurance against the risks facing the Company: first of all at the operational level; secondly through overview by functional management and the RMC; and thirdly through internal, external or joint venture audits.

The integrated internal control and assurance framework document includes a description of the Company's business and assurance models and of its organisation and committee structure, and defines responsibilities. The framework defines the key policies and procedures which govern the way in which Cairn conducts its business and are therefore a core part of its system of internal control. As mentioned earlier, Cairn's internal control and assurance framework document was reviewed by external specialists in 2013 and an updated framework document finalised and rolled out across the business in Q1 2014.

During 2013, the directors reviewed the effectiveness of the Company's system of financial and non-financial controls, including operational and compliance controls, risk management and high-level internal control arrangements. The Directors derived assurance from the following internal and external controls during 2013:

- a regularly updated schedule of matters specifically reserved for a decision by the Board;
- implementation of policies and procedures for key business activities;
- an appropriate organisational structure;
- control over non-operated joint venture activities through delegated representatives;
- specific delegations of authority for all financial transactions and other key technical and commercial decisions;
- segregation of duties where appropriate and cost-effective;
- business and financial reporting, including KPIs;
- functional management reviews;
- an annual "letters of assurance" process, through which asset and functional managers review and confirm the adequacy of internal financial and non-financial controls and their compliance with Company policies, and report any control weaknesses identified in the past year;
- a "letter of assurance" from the Chief Executive confirming the adequacy of internal controls within the Company in line with its policy, and reporting of any control weaknesses identified in the past year;
- an annual internal audit plan, which is approved by the Audit Committee and Board and is driven by risks and key controls;
- reports from the Audit Committee and RMC;
- reports from the external auditor on matters identified during its statutory audit;
- reports from audits by host governments and co-venturers;
- independent third party reviews; and
- the skills and experience of all employees.

#### Compliance with the UK Corporate Governance Code

Throughout 2013 the Company complied with the provisions of the UK Corporate Governance Code published in 2012, except in the following area:

Provision of the UK Corporate Governance Code	Company position	Explanation
B.1.1 – the Board should state its reasons if it determines that a director is independent notwithstanding the existence of relationships or circumstances which may appear relevant to its determination, including if the director has served on the Board for more than nine years from the date of their first election.	Todd Hunt has served on the Board for more than nine years since his initial appointment to the Board in May 2003.	The Company accepts that Mr Hunt is no longer independent given his length of tenure but the Board has agreed that he should continue as a non-executive director in order to retain his valuable technical skills, and extensive business experience following the retirement of Sir Bill Gammell and Dr James Buckee at the AGM.

## Audit Committee Report

### Dear Shareholder

Throughout 2013, our activities continued to be focused on the integrity of the financial reporting of the Group, the quality of the external audit process and the appropriateness of internal controls. We will continue to evolve our activities and our reporting to you in light of guidance from regulators and in line with market best practice.

During the year under review, I served as Chairman of the Audit Committee alongside three of my fellow Non-Executive Directors, all of whom are considered by the Board to be independent.

The members of the Committee who served with me during the year were:

- Dr James Buckee;
- Alexander Berger; and
- Ian Tyler (appointed a member of the committee on 28 June 2013).



Iain McLaren

We met five times in 2013. At our request, the Chief Financial Officer and senior members of the Finance Department attended each of these meetings. Other relevant people from the business are also invited to attend certain meetings to give us the necessary insight into their own areas of business, for example in relation to the reporting of oil and gas reserves.

In addition, all but one of these meetings was attended by the external auditors and by the internal auditors.

The external auditors receive copies of all relevant Audit Committee papers (including the papers that were considered at the meeting when they were not in attendance) and minutes of all Committee meetings. In addition, I regularly meet with the external audit partner to discuss matters relevant to the Group.

### Responsibilities

The Terms of Reference of the Committee take into account the requirements of the Code and are available for inspection on the Group's website.

These include:

- monitoring the integrity of the financial statements of the Group and formal announcements relating to the Group's financial performance and reviewing any significant financial reporting judgements contained in them;
- reviewing accounting policies, accounting treatments and disclosures in financial reports;
- reviewing the Group's internal financial controls and internal control and risk management systems and oversight of the Group's Risk Management Committee;
- monitoring and reviewing the effectiveness of the Group's internal audit function;
- overseeing the Group's relationship with the external auditors, including making recommendations to the Board as to the appointment or reappointment of the external auditors, reviewing their terms of engagement and engagement for non-audit services, and monitoring the external auditors' independence, objectivity and effectiveness; and
- reviewing the Group's whistleblowing procedures and ensuring that arrangements are in place for the proportionate and independent investigation of possible improprieties in respect of financial reporting and other matters and for appropriate follow-up action.

The members of the Committee have been chosen to provide the wide range of financial and commercial experience needed to fulfil these duties. In addition, both Ian Tyler and I have Chartered Accountant qualifications as well as recent and relevant financial experience.

### Main Activities of the Committee During the Year

The first two meetings of the Audit Committee, in January and March 2013, were principally concerned with the 2012 year-end results and process. The significant accounting issues (as reported in the 2012 Annual Report) were discussed and agreed. The Committee also met to conduct the final stage of the competitive tender for external audit services (which was explained in full in the 2012 Annual Report). This took the form of a presentation by four firms to the Audit Committee in January 2013.

The following meetings in June and August 2013 focused on the half-year results for 2013 and planning for the 2013 year-end process. The main issues discussed were in relation to impairment of the Group's remaining ~10% interest in Cairn India Limited which is included adjacent in the 2013 year-end significant accounting issues. Full details are given in Note 3.1 to the Financial Statements on page 116.

There was also a discussion on the treatment of foreign exchange movements in the deferred tax calculation relating to the CIL shares.

In October 2013, the internal audit plan for 2014 was discussed and three audits agreed for the first quarter of 2014.

As explained in the 2012 Annual Report, Cairn ran competitive tenders for the positions of both external auditor and internal auditor last year and time was spent at each Committee meeting in ensuring that the handover plans for these services were being managed effectively.



## Audit Committee Report

### Continued

At each meeting, the Committee monitors the work of the Internal Audit function, now outsourced to Ernst & Young LLP. We agree the areas to be covered by internal audit and ensure that any findings are quickly implemented by management. In relation to whether the annual report and accounts, taken as a whole, are fair balanced and understandable, it was agreed by the Board that this was a responsibility of the whole Board and therefore this has not been delegated to the Audit Committee.

### 2013 Year-End and Significant Accounting Issues

Since the year end, we have met twice (in January and March 2014) in respect of the 2013 year-end accounts. The key issues discussed are set out in the table below.

#### Key accounting issue

Impairment of the Catcher asset	Deferred tax credit arising on the Kraken Field	Goodwill impairment testing on North Sea assets	Impairment of the Financial asset remaining in CIL	Post Balance Sheet Events – restriction on sale of CIL
---------------------------------	---	---	--	--

#### Background

At each reporting date, the Audit Committee review the Group's oil and gas exploration/appraisal assets for indicators that the assets may be impaired. The Committee concluded that an indicator of impairment did exist for one of the Group's UK assets, the Catcher field and an impairment test was performed by management, resulting in impairment of the asset.	In November, DECC approved the field development plan for the UK Kraken field at which point the asset was re-classified from exploration/appraisal assets into development/producing assets. Approval of the field development plan also confirmed that the asset is eligible for two Heavy Oil field allowances, introduced by the UK Government in 2011, reducing the Group's future tax charge on the forecast profits from the field.	Goodwill, allocated to the Mature Basin North Sea segment, is tested annually for impairment by comparing the carrying value of the assets and liabilities in the cash-generating unit ("CGU") to the recoverable amount of the exploration and development assets in this CGU.	The Group's remaining ~10% interest in Cairn India Limited is held at market value in the Group's balance sheet, with movements in the valuation recorded within other comprehensive income. At the July meeting it was noted that there had been a significant fall in the valuation of the asset from the value recorded at the date of its original recognition.	In January 2014, Cairn received a request from the Indian Income Tax Department to provide information in relation to the year ended 31 March 2007. While the interactions with the Indian Income Tax Department continue, Cairn has been restricted from selling its shares in CIL.
---	--	---	---	--

#### Audit Committee action

We carefully examined the asset impairment test and challenged management's underlying assumptions (such as oil price, discount rates, inflation and escalation rates etc.), seeking external evidence to support these assumptions where necessary. These assumptions are used in the discounted cash flow models used to value the asset.	The Audit Committee examined the proposed accounting treatment for these field allowances, where they have been added to the tax base of the Kraken asset recoverable against future taxable profits, and the subsequent recognition of a deferred tax asset.	In addition to the review of the underlying assumptions, the Audit Committee sought assurance from the Director of Operations on the reserve and resource estimates that feed cash flow models used to determine the net present value of the North Sea assets. We challenged the revisions to estimates in the year and the variations between management's estimates and those of the operator.	The Audit Committee debated whether or not this fall in value should result in an impairment of the investment.	Though discussions are ongoing, the Audit Committee examined the disclosures made by management in the 2013 year-end financial statements, confirming that the disclosures were accurate and complete.
---	---	---	---	--

#### Audit Committee conclusions

Following challenge, the Audit Committee gained comfort that management's assumptions were appropriate. We were also satisfied that there were no further indicators of impairment on the Group's other oil and gas assets.	Having discussed with the auditors that management's proposed treatment complied with IFRS and was consistent with emerging industry practice, we accepted management's proposed accounting treatment.	We concluded that impairment of goodwill did exist and that the methodology for determining the fair value less cost of disposal of the Group's North Sea assets was correct and appropriate reserve estimates had been used.	Although we believed that the fall in value was not a permanent diminution in the value of the investment, it was significant and therefore under IFRS, impairment should be recognised.	The Audit Committee agreed with management that the restriction was a non-adjusting post balance sheet event and confirmed with the auditors that the proposed disclosures met the requirements of IFRS.
---	--	---	--	--

#### Further details

Section 2.1 on page 111	Section 4.3 on page 124	Section 2.4 on page 114	Section 3.1 on page 116	Section 6.1 on page 132
-------------------------	-------------------------	-------------------------	-------------------------	-------------------------

### Going Concern

At each reporting date management consider the factors relevant to support a statement of going concern (see Corporate Governance section on page 75). The Audit Committee review and challenge management's conclusions so that we may, in turn, provide comfort to the Board that management's assessment has been considered and challenged where appropriate.

Given the post balance sheet restriction on the sale of the shareholding of Cairn India, reducing the Group's liquid assets, the Audit Committee carefully reviewed management's going concern conclusion based on the Group's latest net cash position and the forecast spend to period ending 31 March 2015. This confirmed that the Group is fully funded to meet its work programme and firm commitments. The Audit Committee subsequently recommended to the Board that the Group continues to use the going concern basis in preparing its financial statements.

# Audit Committee Report

## Continued

### External Audit

The current edition of the UK Corporate Governance Code states that FTSE 350 companies should put the external audit contract out to tender at least every ten years. As explained in the 2012 Annual Report, Cairn decided to comply with this provision early and undertook an external audit re-tendering process in 2012 and early 2013.

Following this process (which was fully described in the 2012 Corporate Governance Statement) Cairn announced in March 2013 that it proposed to appoint PricewaterhouseCoopers LLP (PwC) as auditor of the Group commencing with the 2013 financial half-year, following our recommendation. As resigning auditor, Ernst & Young LLP (EY) provided the Company with a statement of circumstances confirming its resignation as auditor of the Company following their unsuccessful tender and a copy of this statement was circulated to shareholders with the 2013 Notice of AGM. Shareholders subsequently approved the resolution to reappoint PwC as auditor of the Company at the AGM held on 16 May 2013.

PwC therefore took over from EY as external auditor following conclusion of the 2012 year-end audit with a smooth transition and handover completed in advance of the 2013 financial half-year. As part of this transition process, both EY and PwC were in attendance at the March 2013 Audit Committee meeting with PwC assuming full responsibility for reporting to the Audit Committee with effect from the following meeting in June 2013.

### Assessment of External Audit Process

During the course of the year, we have been closely monitoring the performance of PwC as our new auditor. This has included gaining feedback from regular meetings with the Group's senior finance staff on implementation of the transition plan agreed during the tender process, feedback from meetings with key Cairn senior staff throughout the organisation, regular and detailed reporting by the auditor on the findings of interim audit work conducted during 2013 and an assessment of the external audit effectiveness conducted by the Company prior to the March 2014 Audit Committee meeting.

The annual assessment of PwC's performance on their first full year audit of the Group involved completion of a questionnaire by each member of the Audit Committee, the Chief Financial Officer and other senior members of the finance department. The questionnaires were completed following the audit closing meeting held with PwC in early March 2014 and the results of this assessment were then discussed at the March 2014 Committee meeting. There were no actions which required to be taken following this assessment.

### Auditor Independence and Provision of Non-Audit Services

We have a long established policy in relation to the supply of non-audit services by the external auditors. The Group will engage an external adviser to provide non-audit services on the basis of the skills and experience required for the work, where benefit will be derived as a result of the third party's knowledge of the Group and cost. These advisers may include the Group's external auditors, under a restricted set of circumstances (see adjacent), although, before the engagement commences, Cairn must be satisfied that the auditor's objectivity and independence would not be compromised in any way as a result of being instructed to carry out those services.

The Group's current policy for approval of non-audit services was reviewed and re-approved by the Audit Committee in January 2013 and full details of this are set out below.

Fee level (£)	Quotes Required	Audit Committee Approval Required
0-25,000	No	No
25,001-50,000	Yes (with exception*)	No
50,001-100,000	Yes	No
>100,000	Yes	Yes

\* In justifiable circumstances, such as expediency for operational requirements, the need to obtain quotes can be waived.

In all cases, a business justification must be provided for the use of the auditor to undertake the work and where no Audit Committee approval is required, the engagement of the auditor must be approved by the CFO. Where quotes are required these must be obtained from at least two competent firms, with specific reasons being provided for including the Group's auditors. The auditors are specifically excluded from undertaking any work that directly relates to the preparation of the Group financial statements or the financial statements of subsidiaries.

During the year, PwC carried out work on Transfer Pricing, the contract for which is multi-year and had been entered into well in advance of their appointment as external auditor. The independence of PwC as external auditors was maintained as the Transfer Pricing work was performed by a separate team independent of the audit team, and all decisions associated with the work were made by management.

A full breakdown of remuneration paid to the Group's external auditor in respect of both audit and non-audit work is provided in Appendix 5 of the Financial Statements on page 146.

### Internal Audit

Following a competitive tender process, EY was appointed as the Group's internal auditor with effect from July 2013, with KPMG fulfilling the role up to that point. During the handover period, EY reviewed the 2013 Internal Audit Plan and engaged with key stakeholders to identify areas of the business that should be considered for future internal audits. As a result of this work, the Audit Committee confirmed the plan for 2013 and Q1 2014. The full 2014 plan was then agreed at the meeting of the Committee in January 2014.

Prior to the beginning of each year, an internal audit plan is developed by the internal auditor, in consultation with senior management, based on a review of the outcome of the previous year's internal audits, the outcome of the annual assessment of effectiveness of internal control (refer to page 77), the records of historical audits of fundamental business processes and the significant risks in the Group Risk Matrix and identified mitigation measures. The internal auditor also participates in meetings of the Group Risk Management Committee to maintain an understanding of the business activities and associated risks and to update the committee on the internal audit work plan. The Audit Committee also receives updates on the internal audit work plan on an ongoing basis. The external auditors do not place any reliance on the work undertaken by the Group's internal audit function due to the nature of the scope and the timing of their work. The external auditors do, however, attend all Committee meetings where internal audit updates are given.

### Whistleblowing and Related Policies

The Group updated its Whistleblowing Policy during 2012 and the new policy was subsequently rolled out across the organisation and reviewed by the Audit Committee. The committee is satisfied that arrangements are in place for the proportionate and independent investigation of possible improprieties in respect of financial reporting and other matters and for appropriate follow-up action.

The Group has in place a comprehensive Anti-Bribery-and-Corruption Management System and Code of Business Ethics and training has been provided to all staff in relation to these. As Cairn enters new countries, further monitoring is undertaken and training is kept updated. Further information regarding these policies is included in the Group's Corporate Responsibility Report.

Iain McLaren

Chairman of the Audit Committee  
17 March 2013

## Directors' Remuneration Report

### Part 1 – Annual Statement from the Chair of the Committee

Dear Shareholder

As the Chair of Cairn's Remuneration Committee (the "Remuneration Committee" or the "Committee"), I am pleased to present our Directors' Remuneration Report for 2013.

This is the first year that the report is subject to the new regime contained in the amended Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (the "Regulations"). As such, it has been separated into the following parts:

- This "Annual Statement" which identifies the key messages on remuneration for the year under review and explains the business context in which the Committee's major decisions during the period were taken;
- A forward-looking "Directors' Remuneration Policy" which proposes an overall executive remuneration framework that will be adopted and operated by the Company in 2014 and the following two financial years – if approved by shareholders the policy set out in this part of the report will become binding with effect from the AGM to be held on 15 May 2014; and
- An "Annual Report on Remuneration" which provides shareholders with details of the remuneration that was actually delivered to the Company's directors during 2013 and explains how the new policy referred to above will be applied in 2014 – this final part of the report will be subject to an advisory vote at the forthcoming AGM.

#### Overview of Cairn's remuneration policy

Although the form of this year's Directors' Remuneration Report is somewhat different from those of previous periods, the Committee's overall philosophy for rewarding our executives and senior managers remains largely unchanged. Our aim is to ensure that pay arrangements appropriately and responsibly incentivise these individuals to achieve the Group's strategic objectives which should, in turn, create, realise and add value for the Company's shareholders. The total potential remuneration for Executive Directors is generally weighted more towards variable pay and, within that element, the greatest opportunity for reward lies in the delivery of sustained levels of long-term performance. This reflects the nature of Cairn's business and ensures a high degree of alignment with the Company's shareholders.



The outlined approach to pay is reflected in the detailed Directors' Remuneration Policy that is set out on pages 82 to 89. There are no significant differences between this policy and the one that applied in 2013.

#### Summary of 2013 business context and key remuneration decisions

The work of the Committee in 2013 was conducted against a backdrop of a year in which the Company fulfilled its objective of operating with a focus on safety, building a business with appropriate exposure to material frontier and mature basin exploration whilst maintaining a strong balance sheet with financial flexibility.

Its key decisions relating to remuneration in 2013 are described in more detail in the Annual Report on Remuneration contained on pages 90 to 98 and can be summarised as follows:

#### Base salary

Simon Thomson received an increase to base salary of 6.3% with effect from 1 January 2013 and Jann Brown and Dr Mike Watts received increases of 2.6% and 2.7% respectively. The increases for Jann Brown and Dr Mike Watts were consistent with the level of standard annual salary increase awarded to other employees on 1 January 2013. As explained in last year's Directors' Remuneration Report, Simon Thomson's rise in 2013 salary reflected the Committee's view of his progress in his new role as Chief Executive.

#### Annual bonus

Based on an assessment of the extent to which the applicable measures and targets were achieved during 2013, awards made to the Executive Directors under the Company's annual bonus scheme for the period (as a percentage of salary) were 63% in the case of Simon Thomson, 62% for Jann Brown and 61.5% for Dr Mike Watts. Further details of the way in which these awards were determined are set out on pages 93 and 94 of the Annual Report on Remuneration.

#### Long Term Incentive Plan

The performance period applicable to the Long Term Incentive Plan (or "LTIP") awards granted in 2010 came to an end during 2013. However, the performance conditions that required to be satisfied in order for vesting to occur under this arrangement were not achieved with the result that no shares were released to participants and the awards lapsed.

#### Applying the policy for 2014

The ways in which the Company's remuneration policy will be applied in 2014 are set out in detail on page 98 in the Annual Report on Remuneration. In particular, salaries for the Executive Directors were increased by 2.5% on 1 January 2014 in line with the standard annual increase awarded to other employees in the Group. The Group KPI measures used for the annual bonus scheme (and their respective weightings) have been reformulated for 2014 in order to appropriately reflect the Company's strategic goals for the period. In addition, the proportion of the Chief Executive's bonus opportunity for the year that will be determined by reference to these corporate measures has been increased to 100% (from the 90% level that applied in 2013). No material changes have been made to the manner in which the LTIP will operate in 2014.

#### Shareholder support and feedback on Directors' Remuneration Report

We welcome questions and feedback from all parties on both the content and style of this report and hope that shareholders are supportive of the remuneration-related resolutions that are to be proposed at the AGM on 15 May 2014.

**M. Jacqueline Sheppard QC**

Remuneration Committee Chair  
17 March 2014

M. Jackie Sheppard QC

# Directors' Remuneration Report

## Continued

### Part 2 – Directors' Remuneration Policy

#### Introduction

This Directors' Remuneration Policy provides an overview of the Company's policy on directors' pay that will be applied in 2014 and later years. It sets out the various pay structures that the Company will operate and summarises the approach that the Committee will adopt in certain circumstances such as the recruitment of new directors and/or the making of any payments for loss of office.

As highlighted in the Annual Statement from the Chair of the Committee, the policy contained in this part will be subject to a binding vote at the AGM to be held on 15 May 2014 and will take effect immediately upon receipt of such approval from shareholders.

#### Purpose and role of the Remuneration Committee

The Remuneration Committee determines and agrees with the Board the overall remuneration policy for the Executive Directors and the Group's PDMRs (persons discharging managerial responsibilities). Within the terms of this agreed policy, the Committee is also responsible for:

- determining the total individual remuneration package for each Executive Director and PDMR;
- determining the level of awards made under the Company's LTIPs and share option plans and the performance conditions which are to apply;
- determining bonuses payable under the Company's annual cash bonus scheme;
- determining the vesting levels of awards under the Company's LTIPs and share option arrangements; and
- determining the policy for pension arrangements, service agreements and termination payments for Executive Directors and PDMRs.

The Committee also reviews and approves the overall remuneration levels of employees below senior management level, but does not set individual remuneration amounts for such individuals. This oversight role allows the Committee to take into account pay policies and employment conditions within the Group as a whole when designing the reward structures of the Executive Directors and PDMRs. For example, the Committee considers the standard increase applied to basic pay across the Group when setting Executive Directors' base salaries for the same period.

Cairn's Remuneration Committee operates within written terms of reference agreed by the Board. These are reviewed periodically to ensure that the Committee remains up-to-date with best practices appropriate to Cairn, its strategy and the business environment in which it operates. The terms of reference of the Remuneration Committee are available on the Company's website.

#### Consultation with relevant stakeholders

The Committee is always keen to ensure that, in carrying out its functions, it takes into account the views and opinions of all the relevant stakeholders in the business.

During the early part of 2012, the Committee undertook a comprehensive programme of engagement with a selection of the Company's larger institutional investors and their representative bodies in order to:

- understand shareholder concerns which led to a substantial vote against the 2011 Directors' Remuneration Report; and
- highlight a number of proposed changes to the Executive Directors' remuneration arrangements intended to address these issues and give shareholders an early opportunity to raise any questions that they might have.

The Committee believes that undertaking this process of constructive dialogue helped to deliver the strong endorsement of the 2012 Directors' Remuneration Report at the 2013 AGM, full details of which are set out on page 91.

In April 2013, the Chairman and the Company Secretary met a selection of larger investors and shareholder voting agencies to discuss governance and remuneration matters.

Finally, although the Committee does not undertake a formal consultation exercise with employees in relation to the Group's policy on senior management remuneration, members of staff are given the opportunity to raise issues on a variety of matters, including executive pay, via the annual employee engagement survey.

## Directors' Remuneration Report

### Continued

#### Overview of remuneration policy and package for 2014

Cairn's policy on Executive Directors' remuneration for 2014 and subsequent financial years is to ensure that it appropriately incentivises individuals to achieve the Group's strategic objectives to create, realise and add value for its shareholders, whilst offering a competitive package against the market.

A description of each of the elements to be comprised in the pay packages for Cairn's directors under its remuneration policy is as follows:

#### Future Policy Table – Elements of directors' remuneration package

Remuneration element	Purpose and link to strategy	Operation	Opportunity	Framework for assessing performance
<b>Base salary</b>	Helps recruit and retain employees. Reflects individual experience and role.	<p>Normally reviewed annually (with changes taking effect on 1 January) and/or when an individual changes position or responsibility.</p> <p>Aim is to provide a competitive base salary relative to the market (although the Committee does not place undue emphasis on benchmarking data and exercises its own judgement in determining pay levels).</p> <p>Decision influenced by:</p> <ul style="list-style-type: none"> <li>– role and experience;</li> <li>– average change in broader workforce salaries;</li> <li>– individual performance; and</li> <li>– remuneration practices in companies of a broadly similar size and value and relevant oil and gas exploration and production companies.</li> </ul>	<p>Annual increases will not exceed the level of standard increase awarded to other employees except that more significant increases may be awarded at the discretion of the Committee in connection with:</p> <ul style="list-style-type: none"> <li>– an increase in the scope and responsibility of the individual's role; or</li> <li>– the individual's development and performance in the role following appointment; or</li> <li>– a re-alignment with market rates.</li> </ul>	None
<b>Benefits</b>	Helps recruit and retain employees.	Directors are entitled to a competitive package of benefits. For UK executives, the major elements include a company car, permanent health insurance, private health insurance, death-in-service benefit and a gym and fitness allowance.	Company cars up to a value of £70,000 (or, as an alternative, an annual car allowance of up to £8,771) may be provided. Other benefits will be in line with the market.	None

# Directors' Remuneration Report

## Continued

Remuneration element	Purpose and link to strategy	Operation	Opportunity	Framework for assessing performance
<b>Annual bonus</b>	Rewards the achievement of annual KPIs and/or other objectives linked to the Company's strategic goals.	<p>Bonuses are awarded by reference to performance against specific targets measured over a single financial year.</p> <p>Any amounts awarded to an individual under this arrangement are paid out in full shortly after the assessment of the performance targets has been completed. However, annual bonuses may be subject to clawback where, in the period of three years from the end of the relevant financial year, the Committee becomes aware of a material misstatement of the Company's financial results or an error in the calculation of performance targets.</p>	Maximum % of salary: 100%.	<p>The measures and targets applicable to the annual bonus scheme (and the different weightings ascribed to each of them) are set annually by the Committee in order to ensure they are relevant to participants and take account of the most up-to-date business plan and strategy.</p> <p>All, or a significant majority, of the bonus opportunity will normally be determined by reference to performance against demanding Group KPIs such as:</p> <ul style="list-style-type: none"> <li>- exploration and new venture objectives;</li> <li>- development and production targets; and</li> <li>- HSE.</li> </ul> <p>Any remaining part of a director's bonus will normally be based on the achievement of personal objectives relevant to that individual's role within the business.</p> <p>A payment scale for different levels of achievement against each KPI and/or other objective is specified by the Committee at the outset of each year – these range from 0% for below-threshold performance up to 100% for full satisfaction of the relevant condition.</p> <p>The Committee has discretion to vary the measures and weightings during the year if events arise which mean that it would be inappropriate to continue with the originally prescribed structure. The Committee expects that this discretion will only be exercised in exceptional circumstances and not to make the bonus scheme for that year less demanding than when it was originally set.</p> <p>In addition, the Committee has discretion to ensure that the ultimate bonus payment for a financial year is fair and reasonable and properly reflects performance over that period.</p>

## Directors' Remuneration Report

### Continued

Remuneration element	Purpose and link to strategy	Operation	Opportunity	Framework for assessing performance
<b>Long Term Incentive Plan (or "LTIP")</b>	Incentivises Executive Directors to deliver superior levels of long-term performance for the benefit of shareholders, thereby aligning the interests of the directors with those of the Company's investors.	<p>Cairn currently operates one LTIP that was approved by shareholders in 2009.</p> <p>Awards of conditional shares and/or nil-cost options are made annually with vesting dependent on achievement of performance conditions chosen by the Committee. Performance is measured over a three-year period.</p> <p>On vesting of an award, only 50% of the shares to which the holder has become entitled are released/ become exercisable immediately, with the remaining 50% normally being released/becoming exercisable after a further period of one year.</p> <p>The Committee reviews the quantum of awards annually, taking into account factors such as market rates and overall remuneration.</p> <p>Awards may be subject to clawback where, in the period of three years from the end of the relevant performance period, the Committee becomes aware of a material misstatement of the Company's financial results or an error in the calculation of performance conditions.</p>	<p>Normal maximum % of salary: 300%. Exceptional circumstances maximum % of salary: 400%.</p>	<p>Vesting of all awards granted under the LTIP to date is determined by comparing the growth in Total Shareholder Return ("TSR") of Cairn over a performance period of three years from grant with the TSR of a comparator group of international oil and gas companies that is selected by the Committee prior to each grant, with 20% vesting at median, 100% at upper decile and on a straight line sliding scale in between.</p> <p>In order to encourage exceptional performance, the above condition provides that, at upper decile levels, a "multiplier" of up to 1.33 is applied if absolute TSR growth is between 50% and 100% (or more).</p> <p>It also states that no part of any award will vest unless the Remuneration Committee is satisfied that there has been an overall satisfactory and sustained improvement in the performance of the Company as a whole over the performance period.</p> <p>Although the Committee's intention is that the above condition will be applied to LTIP awards granted in 2014, it may decide to impose different (but equally challenging) conditions in future years. The Committee will consult with major shareholders prior to making any such decision and will ensure that the vesting of at least 50% of all awards granted under the LTIP continues to be determined by reference to the Company's TSR performance.</p>
<b>Share Incentive Plan (or "SIP")</b>	Encourages a broad range of employees to become long-term shareholders.	<p>The Company established an HM Revenue and Customs approved share incentive plan in April 2010. It allows the Company to provide eligible employees, including the Executive Directors, with some or all of the following benefits:</p> <ul style="list-style-type: none"> <li>- partnership shares acquired using deductions from salary;</li> <li>- matching shares awarded to those employees who purchase partnership shares on the basis of a ratio specified by the Company; and</li> <li>- free shares.</li> </ul> <p>Matching and free shares awarded under the SIP must normally be held in the plan for a specified period.</p>	<p>Participation limits are those set by the UK tax authorities from time to time. With effect from 6 April 2014, these limits are expected to be as follows:</p> <ul style="list-style-type: none"> <li>- Partnership shares: up to £1,800 per tax year can be deducted from salary.</li> <li>- Matching shares: up to two matching shares for every one partnership share purchased.</li> <li>- Free shares: up to £3,600 worth in each tax year.</li> </ul>	None

# Directors' Remuneration Report

## Continued

Remuneration element	Purpose and link to strategy	Operation	Opportunity	Framework for assessing performance
<b>Pension</b>	Rewards sustained contribution.	<p>The Company operates a defined contribution group personal pension plan in the UK. The scheme is non-contributory and all UK permanent employees, including the Executive Directors, are eligible to participate.</p> <p>The Company contributes a specified percentage of basic annual salary for senior employees, including Executive Directors.</p> <p>Where an Executive Director has an individual personal pension plan (or overseas equivalent), the Company pays its contribution to that arrangement.</p> <p>If an Executive Director's pension arrangements are fully funded or applicable statutory limits are reached, an amount equal to the Company's contribution (or the balance thereof) is paid in the form of additional salary.</p>	Company contributes 15% of basic salary on behalf of Executive Directors or pays them an equivalent amount of additional salary.	None
<b>Non-Executive Directors' fees</b>	Helps recruit and retain high-quality, experienced individuals. Reflects time commitment and role.	<p>Non-Executive Directors' fees are considered annually and are set by the executive members of the Board and the Chairman taking into account a range of relevant factors including:</p> <ul style="list-style-type: none"> <li>- market practice;</li> <li>- time commitment; and</li> <li>- responsibilities associated with the roles.</li> </ul> <p>Additional fees are payable to the Chairs of the Audit and Remuneration Committees.</p>	Company's Articles of Association place a limit on the aggregate annual level of Non-Executive Directors' and Chairman's fees (currently £900,000).	None
<b>Chairman's fees</b>	Helps recruit and retain the relevant individual. Reflects time commitment.	The Chairman's fee is considered annually and is determined in light of market practice, the time commitment and responsibilities associated with the role and other relevant factors.	Company's Articles of Association place a limit on the aggregate annual level of Non-Executive Directors' and Chairman's fees (currently £900,000).	None

### Notes:

- (1) A description of how the Company intends to implement the policy set out in this table during the financial year to 31 December 2014 is provided on page 98.
- (2) The following differences exist between the Company's aforementioned policy for the remuneration of directors and its approach to the payment of employees generally:
  - Participation in the LTIP is limited to the Executive Directors and certain selected senior managers. Other employees are eligible to participate in the Company's share option schemes, details of which are provided on pages 129 and 130.
  - Under the Company's defined contribution pension scheme, the Company contribution for less senior employees is 10% of basic annual salary.
  - A lower level of maximum annual bonus opportunity applies to employees other than the Executive Directors and certain PDMRs.
  - Benefits offered to other employees generally comprise permanent health insurance, private health insurance, death-in-service benefit and gym and fitness allowance.

In general, these differences arise from the development of remuneration arrangements that are market competitive for the various categories of individuals. They also reflect the fact that, in the case of the Executive Directors and PDMRs, a greater emphasis is placed on variable pay.
- (3) The TSR performance conditions applicable to the LTIP (further details of which are provided on page 94) were selected by the Remuneration Committee on the basis that they improve shareholder alignment and are consistent with the Company's objective of delivering superior levels of long-term value to shareholders. Under the terms of these performance conditions, the Committee can specify the basis on which TSR for any company is calculated and has the discretion to make adjustments to this methodology to take account of exceptional circumstances, including share capital variations. Where any company becomes unsuitable as a member of the comparator group as a result of, for example, a change of control or delisting, the Committee has the discretion to treat that company in such manner as it deems appropriate (including replacing it with another organisation).
- (4) Where a nil-cost option award under the LTIP becomes exercisable, it will generally remain so until the tenth anniversary of the date on which it was granted.
- (5) The choice of the performance metrics applicable to the annual bonus scheme reflect the Committee's belief that any incentive compensation should be tied to appropriately challenging measures of both the overall performance of the Company against its strategic KPIs and (where appropriate) those areas of the business that the relevant individual can directly influence.
- (6) The legislation applicable to the SIP does not allow performance conditions to be applied in relation to partnership or matching shares and, given that the SIP is an "all-employee" arrangement, the Company has decided that it is not appropriate to apply performance conditions to free shares awarded under it.
- (7) As highlighted on page 97, the Company has a share ownership policy which requires the Executive Directors to build up and maintain a target holding equal to 100% of base salary. Until such a holding is achieved, an Executive Director is obliged to retain shares with a value equal to 50% of the net-of-tax gain arising from any vesting or exercise under the Company's share incentive plans. Details of the extent to which the Executive Directors had complied with this policy as at 31 December 2013 are set out on page 97.



## Directors' Remuneration Report

### Continued

#### Committee discretions

The Committee will operate the annual bonus scheme, LTIP and Share Incentive Plan according to their respective rules and the policy set out in this report. The Committee, consistent with market practice, retains discretion over a number of areas relating to the operation and administration of these arrangements. These include (but are not limited to) the following:

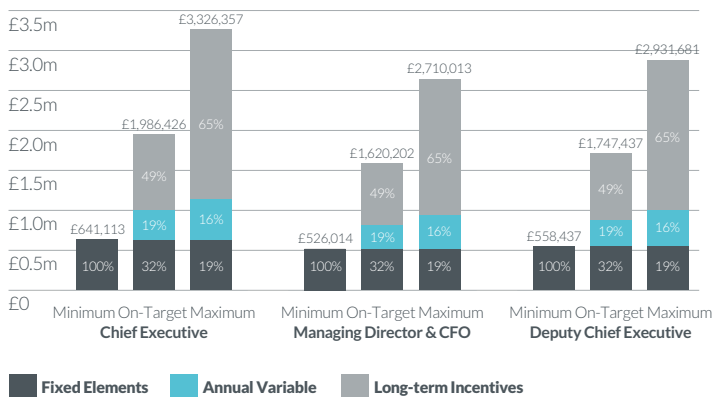
- who participates in the plans;
- the timing of grant of award and/or payment;
- the size of an award and/or a payment;
- discretion relating to the measurement of performance in the event of a change of control or reconstruction;
- the weightings, metrics and targets for the annual bonus plan;
- the determination of the annual bonus payment;
- determination of a “good leaver” (in addition to any specified categories) for incentive plan purposes based on the rules of each plan and the appropriate treatment chosen;
- discretion to disapply time pro-rating in the event of a change of control or good leaver circumstances;
- adjustments or variations required in certain circumstances (e.g. rights issues, corporate restructuring, change of control, special dividends and other major corporate events); and
- the ability to adjust existing performance conditions for exceptional events.

#### Legacy awards

Outstanding share incentive awards that remain unvested/unexercised as detailed on page 95 of the Annual Report on Remuneration remain eligible to vest/be exercised based on their original award terms.

#### Remuneration scenarios relating to the above policy

Cairn's pay policy seeks to ensure that the overall package of the Executive Directors is generally weighted more towards variable pay and, within such variable pay element, that greater emphasis is placed on the delivery of long-term performance through the award of long-term incentives. In the chart below, we show the make-up of remuneration of the Executive Directors in 2014 under minimum, on-target and maximum scenarios.



In developing the above scenarios, the following assumptions have been made:

- The “minimum” columns are intended to show the fixed level of remuneration to which an Executive Director is entitled in 2014 irrespective of performance levels, namely base salary (at current rates), benefits (using the details set out in the 2013 single-figure table provided on page 91) and pension (calculated by applying the percentage entitlement set out in the policy table against latest confirmed salary).
- The “on-target” scenario seeks to illustrate the remuneration the Executive Directors would receive if performance was in line with expectation. In addition to the fixed elements summarised above, it assumes a specified level of payout/vesting under the annual bonus scheme and LTIP. Given that neither of these incentive arrangements explicitly stipulate an “on-target” amount, the assumed levels for this scenario have been calculated by reference to the approximate average annual payouts/vestings for all Executive Directors over the five years up to and including 2013, being a payout of 70% of salary under the annual bonus scheme and a 60% vesting of LTIP awards originally granted over shares worth 300% of salary.
- The “maximum” columns demonstrate total remuneration levels in circumstances where the variable elements payout in full (i.e. annual bonus payment of 100% of salary and 133% vesting of LTIP awards originally granted over shares worth 300% of salary).
- For the purposes of valuing the LTIP awards, any post-grant share price movements have been ignored.
- The Executive Directors are entitled to participate in the SIP on the same basis as other employees. The value that may be received under this arrangement is subject to legislative limits and, for simplicity, has been excluded from the above chart.

# Directors' Remuneration Report

## Continued

### Recruitment policy

#### Base salaries

Salaries for any new director hires (including internal promotions) will be set to reflect their skills and experience, the Company's intended pay positioning and the market rate for the role. Where it is appropriate to offer a below-market salary initially, the Committee will have the discretion to allow phased salary increases over time for newly appointed directors, even though this may involve increases in excess of the rate for the wider workforce and inflation.

#### Benefits

Benefits and pensions for new appointees to the Board will normally be provided in line with those offered to other Executive Directors and employees taking account of local market practice, with relocation expenses/arrangements provided for if necessary. Tax equalisation may also be considered if an executive is adversely affected by taxation due to their employment with Cairn. Legal fees and other relevant costs and expenses incurred by the individual may also be paid by the Company.

#### Variable pay

For external appointments, the Committee will ensure that their variable remuneration arrangements are framed in accordance with the terms of, and are subject to the limits contained in, the Company's existing policy.

The Committee may however, in connection with an external recruitment, offer additional cash and/or share-based elements intended to compensate the individual for the forfeiture of any awards under variable remuneration schemes with a former employer. The design of these payments would appropriately reflect the value, nature, time horizons and performance requirements attaching to the remuneration foregone. Shareholders will be informed of any such arrangements at the time of appointment.

Where an individual is appointed to the Board, different performance measures may be set for the year of joining the Board for the annual bonus, taking into account the individual's role and responsibilities and the point in the year the executive joined.

For an internal appointment, any variable pay element awarded in respect of the prior role may be allowed to pay out according to its terms, adjusted as relevant to take into account the appointment.

#### Non-Executive Directors

On the appointment of a new Chairman or Non-Executive Director, the fees will be set taking into account the experience and calibre of the individual. Where specific cash or share arrangements are delivered to Non-Executive Directors, these will not include share options or other performance-related elements.

### Executive Directors' service contracts

The current Executive Directors' service contracts contain the key terms shown in the table below:

Provision	Detailed terms
Remuneration	<ul style="list-style-type: none"><li>- Salary, pension and benefits.</li><li>- Company car or cash allowance.</li><li>- Permanent health insurance.</li><li>- Private health insurance for director and dependents.</li><li>- Death-in-service benefits.</li><li>- 30 days' paid annual leave.</li><li>- Participation in annual bonus plan, subject to plan rules.</li><li>- Participation in LTIP and SIP, subject to plan rules.</li></ul>
Notice period <sup>(1)</sup>	<ul style="list-style-type: none"><li>- 12 months' notice by the director or by the Company.</li></ul>
Termination payment	<ul style="list-style-type: none"><li>- See separate disclosure below.</li></ul>
Restrictive covenants	<ul style="list-style-type: none"><li>- During employment and for 12 months after leaving.</li></ul>

Note:

(1) The Committee believes that this policy on notice periods provides an appropriate balance between the need to retain the services of key individuals who will benefit the business and the need to limit the potential liabilities of the Company in the event of termination.

The Executive Directors' service contracts are available for inspection, on request, at the Company's registered office.

## Directors' Remuneration Report

### Continued

#### Exit payment policy for Executive Directors

As explained in last year's report, the Company's policies and practices relating to the termination provisions contained in the service contracts of current and future Executive Directors was reviewed and significantly amended during the year ending 31 December 2012.

Executive Directors' contracts allow for termination with contractual notice from the Company or termination with a payment in lieu of notice, at the Company's discretion. The contracts also allow for phased payments to be made on termination with an obligation on the individual to mitigate loss. Neither notice nor a payment in lieu of notice will be given in the event of gross misconduct. The Committee's approach when considering payments in the event of termination is to take account of the individual circumstances including the reason for termination and the contractual obligations of both parties as well as the relevant share plan and pension scheme rules.

In the event of termination by the Company, an Executive Director would be entitled to receive an amount representing base salary and the value of benefits and pension contributions due under the individual's service contract for the notice period. Directors are not entitled to participate in any additional redundancy scheme.

On termination of employment, the Committee has discretion as to the amount of bonus payable in respect of the current year. The bonus paid would reflect the Company's and the individual's performance during that period. However, any bonus payable on termination would not exceed a pro-rated amount to reflect the period for which the individual had worked in the relevant year.

As a general rule, if an Executive Director ceases employment, all unvested awards granted pursuant to the Company's long-term incentive arrangements will lapse immediately. However, if such cessation occurs by reason of death, injury, permanent disability or redundancy, or because the individual's employing company or part of the business in which he/she is employed is transferred out of the Group, or in any other exceptional circumstances determined by the Committee (in each case, a "good leaver"), those awards will not lapse and will continue to vest at the end of the original performance period but only if, and to the extent that, the applicable performance conditions are satisfied. It is the Remuneration Committee's normal policy to time pro-rate any awards held by such a good leaver, although it retains the discretion to refrain from doing so in exceptional circumstances.

On a change of control of the Company resulting in the termination of a director's employment, each of the existing Executive Directors is entitled to compensation of a sum equal to his/her annual basic salary as at the date of termination of employment. As noted and explained in last year's report, the Committee recognises that this provision is no longer in accordance with best practice, and it will not be included in the contracts of future appointees to the Board; however, it continues to apply to the existing Executive Directors.

#### Executive Director board appointments with other companies

The Board believes, in principle, in the benefits of Executive Directors accepting positions as non-executive directors of other companies in order to widen their skills and knowledge for the benefit of the Company, provided that the time commitments involved are not unduly onerous. The Executive Directors are permitted to retain any fees paid for such appointments.

The appointment of any Executive Director to a non-executive position with another company must be approved by the Nomination Committee. In the case of a proposed appointment to a company within the oil and gas industry, permission will only normally be given if the two companies do not compete in the same geographical area.

#### Non-Executive Directors' letters of appointment

None of the Non-Executive Directors nor the Chairman has a service contract but all have letters of appointment that set out their duties and responsibilities, the time commitment expected by the Company and the basis on which their fees will be paid. These letters of appointment can be terminated with immediate effect by either the director concerned or the Company and are subject to the Company's Articles of Association, which provide for the annual election or re-election by shareholders of all of the Company's directors. There are no provisions for compensation payable on termination of appointment.

None of the Non-Executive Directors nor the Chairman participates in any of the Company's share schemes and they are not entitled to a bonus or pension contributions.

The Non-Executive Directors' letters of appointment are available for inspection, on request, at the Company's registered office.

# Directors' Remuneration Report

## Continued

### Part 3 – Annual Report on Remuneration

#### Introduction

This Annual Report on Remuneration provides details of the way in which the Committee operated during the financial year to 31 December 2013 and explains how Cairn's remuneration policy applicable to that period was implemented. It also summarises how the Directors' Remuneration Policy set out on pages 82 to 89 will be applied in 2014.

In accordance with the Regulations, this part of the report will be subject to an advisory vote at the forthcoming AGM on 15 May 2014.

The Company's auditors are required to report to Cairn's shareholders on the "auditable parts" of this Annual Report on Remuneration (which have been highlighted as such below) and to state whether, in their opinion, those parts have been properly prepared in accordance with the Regulations and the Companies Act 2006.

#### Operation of the Remuneration Committee during 2013

##### Members of the Remuneration Committee

The members of the Remuneration Committee during the year (all of whom are independent Non-Executive Directors) were as follows:

- Jackie Sheppard (Chair of the Committee);
- Dr James Buckee;
- Todd Hunt;
- Iain McLaren; and
- Ian Tyler (joined the Committee on 28 June 2013).

The Non-Executive Directors who served on the Committee had no personal financial interest (other than as shareholders) in the matters decided, no potential conflicts of interest from cross-directorships and no day-to-day involvement in running the business. Biographical information on the Committee members is shown on pages 62 and 63 and details of attendance at the Committee's meetings during 2013 are shown on page 71.

##### Internal assistance provided to the Committee

The Chief Executive is not a member of the Remuneration Committee but may attend its meetings by invitation and is consulted in respect of certain of its proposals. Similarly, the Managing Director & Chief Financial Officer is not a member of the Committee but may occasionally be invited to attend parts of its meetings to address specific matters. Neither the Chief Executive nor the Managing Director & Chief Financial Officer is consulted or involved in any discussions in respect of their own remuneration. During the year, the Committee also received material assistance and advice on remuneration policy from the Group's Reward & Benefits Specialist.

##### External assistance provided to the Committee

As and when the Remuneration Committee considers it appropriate, it takes external advice on remuneration from a number of sources. During the year, it received the following assistance:

Adviser	Assistance provided to the Committee during 2013	Fees for Committee assistance in 2013 <sup>1</sup>	Other services provided to the Company during 2013
New Bridge Street <sup>2</sup>	Appointed by the Committee to provide periodic advice on various aspects of the directors' remuneration packages.	£121,451	None
Slaughter and May	Appointed by the Committee to provide advice in relation to the Executive Directors' service contracts and other matters relating to their remuneration arrangements.	£41,676	None
Ernst & Young LLP	In their capacity as Group auditors in the period to 12 April 2013, Ernst & Young carried out an independent verification of the Company's achievement against performance conditions applicable to the Company's LTIP and share option schemes. However, they provided no advice to the Committee.	N/A	Audit services in the period to 12 April 2013.
Shepherd and Wedderburn LLP	Appointed by the Company to carry out regular calculations in relation to the LTIP performance conditions. Also assisted with the preparation of the Directors' Remuneration Report.	£34,700	General legal services to the Group throughout the year.

#### Notes:

- (1) The bases for charging the fees set out in the above table were agreed by the Committee at or around the time the particular services were provided and, in general, reflected the time spent by the adviser in question on the relevant matter.
- (2) "New Bridge Street" is a trading name of Aon Hewitt Limited, part of Aon plc – they are a member of the Remuneration Consultants Group and their work is governed by the Code of Conduct in relation to executive remuneration consulting in the UK.
- (3) The Committee reviews the performance and independence of all its advisers on an annual basis.

# Directors' Remuneration Report

## Continued

### Statement of shareholder voting on 2012 Directors' Remuneration Report

The table below shows the voting outcome at the 16 May 2013 AGM for the 2012 Directors' Remuneration Report.

Number of votes "For" & "Discretionary"	% of votes cast	Number of votes "Against"	% of votes cast	Total number of votes cast	Number of votes "Withheld" <sup>(1)</sup>
394,387,230	99.51%	1,942,770	0.49%	396,330,000	26,051,362

Notes:

(1) A vote withheld is not a vote in law.

99.51% of the votes cast were for the approval of the 2012 Directors' Remuneration Report, with 0.49% against. The Committee welcomed the endorsement of the report shown by the vast majority of shareholders and took steps, wherever practicable, to understand the concerns of investors whose support was withheld.

### Single total figure table for 2013 (audited)

The tables below set out the remuneration received by the Executive Directors and Non-Executive Directors during the year in the following categories.



### Executive Directors

	Financial year	Fixed elements of pay				Pay for performance			Total remuneration	
		Salary and fees	Benefits <sup>(1)</sup>	Pension <sup>(2)</sup>	SIP <sup>(3)</sup>	Fixed element subtotal	Bonus <sup>(4)</sup>	Long-term incentives <sup>(5)</sup>		Performance element subtotal
Simon Thomson	2013	£525,000	£22,269	£78,750	£5,996	£632,015	£330,750	-	£330,750	£962,765
	2012	£494,000	£17,983	£74,100	£6,000	£592,083	£426,487	-	£426,487	£1,018,570
Jann Brown	2013	£427,000	£22,688	£64,050	£5,996	£519,734	£264,740	-	£264,740	£784,474
	2012	£416,000	£22,500	£62,400	£6,000	£506,900	£352,214	-	£352,214	£859,114
Dr Mike Watts	2013	£464,000	£11,497	£69,600	£5,996	£551,093	£285,360	-	£285,360	£836,453
	2012	£452,000	£11,707	£67,800	£6,000	£537,507	£382,694	-	£382,694	£920,201

Notes:

- (1) Taxable benefits available to the Executive Directors during 2013 were a company car/car allowance, private health insurance and, in the case of all of the Executive Directors other than Dr Mike Watts, a gym and fitness allowance. This package of taxable benefits was unchanged from 2012.
- (2) Additional disclosures relating to the pension provision for the Executive Directors during 2013 are set out on page 86.
- (3) This column shows the face value (at date of award) of matching and free shares provided to the Executive Directors under the SIP during the relevant period. Further details on the way in which the SIP was operated during 2013 are set out on page 85.
- (4) This column shows the amount of bonus paid or payable in respect of the year in question. Further information in relation to the annual bonus for 2013 is provided on page 84.
- (5) This column shows the value of shares that vested in respect of LTIP awards with performance conditions that ended during the period in question. Further details of the LTIP's operation during 2013 are provided on page 85.
- (6) Following the end of the year to 31 December 2013, the Committee considered whether there were any circumstances that could or should result in the recovery or withholding of any sums pursuant to the clawback arrangements contained within the Company's remuneration policy. The conclusion reached by the Committee was that it was unaware of any such circumstances.

### Non-Executive Directors

	Financial year	Fixed elements of pay				Pay for performance			Total remuneration
		Salary and fees	Benefits	Pension	Fixed element subtotal	Bonus	Long-term incentives	Performance element subtotal	
Sir Bill Gammell	2013	£236,000	-	-	£236,000	-	-	-	£236,000
	2012	£226,971	-	-	£226,971	-	-	-	£226,971
Todd Hunt	2013	£72,000	-	-	£72,000	-	-	-	£72,000
	2012	£70,000	-	-	£70,000	-	-	-	£70,000
Iain McLaren	2013	£82,000	-	-	£82,000	-	-	-	£82,000
	2012	£80,000	-	-	£80,000	-	-	-	£80,000
Dr James Buckee	2013	£72,000	-	-	£72,000	-	-	-	£72,000
	2012	£71,743	-	-	£71,743	-	-	-	£71,743
Alexander Berger	2013	£72,000	-	-	£72,000	-	-	-	£72,000
	2012	£70,000	-	-	£70,000	-	-	-	£70,000
Jackie Sheppard	2013	£82,000	-	-	£82,000	-	-	-	£82,000
	2012	£78,257	-	-	£78,257	-	-	-	£78,257
Ian Tyler <sup>(3)</sup>	2013	£36,277	-	-	£36,277	-	-	-	£36,277
	2012	£0	-	-	£0	-	-	-	£0

Notes:

- (1) The annual fee for each of the Non-Executive Directors (other than the Chairman) for 2013 was £72,000. In addition, a further annual fee of £10,000 was payable to both Iain McLaren and M. Jackie Sheppard QC for their roles as chair of the Audit Committee and the Remuneration Committee respectively.
- (2) The Non-Executive Directors do not participate in any of the Company's long-term incentive arrangements and are not entitled to a bonus or pension contributions.
- (3) Ian Tyler was appointed a director on 28 June 2013 and his fees for 2013 reflect the period from that date to the year end.

# Directors' Remuneration Report

Continued

## TSR performance graph and further information on Chief Executive pay

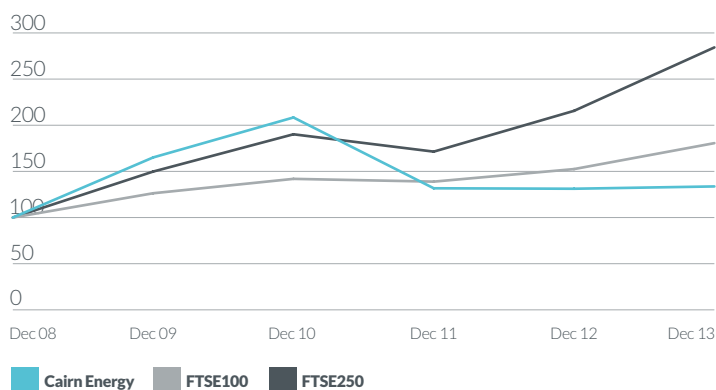
### Introduction

The following chart demonstrates the growth in value of a £100 investment in the Company and an investment of the same amount in both the FTSE 250 Index and the FTSE 100 Index over the last five years. These comparisons have been chosen on the basis that Cairn was a constituent member of the FTSE 250 Index for the whole of 2013 but has also previously been a constituent member of the FTSE 100 Index.

The table beneath the graph illustrates the movements in the total remuneration of the Company's Chief Executive during the same five-year period.

### Performance Graph –

#### Comparison of five-year cumulative TSR on an investment of £100



### Total remuneration of Chief Executive during the same five-year period

Financial year	Chief Executive	Total remuneration of Chief Executive <sup>(1)</sup>	Annual variable element award rates for Chief Executive (as % of max. opportunity)	Long-term incentive vesting rates for Chief Executive (as % of max. opportunity)
2013	Simon Thomson	£962,765	63%	0%
2012	Simon Thomson	£1,018,570	86%	0%
2011	Simon Thomson	£3,405,719	82%	121%
2011 <sup>(2)</sup>	Sir Bill Gammell	£4,053,822	N/A	106%
2010	Sir Bill Gammell	£7,302,533	58%	113%
2009	Sir Bill Gammell	£962,757	54%	0%

Notes:

- The amounts shown in this column have been calculated using the same methodology prescribed by the Regulations for the purposes of preparing the single total figure table shown on page 91.
- Sir Bill Gammell stood down as Chief Executive on 30 June 2011 and was replaced by Simon Thomson (who had previously been Legal and Commercial Director) with effect from that date. Sir Bill Gammell's "total remuneration" for 2011 shown in the above table reflects the amount of salary, benefits and pension paid to him in respect of the period to 30 June 2011. However, during the year to 31 December 2011, Sir Bill Gammell also received, in connection with the termination of his employment and in settlement of his contractual entitlements, a payment of salary and benefits in lieu of his contractual notice period of one year (£770,000) and a cash bonus under the Company's annual cash bonus scheme (£625,000).

### Percentage annual change in Chief Executive's remuneration elements compared to all Group employees

The table below illustrates, for various elements of the Chief Executive's 2013 remuneration package, the percentage change from 2012 and compares it to the average percentage change for all the Group's employees in respect of that same period.

	% change in base salary	% change in taxable benefits <sup>(1)</sup>	% change in annual bonus
Chief Executive	6.3%	24%	22% reduction
All Group employees	4.4%	38%	16% reduction

Note:

- The increase in the Chief Executive's taxable benefits arose as a result of changes made to his company car provision following his appointment. In the case of the figure for "All Group employees", the increase was largely attributable to higher levels of international relocations during the period.

### Executive Directors' base salaries during 2013

Based on a review carried out in December 2012, the following salary increases for Executive Directors became effective on 1 January 2013:

#### 2013 Salary details (Executive Directors)

Executive Director	Job title	Salary as at 31 December 2012	Salary as at 1 January 2013	% increase with effect from 1 January 2013
Simon Thomson	Chief Executive	£494,000	£525,000	6.3%
Jann Brown	Managing Director & CFO	£416,000	£427,000	2.6%
Dr Mike Watts	Deputy Chief Executive	£452,000	£464,000	2.7%

The above increases for Jann Brown and Dr Mike Watts were consistent with the level of standard annual salary increase awarded to other employees on 1 January 2013. As explained in last year's Directors' Remuneration Report, Simon Thomson's rise in 2013 salary reflected the Committee's view of his progress in his new role of Chief Executive.

## Directors' Remuneration Report

### Continued

#### Executive Directors' pension provision during 2013 (audited)

As highlighted in the Directors' Remuneration Policy set out on pages 82 to 89, the Company operates a defined contribution, non-contributory group personal pension plan which is open to all UK permanent employees. The Company contributes 10% of basic annual salary (15% in respect of senior executives) on behalf of all qualifying employees. The Company also has a pension committee which meets on a regular basis to assess the performance and suitability of the Company's pension arrangements.

For the majority of the year, Jann Brown was a member of the Company scheme, but subsequently she established her own individual personal pension plan. The aggregate Company contributions to these arrangements during 2013 amounted to 15% of her annual basic salary.

During the year, Dr Mike Watts received an amount equivalent to 15% of his annual basic salary in the form of additional salary, as his pension arrangements are fully funded.

Simon Thomson has an individual personal pension plan and, during 2013, received a contribution from the Company equal to 15% of his annual basic salary.

Details of the actual amounts of pension contributions/additional salary that were paid to the Executive Directors during 2013 are set out in the "pension" column of the single total figure table on page 91.

Finally, the Company is also the principal employer for a Small Self-Administered Scheme. Sir Bill Gammell is the sole member of this scheme. The Company is not contractually obliged to make any contributions into this arrangement on behalf of Sir Bill Gammell and did not do so during the year.

#### Annual bonus – 2013 structure and outcome (audited)

During 2013, Cairn operated annual cash bonus schemes for all employees and Executive Directors.

For all participants, as in prior years, bonus awards were based on individual and Company performance measures. Individual performance was measured through the Company's performance management system and Company performance conditions were based on annually defined KPIs. Taking into account commercial sensitivities around disclosure, a summary of the relevant targets and ascribed weightings is set out below.

The maximum level of bonus award for the Executive Directors and certain PDMRs for 2013 was 100% of annual salary (as at date of award). As highlighted below, 90% of each Executive Director's bonus opportunity for 2013 was based on performance against certain Group KPIs, with the remaining 10% dependent on the satisfaction of personal performance objectives.

#### 2013 Annual Cash Bonus Scheme – Group KPI performance conditions and achievement levels (max. 90% of total bonus)

Performance measures	Measures and weightings		Performance achieved in 2013	
	Performance targets	Weighting (as % of maximum opportunity)	Bonus awarded (as % of maximum opportunity)	Summary of achievement
Delivery of exploration and appraisal performance	Finding costs efficiency and targeted risked resources.	45%	22.5%	Four high impact prospects matured for drilling in 2014. E&A drilling was relatively disappointing versus targets.
Resource maturity	Conversion of 2C resources to 2P reserves through developments.	13.5%	6.75%	2P reserves booked for Kraken development; Catcher still progressing towards sanction at year end.
Capital Expenditure	Reduce Group capex exposure in non-core projects.	4.5%	2.7%	Mariner divestment successfully completed.
Balance Sheet/Office Costs	Retain balance sheet strength and control office costs.	4.5%	4.5%	Liquid reserves maintained. Gross controllable office costs within approved budget.
HSE/Licence to Operate	Maintain licence to operate by achieving targets for several leading HSE performance indicators.	13.5%	10.35%	Good performance against almost all the leading targets; lagging indicators less successful.
Work Programme	Delivery of approved 2013 work programme.	9%	7.2%	Drilling operations and seismic and environmental/baseline surveys conducted safely and on budget in Greenland, Morocco & Senegal.
Totals		90%	54%	

# Directors' Remuneration Report

## Continued

### 2013 Annual Cash Bonus Scheme – Individual performance conditions and achievement levels (max. 10% of total bonus)

Each Executive Director was given a number of different personal objectives tailored to their role and the needs of the business for the year. The precise objectives are considered commercially sensitive, but in summary they included the creation and execution of our strategy and its communication to stakeholders, risk management, financial planning, internal controls, people management, health & safety and governance.

The achievements against the above objectives were carefully considered by the Committee following which it awarded each Executive Director between 7.5% and 9% of salary out of a maximum of 10%, as set out below.

### 2013 Annual Cash Bonus Scheme – Actual payments awarded (Executive Directors)

Executive Director	Award (as % of salary) based on achievement against performance measures relating to:		Actual amount of bonus
	Group KPIs	Individual performance	
Simon Thomson	54%	9%	£330,750
Jann Brown	54%	8%	£264,740
Dr Mike Watts	54%	7.5%	£285,360

#### Notes:

- The above bonuses were paid in cash to the directors in question shortly after determination by the Remuneration Committee. No part of the awards was deferred.
- As explained in the Directors' Remuneration Policy, these bonuses may be subject to clawback where, in the period of three years from the end of the 2013 financial year, the Committee becomes aware of a material misstatement of the Company's financial results or an error in the calculation of performance targets.

The Remuneration Committee considered that the above award levels were appropriately reflective of overall performance during the year.

### Long-term incentives during 2013

#### Introduction

During the year to 31 December 2013, the Executive Directors participated in the Cairn Energy PLC Long Term Incentive Plan (2009) (the "LTIP"), which was originally approved by shareholders at the AGM held on 19 May 2009.

The LTIP enables selected senior individuals to be granted conditional awards or nil-cost options over ordinary shares, the vesting of which is normally dependent on both continued employment with the Group and the extent to which pre-determined performance conditions are met over a specified period of three years.

In the case of all awards under the LTIP (including those granted during 2010, 2011, 2012 and 2013), the performance conditions involve a comparison of the TSR of the Company over a three-year performance period (commencing on the date of grant of the relevant award) with the TSR of a share in each company in a comparator group. At the end of this period, each company in the comparator group is listed in order of TSR performance to produce a "ranking table". The vesting of awards then takes place as follows:

Ranking of Company against the comparator group	Percentage of ordinary shares comprised in award that vest
Below median	0%
Median	20%
Upper decile (i.e. top 10%)	100%
Between median and upper decile	20%–100% on a straight line basis

A list of the companies comprised in the comparator groups applicable to all LTIP awards that were outstanding during 2013 is set out on page 96.

In order to ensure that the LTIP encourages and rewards exceptional performance in terms of delivering increased growth and shareholder value, the performance conditions attaching to awards also provide that, where the TSR of the Company produces a ranking at or above the upper decile level in the appropriate comparator group, a participant will then be given the opportunity to increase the percentage of his/her award that vests through the application of a "multiplier" that is linked to the TSR actually achieved over the performance period. The way in which this multiplier operates is as follows:

Multiplier applied to determine the number of ordinary shares that actually vest	TSR of the Company over the performance period
1	50% or less
1.33	100% or more
1–1.33 on a straight line basis	Between 50% and 100%

However, notwithstanding the performance of the Company against the above targets, no part of any award will vest unless the Remuneration Committee is satisfied that there has been an overall satisfactory and sustained improvement in the performance of the Company as a whole over the performance period. In addition, and as noted in the Directors' Remuneration Policy, awards granted in 2012 and later years are subject to clawback provisions which may be operated by the Committee where, in the period of three years from the end of the applicable performance period, it becomes aware of either a material misstatement of the Company's financial results or an error in the calculation of performance metrics.

On any vesting of an award under the LTIP, only 50% of the ordinary shares to which the holder has become entitled are released/become exercisable immediately, with the remaining 50% normally being released/becoming exercisable after a further period of one year.



## Directors' Remuneration Report

### Continued

#### LTIP – Awards granted during 2013 (audited)

On 20 March 2013, the following awards under the LTIP were granted to Executive Directors:

Executive Director	Type of award	Basis of award granted	Share price at date of grant	No. of shares over which award originally granted	% of shares over which award originally granted that vest at threshold	Face value (£,000) of ...		Vesting determined by performance over
						...shares over which award originally granted <sup>(3)</sup>	...max. no. of shares to vest if all performance measures met <sup>(4)</sup>	
Simon Thomson	Nil-cost option	3 times salary of £525,000	£2.784	565,732	20%	£1,575	£2,095	
Jann Brown	Nil-cost option	3 times salary of £427,000	£2.784	460,129	20%	£1,281	£1,704	3 years until 19 March 2016
Dr Mike Watts	Nil-cost option	3 times salary of £464,000	£2.784	500,000	20%	£1,392	£1,851	

Notes:

- (1) Details of the performance conditions applicable to the awards granted in 2013 are provided on page 94.
- (2) No price is payable by participants for their shares on the exercise of a nil-cost option granted under the LTIP.
- (3) The values shown in this column have been calculated by multiplying the "number of shares over which the award was originally granted" by the "share price at date of grant" (being, for these purposes, the closing mid-market price of a share in the Company on the day immediately preceding the date of its grant).
- (4) The values shown in this column have been calculated by multiplying the "number of shares over which the award was originally granted" by 133% (being the vesting percentage that would apply on full satisfaction of all performance conditions to which the awards are subject – see page 94) and multiplying the result by the "share price at date of grant" (being, for these purposes, the closing mid-market price of a share in the Company on the day immediately preceding the date of its grant).

#### LTIP – Awards vesting during the year (audited)

On 25 March 2013, the three-year performance period applicable to the awards granted under the LTIP on 26 March 2010 to various participants (including the Executive Directors) came to an end. Thereafter, the Remuneration Committee assessed the relevant performance conditions. The results of this assessment can be summarised as follows:

Performance measure	% of award subject to measure	Performance achieved 2010–2013	% of award vested
Relative TSR performance against a comparator group of 18 companies with the opportunity for additional multiplier of up to 1.33 to be applied for upper decile performance.	100%	Cairn's TSR over the period ranked below the median company in the comparator group.	0%

Notes:

- (1) Further details of the performance conditions that applied to the above awards are set out on page 94.
- (2) At various points in the period 26 March 2010 to 25 March 2013, the Committee was required to determine the treatment of those comparator group companies that were the subject of takeover transactions. No other discretions were exercised by the Remuneration Committee during or after the relevant performance period.
- (3) The calculations used to inform the Committee's determinations in relation to the above awards were independently verified by Ernst & Young LLP.

#### LTIP – Other awards held by the Executive Directors during the year

For the sake of completeness, and in order to allow comparisons to be made with the awards granted under the LTIP during 2013, set out below are details of the other entitlements under the Plan that were held by the Executive Directors during the year:

Executive Director	Date of grant	Type of award <sup>(2)</sup>	Basis of award granted	Share price at date of grant	No. of shares over which award originally granted	% of shares over which award originally granted that vest at threshold	Face value (£,000) of ...		Vesting determined by performance over three years until...
							...shares over which award originally granted <sup>(3)</sup>	...max. no. of shares to vest if all performance measures met <sup>(4)</sup>	
Simon Thomson	17 June 2011	Nil-cost option	3.5 times salary of £375,000	£4.033	325,440	20%	£1,312	£1,746	16 June 2014
	14 June 2012	Nil-cost option	3 times salary of £494,000	£2.887	513,335	20%	£1,482	£1,971	13 June 2015
Jann Brown	17 June 2011	Nil-cost option	3.5 times salary of £375,000	£4.033	325,440	20%	£1,312	£1,746	16 June 2014
	14 June 2012	Nil-cost option	3 times salary of £416,000	£2.887	432,282	20%	£1,248	£1,660	13 June 2015
Dr Mike Watts	17 June 2011	Nil-cost option	3.5 times salary of £435,000	£4.033	377,510	20%	£1,522	£2,025	16 June 2014
	14 June 2012	Nil-cost option	3 times salary of £452,000	£2.887	469,691	20%	£1,356	£1,803	13 June 2015

Notes:

- (1) Further details of the performance conditions that apply to these awards are set out on page 94.
- (2) The awards shown in the above table were originally made in the form of conditional shares. However, to provide flexibility to participants, they have been converted into nil-cost options.
- (3) The values shown in this column have been calculated by multiplying the relevant "number of shares over which the award was originally granted" by the appropriate "share price at date of grant" (being, for these purposes, the closing mid-market price of a share in the Company on the day immediately preceding the date of its grant).
- (4) The values shown in this column have been calculated by multiplying the relevant "number of shares over which the award was originally granted" by 133% (being the vesting percentage that would apply on full satisfaction of all performance conditions to which the awards are subject – see page 94) and multiplying the result by the appropriate "share price at date of grant" (being, for these purposes, the closing mid-market price of a share in the Company on the day immediately preceding the date of its grant).

# Directors' Remuneration Report

## Continued

### Comparator group companies applicable to LTIP awards

The table below provides details of the comparator groups applicable to each tranche of awards granted under the LTIP that were outstanding during 2013.

Company	Comparator group applicable to LTIP awards granted on....			
	26 March 2010	17 June 2011	14 June 2012	20 March 2013
Afren PLC		✓	✓	✓
BG Group PLC	✓	✓	✓	✓
Bharat Petroleum Corporation Limited	✓	✓		
Chesapeake Energy Corporation	✓			
CNOOC Limited	✓			
Dana Petroleum PLC*	✓			
DNO ASA		✓	✓	✓
EnQuest PLC		✓	✓	✓
EOG Resources, Inc	✓	✓		
Faroe Petroleum PLC			✓	✓
Genel Energy PLC			✓	✓
Hindustan Petroleum Corporation Limited	✓			
Indian Oil Corporation Limited	✓			
JKX Oil & Gas PLC		✓	✓	✓
Lundin Petroleum AB			✓	✓
Melrose Resources PLC*		✓		
Newfield Exploration Company	✓	✓		
Niko Resources Limited			✓	✓
Noble Energy, Inc	✓	✓		
Oil and Natural Gas Corporation Limited	✓	✓		
Ophir Energy PLC			✓	✓
Petroceltic International PLC			✓	✓
PTT Exploration & Production PLC	✓			
Premier Oil PLC	✓	✓	✓	✓
Rockhopper Exploration PLC			✓	✓
Salamander Energy PLC		✓	✓	✓
Santos Limited	✓	✓	✓	✓
SOCO International plc	✓		✓	✓
Talisman Energy, Inc	✓	✓	✓	✓
Tullow Oil PLC	✓	✓	✓	✓
Woodside Petroleum Limited	✓	✓		

\* Denotes companies that have delisted during the applicable performance period.

### Participation of Executive Directors in all-employee share schemes during 2013

#### Introduction

In order to encourage increased levels of long-term share ownership amongst its general employee population, the Company launched an HM Revenue and Customs approved share incentive plan ("SIP") in April 2010. The SIP provides eligible employees, including the Executive Directors, with the following benefits:

- "Partnership shares" - employees can authorise deductions of up to £1,500 (£1,800 with effect from 6 April 2014) per tax year from pre-tax salary, which are then used to acquire ordinary shares on their behalf.
- "Matching shares" - the Company can award further free shares to all participants who acquire partnership shares on the basis of up to two matching shares for every one partnership share purchased. For the tax year 2013/2014, the Company awarded two matching shares for every one partnership share purchased and intends to continue using this award ratio for the tax year 2014/2015.
- "Free shares" - employees can be given up to £3,000 (£3,600 with effect from 6 April 2014) worth of ordinary shares free in each tax year. On 9 June 2013, an award of free shares was made to employees, including the Executive Directors.

As the SIP is an "all-employee" arrangement, no performance conditions are imposed in relation to any matching or free shares awarded pursuant to its terms.

## Directors' Remuneration Report

### Continued

#### Details of Executive Directors' SIP participation in 2013

Details of the shares purchased by and awarded to the Executive Directors under the SIP during the course of the year are as follows:

Executive Director	Total SIP shares held at 1 January 2013	Free shares awarded on 9 April 2013 at a price of £2.82 per share	Partnership shares awarded on 7 May 2013 at a price of £2.845 per share	Matching shares awarded on 7 May 2013 at a price of £2.845 per share	Total SIP shares held at 31 December 2013
Simon Thomson	4,117	1,063	527	1,054	6,761
Jann Brown	4,117	1,063	527	1,054	6,761
Dr Mike Watts	4,117	1,063	527	1,054	6,761

The total number of shares held by each of the current Executive Directors under the SIP is included in their beneficial shareholdings disclosed in the directors' report on page 64.

#### Shareholding guidelines for Directors (audited)

The Committee believes that a significant level of shareholding by the Executive Directors strengthens the alignment of their interests with those of shareholders. Accordingly, a formal share ownership policy is in place under which the Executive Directors are required to build up and maintain a target holding equal to 100% of base salary. The policy also provides that, until such a holding is achieved, an Executive Director is obliged to retain shares with a value equal to 50% of the net-of-tax gain arising from any vesting or exercise under the Company's share incentive plans.

The following table discloses the beneficial interest of each director in the ordinary shares of the Company as at 31 December 2013 and, in the case of the Executive Directors, highlights the extent to which the above shareholding guidelines were satisfied as at that date.

	Ordinary shares	Ordinary shares held in the SIP <sup>(2)</sup>	Total holding of ordinary shares	Value of holding as a % of salary on 1 January 2014 <sup>(3)</sup>	Ordinary shares subject to outstanding unvested awards under the LTIP <sup>(4)</sup>	Total interest in ordinary shares
<b>Executive</b>						
Simon Thomson	380,622	6,761	387,383	195%	1,404,507	1,791,890
Jann Brown	288,789	6,761	295,550	183%	1,217,851	1,513,401
Dr Mike Watts	1,158,171	6,761	1,164,932	665%	1,347,201	2,512,133
<b>Non-Executive</b>						
Sir Bill Gammell	596,331	–	596,331	–	–	596,331
Todd Hunt	72,012	–	72,012	–	–	72,012
Iain McLaren	7,878	–	7,878	–	–	7,878
Dr James Buckee	37,788	–	37,788	–	–	37,788
Alexander Berger	10,979	–	10,979	–	–	10,979
Jackie Sheppard	0	–	0	–	–	0
Ian Tyler	0	–	0	–	–	0
	<b>2,552,570</b>	<b>20,283</b>	<b>2,572,853</b>		<b>3,969,559</b>	<b>6,542,412</b>

#### Notes:

- (1) Details of the Company's share ownership policy for Executive Directors are set out above.
- (2) Under the rules of the SIP, certain shares awarded to participants must be retained in the plan for a specified "holding period" of up to five years. The receipt of these shares is not subject to the satisfaction of performance conditions.
- (3) Share price used is the average share price over the period of 90 days ending on 1 January 2014.
- (4) This column shows all unvested and outstanding awards under the LTIP that were held by the Executive Director concerned as at 31 December 2013 (i.e. including those granted during the year). Details of these entitlements, the vesting of which is subject to the satisfaction of performance conditions, are set out on page 94.

#### Dilution of share capital pursuant to share plans during 2013

In any ten-year rolling period, the number of ordinary shares which may be issued in connection with the Company's discretionary share plans cannot exceed 5% of the Company's issued ordinary share capital.

In addition, in any ten-year rolling period, the number of ordinary shares which may be issued in connection with all of the Company's employee share schemes (whether discretionary or otherwise) cannot exceed 10% of the Company's issued ordinary share capital.

For the purposes of operating both the above limits, the number of shares issued prior to 6 February 2012 in connection with options and awards is adjusted to reflect the share capital consolidation which became effective on that date.

It should also be noted that all shares acquired by or awarded to participants under the SIP are existing ordinary shares purchased in the market. As a result, the SIP does not involve the issue of new shares or the transfer of treasury shares.

# Directors' Remuneration Report

Continued

## Board appointments with other companies during 2013

Certain of the Company's Executive Directors serve as Non-Executive Directors on the boards of other companies and are permitted to retain any associated fees. Details of the positions held during 2013 and the fees that were payable are as follows:

Executive Director	Position held	Fees (2013)
Simon Thomson	Non-Executive Director, Graham's The Family Dairy Limited	£30,417
Dr Mike Watts	Non-Executive Director, SOCO International plc	£45,000
Jann Brown	Non-Executive Director, Troy Income & Growth Trust plc	£17,162

## Relative importance of spend on pay

Set out below are details of the amounts of, and percentage change in, remuneration paid to or receivable by all Group employees and distributions to shareholders in the years ended 31 December 2012 and 2013.

	Financial Year 2012	Financial Year 2013	% change
Employee costs (\$m)	\$40.5	\$41.5	2.5%
Distributions (\$m) <sup>(1)</sup>	\$3,575.8	\$36.6	99% reduction

Notes:

- (1) For the purposes of the above table, "Distributions" include amounts distributed to shareholders by way of dividend and share buyback. The figure for 2012 represents the return of cash that took place in February of that year whereas the 2013 amount is comprised of share-buybacks that took place throughout the period.
- (2) Employee costs exclude employers' tax and social security costs and share-based payments.

## Implementation of remuneration policy in 2014

The following table provides details of how the Company intends to implement the key elements of the Directors' Remuneration Policy set out on pages 82 to 89 during the year to 31 December 2014.

Remuneration element	Implementation during 2014
<b>Base salary</b>	Each of the Executive Directors received a 2.5% increase in base salary on 1 January 2014 – this was in line with the standard annual increase awarded to other employees on that date. After applying this increase, details of the base salaries payable to each of the current Executive Directors for the year to 31 December 2014 are as follows: <ul style="list-style-type: none"> <li>– Simon Thomson, Chief Executive – £538,125;</li> <li>– Jann Brown, Managing Director &amp; CFO – £437,675; and</li> <li>– Dr Mike Watts, Deputy Chief Executive – £475,600.</li> </ul>
<b>Benefits</b>	Executive Directors will continue to receive the same benefits as in 2013.
<b>Annual bonus</b>	In accordance with the requirements of the policy, Executive Directors will be eligible to receive a bonus of up to 100% of base salary depending on the extent to which specified measures are satisfied over the year. All of the Chief Executive's 2014 bonus opportunity will be based on the demanding Group KPIs described below (with details of the weighting specified in brackets): <ul style="list-style-type: none"> <li>– exploration and new ventures (45%);</li> <li>– active portfolio optimisation (15%);</li> <li>– retain balance sheet strength (5%);</li> <li>– maintain licence to operate (15%); and</li> <li>– operational excellence (20%).</li> </ul> <p>In the case of the Deputy Chief Executive and of the Managing Director &amp; CFO, 90% of their 2014 bonus opportunity will be based on the same Group KPIs (and weightings) set out above. The remaining 10% will be determined by reference to the achievement of personal objectives.</p> <p>The specific targets to be used for the purposes of the 2014 bonus scheme are commercially sensitive and have not, therefore, been set out in detail above. However, appropriate disclosures in relation to the 2014 bonus scheme will be included in next year's Annual Report on Remuneration.</p>
<b>Long Term Incentive Plan</b>	It is intended that, during 2014, the Executive Directors will be granted LTIP awards over shares worth 300% of salary (being the same level as was awarded in 2013). The performance conditions that will determine the vesting of these grants will be unchanged from those that applied to last year's awards (full details of which are set out on page 94 of the Annual Report on Remuneration).
<b>Share Incentive Plan</b>	Executive Directors will be given the opportunity to participate in the SIP on the same terms as apply to all other eligible employees in the arrangement.
<b>Pension</b>	The Company will continue to contribute 15% of basic salary on behalf of Executive Directors or pay them an equivalent amount of additional salary.
<b>Non-Executive Directors' fees</b>	The annual Non-Executive Director fee for 2014 has been increased from £72,000 to £73,800. The additional annual fee for chairing the Audit and/or Remuneration Committees is unchanged at £10,000.
<b>Chairman's fees</b>	At the start of 2014, the annual Chairman's fee for the year was set at £241,900 (compared to £236,000 for 2013). However, this fee was subsequently reassessed in light of the succession of Ian Tyler to the role and will be £160,000 per annum, commencing at the end of the 2014 AGM.

By Order of the Board

**M. Jacqueline Sheppard QC**

Chair of the Remuneration Committee

17 March 2014

# Independent Auditors' Report to the Members of Cairn Energy PLC

## Report on the financial statements

### Our opinion

In our opinion:

- the financial statements, defined below, give a true and fair view of the state of the Group's and of the Parent Company's affairs as at 31 December 2013 and of the Group's loss and of the Group's and Parent Company's cash flows for the year then ended;
- the Group financial statements have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union;
- the Parent Company financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

This opinion is to be read in the context of what we say in the remainder of this report.

### What we have audited

The Group financial statements and Parent Company financial statements (the "financial statements"), which are prepared by Cairn Energy PLC, comprise:

- the Group and Parent Company balance sheet as at 31 December 2013;
- the Group income statement and statement of comprehensive income for the year then ended;
- the Group and Parent Company statements of changes in equity and statements of cash flows for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies and other explanatory information.

The financial reporting framework that has been applied in their preparation comprises applicable law and IFRSs as adopted by the European Union and, as regards the Parent Company, as applied in accordance with the provisions of the Companies Act 2006.

Certain disclosures required by the financial reporting framework have been presented elsewhere in the Annual Report and Accounts (the "Annual Report"), rather than in the notes to the financial statements. These are cross-referenced from the financial statements and are identified as audited.

### What an audit of financial statements involves

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) ("ISAs (UK & Ireland)"). An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- whether the accounting policies are appropriate to the Group's and Parent Company's circumstances and have been consistently applied and adequately disclosed;
- the reasonableness of significant accounting estimates made by the directors; and
- the overall presentation of the financial statements.

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

### Overview of our audit approach

#### Materiality

We consider an item to be material if, in our judgement, it is likely to impact the economic decisions of the members of Cairn Energy PLC to whom this report is addressed.

We set certain thresholds for materiality. These helped us to determine the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and on the financial statements as a whole.

Based on our professional judgement, we determined materiality for the Group financial statements as a whole to be \$36 million. This represents approximately 1% of total assets, which we consider to be an appropriate measure for an exploration and development Oil and Gas group that does not currently have producing assets.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above \$1.8 million as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

#### Overview of the scope of our audit

The Group is structured in two key operating segments which are further subdivided by geography based on exploration activities: Frontier Exploration – North Atlantic; Frontier Exploration – Africa; Mature Basin – UK and Norwegian North Sea; and Other Cairn Energy Group. The Group financial statements are a consolidation of 166 entities, comprising the group's operating businesses and centralised functions.

In establishing the overall approach to the group audit, we determined the type of work that needed to be performed at the entities by us, as the group engagement team, or component auditors within PwC UK and from other PwC network firms operating under our instruction. Where the work was performed by component auditors, we determined the level of involvement we needed to have in the audit work at those entities to be able to conclude whether sufficient appropriate audit evidence had been obtained as a basis for our opinion on the Group financial statements as a whole.

A large number of the entities were established to hold individual licence interests which in the current period have little or no activity, accordingly we identified that only 6 entities required an audit of their complete financial information due to their size. In addition, specific audit procedures were performed on certain balances and transactions at a further 8 entities.

# Independent Auditors' Report to the Members of Cairn Energy PLC

## Continued

This work gave us coverage of 93% over the Group total assets at 31 December 2013 and, together with the procedures performed at a Group level, including confirming bank balances and goodwill impairment testing, gave us the evidence we needed to form our opinion on the Group financial statements.

### Areas of particular audit focus

In preparing the financial statements, the directors made a number of subjective judgements, for example in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. We primarily focused our work in these areas by assessing the directors' judgements against available evidence, forming our own judgements, and evaluating the disclosures in the financial statements.

In our audit, we tested and examined information, using sampling and other auditing techniques, to the extent we considered necessary to provide a reasonable basis for us to draw conclusions. We obtained audit evidence through testing the effectiveness of controls, substantive procedures or a combination of both.

We considered the following risks, arising from risk of fraud, error and/or judgement, to be those that required particular focus in the current year. This is not a complete list of all risks or areas of focus identified by our audit. We discussed these areas of focus with the Audit Committee. Their report on those matters that they considered to be significant issues in relation to the financial statements is set out on pages 78 to 80.

Risks	Nature of risk		
	Fraud	Error	Judgement
Impairment of exploration/development costs and goodwill	X	X	X
Tax judgements		X	X
Management override of controls	X		

The scope of our audit addressed these risks as follows:

Area of focus	How the scope of our audit addressed the area of focus
<p><b>Impairment of capitalised exploration and development costs and goodwill</b></p> <p>We focused on this area due to the significant value attached to goodwill and capitalised exploration and development costs in the balance sheet. Management are required to make a number of significant judgements in determining the recognition of, and the carrying value of, these assets and in determining whether there are any indicators of impairment.</p> <p>Potential indicators of impairment could include:</p> <ul style="list-style-type: none"> <li>- unsuccessful exploration activities;</li> <li>- falling commodity prices and/or cost escalation;</li> <li>- changing reserves estimates; and</li> <li>- consolidated net assets greater than the market capitalisation of the group.</li> </ul> <p>Refer to Note 2.1 to the financial statements.</p>	<p>We tested management's impairment review of goodwill and capitalised exploration and development costs. Specific work included:</p> <ul style="list-style-type: none"> <li>- comparing the assumptions used within the impairment review model to the approved budgets and business plans and other evidence of future intentions for individual exploration properties;</li> <li>- benchmarking of key assumptions including commodity price and discount rate and inflation;</li> <li>- comparing reserves and production profiles to group approved values or operator estimates;</li> <li>- matching capital and operating expenditure forecasts to group approved or operator estimates;</li> <li>- performing sensitivity analysis over key assumptions in the model in order to assess the potential impact of a range of possible outcomes;</li> <li>- checking the impairment models for mathematical accuracy; and</li> <li>- considering the overall impact on the valuation of our knowledge of Cairn and the industry.</li> </ul>

## Independent Auditors' Report to the Members of Cairn Energy PLC

Continued

### Tax judgements

We focused on this area because:

- Cairn operates in a complex tax environment comprising a number of jurisdictions with specific tax rules relating to oil and gas activities. As a result, management have to make significant judgements regarding current and deferred tax positions; and
- specifically, on 22 January 2014 the Group received a request for information from the Indian tax authorities in respect of amendments introduced in the 2012 Indian Finance Act which seek to tax prior year transactions under legislation applied retrospectively. At the same time the Group received an order not to sell the remaining shares in Cairn India. Management have made judgements in respect of this notification.

Refer to Note 4.3 and 6.1 to the financial statements.

Our assessment of the tax judgements, was made on the basis of:

- our tax knowledge from similar circumstances and past experience;
- our understanding of the Group and the relevant transactions;
- reviewing correspondence with tax authorities and/or evidence from similar precedent; and
- our professional judgement.

In relation to corporate and deferred tax positions:

- we have considered the information available in relation to the Group's open tax positions and assessed the associated level of provisioning;
- we have considered the impact of the Group's future plans and current legislation specifically related to oil and gas on the recognition of deferred tax. In particular, we have assessed the treatment of heavy oil field allowances awarded at the time of Field Development Plan approval in line with industry practice; and
- we assessed the basis on which deferred tax assets are expected to be recovered.

In assessing the potential impact of the request for information by the Indian tax authorities we read the correspondence received by the Group, understood the group reconstruction under review, and the potential basis for any claim, including the relevant legislation and other precedents.

In doing this, we considered:

- the Director's view that no provision for tax should be made at this time;
- the adequacy of the disclosure in the Annual Report; and
- the impact of the restriction on sale of Cairn India shares on the future funding requirements for the Group.

### Risk of management override of internal controls

ISAs (UK & Ireland) require that we consider this.

We assessed the overall control environment of the Group, including the arrangements for staff to "whistle-blow" inappropriate actions, and interviewed senior management and the Group's internal audit function in respect of fraud. We examined the significant accounting estimates and judgements relevant to the financial statements for evidence of bias by the directors that may represent a risk of material misstatement due to fraud. We also tested the appropriateness of manual journal entries.

### Going Concern

Under the Listing Rules we are required to review the directors' statement, set out on page 75, in relation to going concern. We have nothing to report having performed our review.

As noted in the directors' statement, the directors have concluded that it is appropriate to prepare the Group's and Parent Company's financial statements using the going concern basis of accounting. The going concern basis presumes that the Group and Parent Company have adequate resources to remain in operation, and that the directors intend them to do so, for at least one year from the date the financial statements were signed. As part of our audit we have concluded that the directors' use of the going concern basis is appropriate.

However, because not all future events or conditions can be predicted, these statements are not a guarantee as to the Group's and the Parent Company's ability to continue as a going concern.

### Opinions on other matters prescribed by the Companies Act 2006

In our opinion:

- the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements;
- the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006; and
- the information given in the Corporate Governance Statement set out on pages 75 to 77 in the Annual Report with respect to internal control and risk management systems and about share capital structures is consistent with the financial statements.

### Other matters on which we are required to report by exception

#### Adequacy of accounting records and information and explanations received

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the Parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- the Parent Company financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

# Independent Auditors' Report to the Members of Cairn Energy PLC

## Continued

### Directors' remuneration

Under the Companies Act 2006 we are required to report to you if, in our opinion, certain disclosures of directors' remuneration specified by law have not been made. We have no exceptions to report arising from this responsibility.

### Corporate Governance Statement

Under the Companies Act 2006, we are required to report to you if, in our opinion a corporate governance statement has not been prepared by the Parent Company. We have no exceptions to report arising from this responsibility. Under the Listing Rules we are required to review the part of the Corporate Governance Statement relating to the Parent Company's compliance with nine provisions of the UK Corporate Governance Code ('the Code'). We have nothing to report having performed our review.

On page 75 of the Annual Report, as required by the Code Provision C.1.1, the directors state that they consider the Annual Report taken as a whole to be fair, balanced and understandable and provides the information necessary for members to assess the Group's performance, business model and strategy. On page 79, as required by C.3.8 of the Code, the Audit Committee has set out the significant issues that it considered in relation to the financial statements, and how they were addressed. Under ISAs (UK & Ireland) we are required to report to you if, in our opinion:

- the statement given by the directors is materially inconsistent with our knowledge of the Group acquired in the course of performing our audit; or
- the section of the Annual Report describing the work of the Audit Committee does not appropriately address matters communicated by us to the Audit Committee.

We have no exceptions to report arising from this responsibility.

### Other information in the Annual Report

Under ISAs (UK & Ireland), we are required to report to you if, in our opinion, information in the Annual Report is:

- materially inconsistent with the information in the audited financial statements; or
- apparently materially incorrect based on, or materially inconsistent with, our knowledge of the Group and Parent Company acquired in the course of performing our audit; or
- is otherwise misleading.

We have no exceptions to report arising from this responsibility.

### Responsibilities for the financial statements and the audit

#### Our responsibilities and those of the directors

As explained more fully in the Directors' Responsibilities Statement set out on page 74, the directors are responsible for the preparation of the Group and Parent Company financial statements and for being satisfied that they give a true and fair view.

Our responsibility is to audit and express an opinion on the Group and Parent Company financial statements in accordance with applicable law and ISAs (UK & Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.



#### Michael Timar (Senior Statutory Auditor)

for and on behalf of PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
Glasgow  
17 March 2014

#### Notes:

- The maintenance and integrity of the Cairn Energy PLC website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.
- Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.



## Contents

104	<b>Group Income Statement</b>
104	<b>Group Statement of Comprehensive Income</b>
105	<b>Group Balance Sheet</b>
106	<b>Group Statement of Cash Flow</b>
107	<b>Group Statement of Changes in Equity</b>
<hr/>	
108	<b>Section 1 Basis of Preparation</b>
108	1.1 Significant Accounting Policies
<hr/>	
110	<b>Section 2 Oil and Gas Assets and Related Goodwill</b>
111	2.1 Intangible Exploration/Appraisal Assets
113	2.2 Property, Plant & Equipment – Development/Producing Assets
113	2.3 Capital Commitments
114	2.4 Intangible Assets – Goodwill
115	2.5 Impairment Sensitivity Analysis
<hr/>	
116	<b>Section 3 Financial Assets, Working Capital and Provisions</b>
116	3.1 Available-for-sale Financial Assets
117	3.2 Net Funds
118	3.3 Income Tax Assets
118	3.4 Other Receivables
118	3.5 Trade and Other Payables
119	3.6 Provisions
119	3.7 Financial Instruments
<hr/>	
121	<b>Section 4 Results for the Year</b>
121	4.1 Segmental Analysis
123	4.2 Finance Income
124	4.3 Taxation on Loss
126	4.4 Earnings per Ordinary Share
<hr/>	
127	<b>Section 5 Capital Structure and Other Disclosures</b>
127	5.1 Issued Capital and Reserves
128	5.2 Capital Management
128	5.3 Staff Costs
129	5.4 Share-based Payments
130	5.5 Directors' Emoluments and Remuneration of Key Management Personnel
131	5.6 Guarantees
<hr/>	
132	<b>Section 6 Post Balance Sheet Events</b>
132	6.1 Restriction on Sale of Available-for-sale Financial Asset
132	6.2 Farm-down of Senegal Licences
<hr/>	
133	<b>Company Balance Sheet</b>
134	<b>Company Statement of Cash Flow</b>
135	<b>Company Statement of Changes in Equity</b>
<hr/>	
136	<b>Section 7 Notes to the Company Financial Statements</b>
136	7.1 Basis of Preparation
136	7.2 Net Funds
136	7.3 Other Receivables
136	7.4 Trade and Other Payables
137	7.5 Financial Instruments
137	7.6 Investments in Subsidiaries
138	7.7 Capital Management
138	7.8 Related Party Transactions
<hr/>	
140	<b>Appendices to the Group and Company Financial Statements</b>
140	Appendix 1 Prior Year Corporate Acquisitions
142	Appendix 2 Principal Subsidiary Undertakings
143	Appendix 3 Financial Risk Management: Objectives and Policies
145	Appendix 4 Share-based Payments
146	Appendix 5 Auditors' Remuneration

## Group Income Statement

For the year ended 31 December 2013

	Section	2013 US\$m	2012 US\$m
<b>Continuing operations</b>			
Pre-award costs		(23.5)	(18.1)
Unsuccessful exploration costs	2.1	(213.1)	(158.7)
Administrative expenses		(42.2)	(53.3)
Other expenses		-	(11.2)
Impairment of oil and gas assets	2.1	(251.4)	(6.0)
Loss on sale of oil and gas assets	2.2	(24.7)	-
Impairment of goodwill	2.4	(324.2)	-
<b>Operating loss</b>		<b>(879.1)</b>	<b>(247.3)</b>
Loss on sale of available-for-sale financial assets	3.1	-	(81.5)
Impairment of available-for-sale financial assets	3.1	(267.5)	-
Finance income	4.2	50.6	135.9
Finance costs		(2.9)	(1.3)
<b>Loss before taxation from continuing operations</b>		<b>(1,098.9)</b>	<b>(194.2)</b>
<b>Taxation</b>			
Tax credit	4.3a	543.0	266.8
<b>(Loss)/profit for the year attributable to equity holders of the parent</b>		<b>(555.9)</b>	<b>72.6</b>
<b>(Loss)/earnings per ordinary share – basic (cents)</b>	<b>4.4</b>	<b>(93.24)</b>	<b>11.13</b>
<b>(Loss)/earnings per ordinary share – diluted (cents)</b>	<b>4.4</b>	<b>(93.24)</b>	<b>11.12</b>

## Group Statement of Comprehensive Income

For the year ended 31 December 2013

	Section	2013 US\$m	2012 US\$m
<b>(Loss)/profit for the year</b>		<b>(555.9)</b>	<b>72.6</b>
<b>Other comprehensive income – items that may be recycled to profit or loss</b>			
(Deficit)/surplus on valuation of financial assets	3.1	(110.8)	55.6
Deferred tax credit/(charge) on valuation of financial assets	4.3a	48.8	(18.8)
Valuation movement recycled to Income Statement	3.1	267.5	(12.8)
Deferred tax (charge)/credit on valuation movement recycled to Income Statement	4.3a	(74.5)	9.1
Currency translation differences		7.6	(24.5)
<b>Other comprehensive income for the year</b>		<b>138.6</b>	<b>8.6</b>
<b>Total comprehensive income for the year attributable to equity holders of the parent</b>		<b>(417.3)</b>	<b>81.2</b>

## Group Balance Sheet

As at 31 December 2013

	Section	2013 US\$m	2012 US\$m
<b>Non-current assets</b>			
Intangible exploration/appraisal assets	2.1	498.6	899.8
Property, plant & equipment – development/producing assets	2.2	299.9	71.0
Intangible assets – goodwill	2.4	163.4	485.5
Other property, plant & equipment and intangible assets		6.0	6.6
Available-for-sale financial assets	3.1	1,027.6	1,138.4
Deferred tax assets	4.3c	58.7	–
		<b>2,054.2</b>	<b>2,601.3</b>
<b>Current assets</b>			
Income tax asset	3.3	81.3	65.1
Inventory		10.0	–
Other receivables	3.4	152.3	72.7
Cash and cash equivalents and bank deposits	3.2	1,308.3	1,588.6
		<b>1,551.9</b>	<b>1,726.4</b>
<b>Total assets</b>		<b>3,606.1</b>	<b>4,327.7</b>
<b>Current liabilities</b>			
Trade and other payables	3.5	201.0	82.4
Provisions	3.6	11.4	40.5
Loans and borrowings	3.2	55.3	29.6
		<b>267.7</b>	<b>152.5</b>
<b>Non-current liabilities</b>			
Deferred tax liabilities	4.3c	148.0	530.9
Provisions	3.6	2.6	2.6
		<b>150.6</b>	<b>533.5</b>
<b>Total liabilities</b>		<b>418.3</b>	<b>686.0</b>
<b>Net assets</b>		<b>3,187.8</b>	<b>3,641.7</b>
<b>Equity attributable to equity holders of the parent</b>			
Called-up share capital	5.1	12.8	13.0
Share premium	5.1	486.9	486.9
Shares held by ESOP/SIP Trusts	5.1	(28.0)	(28.7)
Foreign currency translation	5.1	(23.9)	(31.5)
Capital reserves – non-distributable	5.1	40.4	40.2
Merger reserve	5.1	255.9	255.9
Available-for-sale reserve	5.1	56.2	(74.8)
Retained earnings		2,387.5	2,980.7
<b>Total equity</b>		<b>3,187.8</b>	<b>3,641.7</b>

The financial statements on pages 104 to 146 were approved by the Board of Directors on 17 March 2014 and signed on its behalf by:



**Jann Brown**  
Managing Director & CFO



**Simon Thomson**  
Chief Executive

## Group Statement of Cash Flow

For the year ended 31 December 2013

Section	2013 US\$m	2012 US\$m
<b>Cash flows from operating activities</b>		
Loss before taxation	(1,098.9)	(194.2)
Unsuccessful exploration costs	213.1	158.7
Depreciation and amortisation	4.5	3.5
Share-based payments charge	14.0	9.9
Impairment of oil and gas assets	251.4	6.0
Loss on sale of oil and gas assets	24.7	-
Impairment of goodwill	324.2	-
Loss on sale of available-for-sale financial asset	-	81.5
Impairment of available-for-sale financial assets	267.5	-
Net finance income	(47.7)	(134.6)
Interest paid	(2.9)	(1.3)
Income tax received	59.9	8.2
Foreign exchange differences	1.3	(9.3)
Other receivables movement	(6.4)	29.4
Trade and other payables movement	34.5	(31.5)
<b>Net cash from/(used in) operating activities</b>	<b>39.2</b>	<b>(73.7)</b>
<b>Cash flows from investing activities</b>		
Expenditure on intangible exploration/appraisal assets	(386.6)	(139.1)
Expenditure on property, plant & equipment – development/producing assets	(31.4)	-
Proceeds on disposal of intangible exploration/appraisal assets	7.1	33.3
Proceeds on disposal of property, plant & equipment – development/producing assets	72.7	-
Purchase of inventory	(10.3)	-
Purchase of other property, plant & equipment and intangible assets	(4.4)	(6.0)
Movement in funds on bank deposits	2.0	6.4
Dividend received	40.5	18.0
Interest received	3.8	6.7
Consideration paid for business combinations	-	(844.5)
Cash acquired as a result of business combinations	-	123.9
Expenses incurred on disposal of Cairn India group	-	(43.7)
Proceeds on disposal of available-for-sale financial asset	-	1,286.2
<b>Net cash (used in)/from investing activities</b>	<b>(306.6)</b>	<b>441.2</b>
<b>Cash flows from financing activities</b>		
Cost of shares purchased	(36.6)	(27.0)
Proceeds from exercise of share options	-	3.2
Proceeds of borrowings	32.5	22.5
Return of cash to shareholders	-	(3,575.2)
<b>Net cash flows used in financing activities</b>	<b>(4.1)</b>	<b>(3,576.5)</b>
Net decrease in cash and cash equivalents	(271.5)	(3,209.0)
Opening cash and cash equivalents at beginning of year	1,586.3	4,730.7
Exchange (losses)/gains on cash and cash equivalents	(6.8)	64.6
<b>Closing cash and cash equivalents</b>	<b>3.2</b>	<b>1,308.0</b>

## Group Statement of Changes in Equity

For the year ended 31 December 2013

	Equity share capital US\$m	Shares held by ESOP Trust and SIP Trust US\$m	Foreign currency translation US\$m	Merger and capital reserves US\$m	Available- for-sale reserve US\$m	Retained earnings US\$m	Total equity US\$m
At 1 January 2012	497.6	(1.7)	(7.0)	40.2	(107.9)	6,472.1	6,893.3
Profit for the year	-	-	-	-	-	72.6	72.6
Surplus on valuation of financial assets	-	-	-	-	55.6	-	55.6
Deferred tax charge on valuation of financial assets	-	-	-	-	(18.8)	-	(18.8)
Valuation movement recycled to Income Statement	-	-	-	-	(12.8)	-	(12.8)
Deferred tax credit on valuation movement recycled to Income Statement	-	-	-	-	9.1	-	9.1
Currency translation differences	-	-	(24.5)	-	-	-	(24.5)
Total comprehensive income for the year	-	-	(24.5)	-	33.1	72.6	81.2
Exercise of employee share options	3.2	-	-	-	-	-	3.2
Share-based payments	-	-	-	-	-	9.9	9.9
Shares issued for acquisitions	1.0	-	-	255.9	-	-	256.9
Return of cash to shareholders	(1.9)	-	-	-	-	(3,573.9)	(3,575.8)
Cost of shares purchased	-	(27.0)	-	-	-	-	(27.0)
At 31 December 2012	499.9	(28.7)	(31.5)	296.1	(74.8)	2,980.7	<b>3,641.7</b>
Loss for the year	-	-	-	-	-	(555.9)	<b>(555.9)</b>
Deficit on valuation of financial assets	-	-	-	-	(110.8)	-	<b>(110.8)</b>
Deferred tax credit on valuation of financial assets	-	-	-	-	48.8	-	<b>48.8</b>
Valuation movement recycled to Income Statement	-	-	-	-	267.5	-	<b>267.5</b>
Deferred tax charge on valuation movement recycled to Income Statement	-	-	-	-	(74.5)	-	<b>(74.5)</b>
Currency translation differences	-	-	7.6	-	-	-	<b>7.6</b>
Total comprehensive income for the year	-	-	7.6	-	131.0	(555.9)	<b>(417.3)</b>
Share buy-back	(0.2)	-	-	0.2	-	(50.6)	<b>(50.6)</b>
Share-based payments	-	-	-	-	-	14.0	<b>14.0</b>
Cost of shares vesting	-	0.7	-	-	-	(0.7)	-
<b>At 31 December 2013</b>	<b>499.7</b>	<b>(28.0)</b>	<b>(23.9)</b>	<b>296.3</b>	<b>56.2</b>	<b>2,387.5</b>	<b>3,187.8</b>

## Section 1 – Basis of Preparation

This section contains the Group's significant accounting policies that relate to the financial statements as a whole. Significant accounting policies specific to one note are included with that note. Accounting policies relating to non-material items are not included in these financial statements.

This section also includes new EU endorsed accounting standards, amendments and interpretations and their expected impact, if any, on the performance of the Group.

### 1.1 Significant Accounting Policies

#### a) Basis of preparation

The consolidated financial statements of Cairn Energy PLC ('Cairn' or 'the Group') for the year ended 31 December 2013 were authorised for issue in accordance with a resolution of the directors on 17 March 2014. Cairn is a limited company incorporated and domiciled in the United Kingdom whose shares are publicly traded. The registered office is located at 50 Lothian Road, Edinburgh, Scotland, EH3 9BY.

Cairn prepares its financial statements on a historical cost basis, unless accounting standards require an alternate measurement basis. Where there are assets and liabilities calculated on a different basis this fact is disclosed either in the relevant accounting policy or in the notes to the financial statements.

The Group's financial statements are prepared on a going concern basis.

#### b) Accounting standards

Cairn prepares its financial statements in accordance with applicable International Financial Reporting Standards ('IFRS'), issued by the International Accounting Standards Board ('IASB') as adopted by the EU. The Group's financial statements are also consistent with IFRS as issued by the International Accounting Standards Board ('IASB') as they apply to accounting periods ended 31 December 2013 with the exception of IFRS 10, 11 and 12 which Cairn will adopt from 1 January 2014.

Effective 1 January 2013, Cairn has adopted the following standards impacting the Group's accounting policies and/or presentation in the Group's financial statements:

- IFRS 13 'Fair Value Measurement'; (effective 1 January 2013)
- IAS 1 (amended) 'Presentation of Financial Statements'; (effective 1 January 2013)
- IAS 19 (revised) 'Employee Benefits'; (effective 1 January 2013)

The amendments to accounting policies will result in minor changes in disclosures within the Statement of Other Comprehensive Income and notes to these financial statements but have no material impact on the results for the year. Other changes to IFRS effective 1 January 2013 have no impact on Cairn's accounting policies or financial statements.

The following new standards, issued by the IASB and endorsed by the EU, have yet to be adopted by the Group :

- IFRS 10 'Consolidated Financial Statements'; (effective 1 January 2014)
- IFRS 11 'Joint Arrangements'; (effective 1 January 2014)
- IFRS 12 'Disclosure of interests in Other Entities' (effective 1 January 2014)
- IAS 27 (amendment) 'Separate Financial Statements' (effective 1 January 2014)
- IAS 28 (amendment) 'Investments in Associates and Joint Ventures' (effective 1 January 2014)

The adoption of these new standards will result in the Group's participating interests in material exploration and development licences, currently disclosed as joint ventures, being re-classified as joint operations. No other changes to the financial statements are expected. No other standards issued by the IASB and endorsed by the EU, but not yet adopted are expected to have any material impact on the Group's financial statements.

#### c) Basis of consolidation

The consolidated financial statements include the results of Cairn Energy PLC and its subsidiary undertakings to the Balance Sheet date. Where subsidiaries follow differing accounting policies from those of the Group, those accounting policies have been adjusted to align with those of the Group. Inter-company balances and transactions between group companies are eliminated on consolidation, though foreign exchange differences arising on inter-company balances between subsidiaries with differing functional currencies are not offset.

The results of subsidiaries acquired in any year are included in the Income Statement and Statement of Cash Flows from the effective date of acquisition while the results of subsidiaries disposed of during the year are included in the Income Statement and Statement of Cash Flows to the date at which control passes from the Group.

#### d) Joint Ventures

Cairn participates in several unincorporated joint ventures which involve the joint control of assets used in the Group's oil and gas exploration and development activities. Cairn recognises its share of the assets, liabilities, income and expenditure of jointly controlled assets in which the Group holds an interest, classified in the appropriate Balance Sheet and Income Statement headings. Cairn's principal licence interests are jointly controlled assets.

A list of Cairn's oil and gas licence interests is given on page 147.

## Section 1 – Basis of Preparation

### Continued

#### 1.1 Significant Accounting Policies – Continued

##### e) Foreign currencies

The financial statements are presented in US dollars ('US\$'), the functional currency of most companies in the Group.

In the financial statements of individual Group companies, Cairn translates foreign currency transactions into the functional currency at the rate of exchange prevailing at the transaction date. Monetary assets and liabilities denominated in foreign currency are translated into the functional currency at the rate of exchange prevailing at the Balance Sheet date. Exchange differences arising are taken to the Income Statement except for those incurred on borrowings specifically allocable to development projects, which are capitalised as part of the cost of the asset.

The Group maintains the accounts of the parent and subsidiary undertakings in their functional currency. Where applicable, the Group translates subsidiary accounts into the presentation currency, US\$, using the closing rate method for assets and liabilities which are translated at the rate of exchange prevailing at the Balance Sheet date and rates at the date of transactions for Income Statement accounts. Cairn takes exchange differences arising on the translation of net assets of Group companies whose functional currency is non-US\$ directly to reserves.

Rates of exchange to US\$1 were as follows:

	Closing 2013	YTD Average 2013	Closing 2012	YTD Average 2012
Sterling	0.604	0.639	0.615	0.631
Indian Rupee	61.810	58.316	54.995	53.284
Norwegian Kroner	6.068	5.871	5.567	5.814
Euro	0.728	0.730	0.758	0.777

## Section 2 – Oil and Gas Assets and Related Goodwill

This section focuses on the assets in the Balance Sheet which form the core of Cairn's business. This includes exploration and appraisal assets in frontier and mature basins, development assets in the UK and Norwegian North Sea and goodwill relating to the Group's oil and gas assets that has arisen on past corporate transactions.

This section quantifies the financial impact of the operations for the year fully described in the operational review on pages 30 to 37.

### Significant accounting judgements in this section:

#### Indicators of impairment for intangible exploration/appraisal assets

Cairn has reviewed intangible exploration/appraisal assets for indicators of impairment and concluded that such indicators did exist on one of the Group's assets. Impairment tests were therefore conducted on the asset where indicators of impairments were identified. See section 2.1.

#### Impairment testing of goodwill

The Group recognised goodwill on business combinations in the prior year (see Appendix 1). This goodwill was largely attributable to deferred tax provided on the temporary taxable difference between the fair value of the assets acquired and their underlying tax base cost. When testing goodwill for impairment at each subsequent reporting date, the remaining deferred tax provision relating to the business combinations is included in the carrying amount of the cash-generating unit to which goodwill is allocated.

### Key estimates and assumptions in this section:

#### Impairment testing of intangible exploration/appraisal assets

Where an indicator of impairment is identified on an intangible exploration/appraisal asset, an impairment test is conducted by comparing the carrying value of the assets within the cash-generating unit containing the asset to the recoverable amount of those assets.

The cash-generating unit represents the smallest group of assets that are expected to generate separately identifiable cash flows. These include exploration/appraisal assets and any development/producing assets within that area. The recoverable amount of the assets in the cash-generating unit represents its fair value less costs of disposal. Where there is no verifiable third party arm's-length transaction from which a market value can be obtained, the fair value of an asset is calculated using discounted cash flow models. This represents a fair value measurement categorised within Level 3 of the fair value hierarchy.

Where the cash-generating unit contains assets with discovered resource, fair value is calculated using forecast net cash flows based on estimated production profiles and cost and oil price assumptions over the expected life of the field discounted to the Balance Sheet date. Where resource is prospective, fair value represents the expected net present value of the prospect, risk-weighted for future exploration success. Given the inherent risk associated with exploration activities, valuations of prospective resource are highly subjective.

The key assumptions used in the Group's discounted cash flow models reflect past experience and take account of external factors. These assumptions are:

- Long-term oil price of US\$90 per boe escalated at 2.5% per annum;
- Reserve estimates of discovered resource (2P and 2C) based on P50 reserve estimates;
- Production profiles based on Cairn's internal estimates;
- Cost profiles for the development of the field and subsequent operating costs supplied by the operator and escalated at 2.5% per annum; and
- Discount rates of 10% for the Group's UK and Norwegian North Sea assets.

#### Impairment testing of goodwill

The goodwill arising from past corporate transactions in the UK and Norwegian North Sea is tested for impairment by comparing the recoverable amount against the carrying value of the underlying oil and gas assets in the UK and Norwegian North Sea operating segment. As with intangible exploration/appraisal assets, fair value less cost of disposal are based on discounted cash flow models as no recent third party transactions exist on which a reliable market-based fair value can be established. The key assumptions are therefore consistent with those for testing intangible exploration/appraisal assets.

Key estimates and assumptions used in the measurement of deferred tax liabilities, which are included in the cash generating unit, will also impact on the goodwill impairment test. See section 4.3.



## Section 2 – Oil and Gas Assets and Related Goodwill

### Continued

#### 2.1 Intangible Exploration/Appraisal Assets

##### Accounting Policy

Cairn follows a successful efforts based accounting policy for oil and gas assets.

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

Expenditure incurred on the acquisition of a licence interest is initially capitalised on a licence-by-licence basis. Costs are held, un-depleted, within intangible exploration/appraisal assets until such time as the exploration phase on the licence area is complete or commercial reserves have been discovered. Exploration expenditure incurred in the process of determining oil and gas exploration targets is capitalised initially within intangible exploration/appraisal assets and subsequently allocated to drilling activities. Exploration/appraisal drilling costs are initially capitalised on a well-by-well basis until the success or otherwise of the well has been established. The success or failure of each exploration/appraisal effort is judged on a well-by-well basis. Drilling costs are written off on completion of a well unless the results indicate that hydrocarbon reserves exist and there is a reasonable prospect that these reserves are commercial.

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

##### Impairment

Intangible exploration/appraisal assets are reviewed regularly for indicators of impairment and tested for impairment where such indicators exist. An indicator that one of the Group's assets may be impaired is most likely to be one of the following:

- There are no further plans to conduct exploration activities in the area;
- Exploration drilling in the area has failed to discover commercial reserve volumes; or
- Development proposals for appraisal assets in the pre-development stage indicate that it is unlikely that the carrying value of the exploration/appraisal asset will be recovered in full.

In such circumstances the intangible exploration/appraisal asset is allocated to property, plant & equipment – development/producing assets within the same cash generating unit and tested for impairment. Any impairment arising is recognised in the Income Statement for the year. Where there are no development/producing assets within the cash generating unit, the excess of the carrying amount of exploration/appraisal asset over its recoverable amount are charged immediately to the Income Statement.

	Frontier Exploration			Mature Basin	Total US\$m
	North Atlantic US\$m	Africa US\$m	Mediterranean US\$m	UK and Norwegian North Sea US\$m	
<b>Net book value</b>					
At 1 January 2012	79.5	-	1.3	-	80.8
Foreign exchange	0.1	-	-	20.3	20.4
Acquisitions	-	-	-	976.5	976.5
Additions	(2.1)	2.2	8.3	82.1	90.5
Disposals	(33.3)	-	-	-	(33.3)
Transfers	-	-	-	(70.4)	(70.4)
Impairment	(5.8)	-	(0.2)	-	(6.0)
Unsuccessful exploration costs	6.1	-	(5.8)	(159.0)	(158.7)
<b>At 1 January 2013</b>	<b>44.5</b>	<b>2.2</b>	<b>3.6</b>	<b>849.5</b>	<b>899.8</b>
Foreign exchange	-	-	-	7.4	7.4
Additions	17.3	177.9	4.5	160.5	360.2
Disposals	-	-	(0.5)	(5.1)	(5.6)
Transfers	-	-	-	(298.7)	(298.7)
Impairment	-	-	-	(251.4)	(251.4)
Unsuccessful exploration costs	(23.6)	(107.4)	(0.8)	(81.3)	(213.1)
<b>At 31 December 2013</b>	<b>38.2</b>	<b>72.7</b>	<b>6.8</b>	<b>380.9</b>	<b>498.6</b>

## Section 2 – Oil and Gas Assets and Related Goodwill

Continued

### 2.1 Intangible Exploration/Appraisal Assets – Continued

#### Frontier Exploration

##### North Atlantic – Greenland and Republic of Ireland

In Greenland, additional costs of the well abandonment programme were offset by the release of costs accrued following the resolution of a disputed contract from the 2011 drilling campaign, leaving net additions of US\$8.7m. Costs of US\$23.6m relating to certain licences in Greenland where no future exploration activity is planned have been charged to the Income Statement as unsuccessful exploration costs.

Disposals in 2012 relate to proceeds received from Statoil to cover back costs and bonuses under the terms of the farm down agreement for the Pitu block in North West Greenland.

Republic of Ireland additions of US\$8.6m in 2013 represent costs incurred post the farm-in completed in the year.

##### Africa – Morocco, Senegal and Mauritania

The first well in Cairn's Atlantic Margin drilling campaign offshore Morocco was drilled on the Fom Draa block and completed in early 2014. Subsequently the rig moved to the Juby Maritime block, also offshore Morocco and completed the second exploration well in March 2014. Both wells failed to encounter commercial hydrocarbons and were plugged and abandoned. Costs of US\$107.4m incurred to 31 December 2013 have been charged to the Income Statement; US\$93.1m relating to the Fom Draa well and US\$14.3m to Juby Maritime costs incurred in advance of drilling.

Further additions in the year of US\$70.5m include back-costs paid of US\$27.0m as Cairn farmed-in to the C19 licence offshore Mauritania and costs incurred in relation to the current drilling programme. An additional US\$41.6m was incurred in three blocks offshore Senegal, including back-costs following the farm-in completed in the year and subsequent additions, of which US\$17.4m will be recovered following completion of a farm-down to ConocoPhillips (see section 6.2).

#### Mature Basin

##### UK and Norwegian North Sea

Acquisition costs of US\$976.5m in 2012 represent the fair value of exploration and appraisal assets added through the acquisitions of Agora Oil & Gas AS (now Capricorn Norge AS) (US\$411.0m) and Nautical Petroleum plc (US\$565.5m). See Appendix 1.

Additions in the current year of US\$160.5m (2012: US\$82.1m) relate to expenditure on exploration and appraisal wells drilled and new prospects added to the portfolio. From the date of acquisition, Cairn has participated in 12 exploration and appraisal wells; seven in 2012 and five in 2013. Four of these wells were successful, of which three are in the Skarvfjell field. A summary of the unsuccessful costs, by well, is as follows:

	2013 US\$m	2012 US\$m
<i>UK:</i>		
Timon	5.5	29.4
Tybart	-	50.2
Bardolph	0.3	22.3
Spaniards East	0.3	7.3
Other non-drilling costs	1.7	-
<i>Norway:</i>		
Frode	53.5	-
Klara	18.6	-
Kakelborg	1.4	34.1
Geite	-	15.7
Unsuccessful exploration costs	81.3	159.0

During 2013, Cairn and its joint venture partners received approval of the development plan of the Kraken field, and consequently costs of US\$298.7m were transferred from intangible exploration/appraisal assets to property, plant & equipment – development/producing assets, after testing for impairment. The similar transfer in 2012 of US\$70.4m related to the Mariner field.

During the year end impairment review of exploration/appraisal assets, an indicator of impairment was identified on the Catcher asset which consists of the main Catcher project, satellite discoveries and additional prospects. Revisions to the project economics, with lower resource estimates and increased cost assumptions, have reduced the recoverable amount of the asset below its carrying value. The subsequent impairment test conducted resulted in a US\$251.4m charge to the Income Statement. Details of the sensitivity of the impairment charge to changes in assumptions are given in section 2.5.

Exploration costs remaining at the year end include the net book value of the Catcher and Skarvfjell fields and associated satellite prospects. The Group added additional prospects to its existing exploration portfolio through the acquisition of non-operated interests in the Klara and Grosbeak prospects in the Norwegian North Sea and through licences awarded under the latest rounds in the UK and Norway.

## Section 2 – Oil and Gas Assets and Related Goodwill

Continued

### 2.2 Property, Plant & Equipment – Development/Producing Assets

	Mature Basin UK and Norwegian North Sea US\$m	Total US\$m
<b>Cost and net book value</b>		
At 1 January 2012	–	–
Transfers	70.4	70.4
Foreign exchange	0.6	0.6
At 1 January 2013	71.0	<b>71.0</b>
Foreign exchange	1.7	<b>1.7</b>
Additions	44.2	<b>44.2</b>
Transfers	298.7	<b>298.7</b>
Disposals	(115.7)	<b>(115.7)</b>
<b>At 31 December 2013</b>	<b>299.9</b>	<b>299.9</b>

Additions in the year relate to costs incurred on the Mariner field, which was transferred from exploration/appraisal assets in 2012. During the current period, Cairn agreed the sale of the Mariner asset to Dyas BV and the sale received formal approval in December 2013. The disposal of Mariner resulted in a US\$24.7m loss to the Income Statement.

Costs of the Kraken field were transferred to development/producing assets in 2013 and this asset represents the carrying value as at 31 December 2013. Impairment tests performed at 31 December 2013 concluded that no impairment existed and no reasonable change in estimates would give rise to impairment (2012: US\$nil).

### 2.3 Capital Commitments

	2013 US\$m	2012 US\$m
Oil and gas expenditure:		
Intangible exploration/appraisal assets – non-rig commitments	<b>292.6</b>	154.3
Intangible exploration/appraisal assets – drilling rig commitments	<b>195.2</b>	–
Property, plant & equipment – development/producing assets	<b>372.8</b>	276.3
Contracted for	<b>860.6</b>	430.6

Capital commitments represent Cairn's share of obligations in relation to its interests in joint ventures. As all Cairn joint ventures are jointly controlled assets, these commitments include Cairn's share of the capital commitments of the joint ventures themselves.

The capital commitments for intangible exploration/appraisal assets relate to operations in Morocco, Senegal, Republic of Ireland and the UK and Norwegian North Sea and do not reflect additional or reduced commitments relating to transactions that completed after the balance sheet date (see section 6.2).

Cairn has entered into operating lease agreements to contract two rigs for drilling in the North Atlantic and Africa. The drilling rig commitments disclosed do not reflect the rig costs of US\$37.3m that Cairn expects to recover from joint venture partners.

Capital commitments for property, plant & equipment – development/producing assets include US\$330.0m relating to a lease commitment due over the next 10 years. The lease term for this asset has not yet commenced.

The Group has no further material capital expenditure committed at the Balance Sheet date.

## Section 2 – Oil and Gas Assets and Related Goodwill

Continued

### 2.4 Intangible Assets – Goodwill

#### Accounting policy

##### Goodwill

Cairn allocates the purchase consideration on the acquisition of a subsidiary to the assets and liabilities acquired on the basis of fair value at the date of acquisition. Any excess of the cost of acquisition over the fair value of the assets and liabilities is recognised as goodwill. Any goodwill arising is recognised as an asset and is subject to annual review for impairment. Goodwill is written off where circumstances indicate that the recoverable amount of the underlying cash generating unit including the asset may no longer support the carrying value of goodwill. Any such impairment loss arising is recognised in the Income Statement for the year. Impairment losses relating to goodwill cannot be reversed in future periods.

In testing for impairment, goodwill arising on business combinations is allocated from the date of acquisition to the group of cash-generating units representing the lowest level at which it will be monitored. Cairn's policy is to monitor goodwill at operating segment level before combining segments for reporting.

The recoverable amount of a cash-generating unit, or group of cash generating units, within the segment is based on its fair value less costs of disposal, using estimated cash flow projections over the licence period of the exploration assets risk-weighted for future exploration success. The key assumptions are sensitive to market fluctuations and the success of future exploration drilling programmes. The most likely factor which will result in a material change to the recoverable amount of the cash-generating unit is the result of future exploration drilling, which will determine the licence area's future economic potential.

	Mature Basin UK and Norwegian North Sea US\$m	Total US\$m
<b>Net book value</b>		
At 1 January 2012	–	–
Additions	473.9	473.9
Foreign exchange	11.6	11.6
At 1 January 2013	485.5	<b>485.5</b>
Foreign exchange	2.1	<b>2.1</b>
Impairment	(324.2)	<b>(324.2)</b>
<b>At 31 December 2013</b>	<b>163.4</b>	<b>163.4</b>

Goodwill additions in 2012 relate to the corporate acquisitions during the year and are largely generated by the deferred tax provided. Details of the corporate acquisitions can be found in Appendix 1. This goodwill is fully allocated to the UK and Norwegian North Sea operating segment.

At 31 December 2012, the goodwill impairment test did not identify any impairment, with the carrying value of the UK and Norwegian North Sea operating segment being equal to the recoverable amount of the underlying assets, notably the Catcher, Kraken and Skarfjell assets.

The impairment of the Catcher asset in 2013 (see section 2.1) reduces both the carrying value of the operating segment and its recoverable amount in equal measures. The release of deferred tax provided on the Catcher asset however, increases the carrying value of the segment in relation to the recoverable amount. Additionally, the recognition of tax credits for field allowances to which the Kraken asset is eligible, further increases the carrying value of the segment. As a result, the recoverable amount of the assets can no longer support their carrying value and at 31 December 2013, the year end impairment test identified an impairment and a charge of US\$324.2m was recorded.

The remaining carrying value of goodwill at 31 December 2013 is supported by fair value less costs of disposal of the Group's UK and Norwegian North Sea assets, principally through its three main projects Catcher, Kraken and Skarfjell. Additional fair value is attributed to other exploration prospects that have been identified in this segment. The values are calculated internally and the key assumptions used in the valuations include a high level of subjectivity reflecting the nature of oil and gas exploration activities.

## Section 2 – Oil and Gas Assets and Related Goodwill

Continued

### 2.5 Impairment Sensitivity Analysis

At 31 December 2013, impairment was recognised on one intangible exploration/appraisal asset in the UK North Sea and on goodwill allocated to the UK and Norwegian North Sea operating segment. The key assumptions that Cairn has used to value its assets are subjective and reasonable changes to the oil price assumption, discount rate or oil and gas reserve estimates could materially impact the impairment charges recognised in the year.

Cairn has run sensitivities on its oil price assumption of US\$90 per boe looking at a variance of US\$5 above and below and discount rate sensitivities of 8% and 12% either side of the 10% currently used. The impact of these changes on the carrying value of the Group's Catcher asset and goodwill is summarised below:

	Increase/ (Decrease) in Intangible Exploration/ Appraisal assets US\$m	Increase/ (Decrease) in Goodwill US\$m
Decrease in oil price assumption to US\$85 per boe	(27.0)	(11.5)
Increase in oil price assumption to US\$95 per boe	59.0	123.5
Decrease in discount rate to 8%	73.0	174.1
Increase in discount rate to 12%	(25.0)	(46.8)

The Group's proved and probable and contingent reserve estimates are based on P50 probabilities. P10 and P90 estimates are also produced but would not provide a reasonable estimate to be used in calculating the fair value of the Group's assets.

Cost assumptions are based on the latest estimates provided by the operators and are consistent with the forecast costs included in field development plans where applicable.

## Section 3 – Financial Assets, Working Capital and Provisions

Cairn's financial assets and liquid cash resources ensure the Group is fully funded to meet its current exploration programme.

This section focuses on those assets, together with the working capital position of the Group and provisions that exist at the year end.

### Significant accounting judgements in this section:

#### Impairment of Available-for-sale Financial Asset

At 30 June 2013, the Group's 10.3% shareholding in Cairn India Limited, classified as a non-current available-for-sale financial asset, had suffered a significant fall in value from that at the date of initial recognition in 2011. Though the fall is not expected to be a permanent diminution, the size of the deficit was such that cumulative mark-to-market valuation movements recognised in 'Other Comprehensive Income' were recycled to the Income Statement as an impairment.

### Key estimates and assumptions in this section:

There were no key estimations or assumptions in this section.

## 3.1 Available-for-sale Financial Assets

### Accounting policy

The Group's available-for-sale financial assets represent listed equity shares which are held at fair value (the quoted market price). Movements in the fair value during the year are recognised directly in equity and are disclosed in the Statement of Comprehensive Income. The cumulative gains or losses that arise on subsequent disposal of available-for-sale assets are recycled through the Income Statement.

At each reporting date, the fair value of the financial asset is compared to the value at the date of its initial recognition for signs of a prolonged or significant deficit in the valuation, which would indicate impairment. Where impairment is identified, cumulative losses recognised in Other Comprehensive Income are recycled to the Income Statement. In the event of a subsequent recovery in the valuation of the asset, there is no reversal of impairment; any such post-impairment gains are recognised as a surplus through other comprehensive income. Any further impairment losses will be recognised through the Income Statement.

	Listed equity shares US\$m
<b>Fair Value</b>	
As at 1 January 2012	2,463.3
Disposals	(1,380.5)
Surplus on valuation	55.6
As at 1 January 2013	<b>1,138.4</b>
Deficit on valuation	<b>(110.8)</b>
<b>As at 31 December 2013</b>	<b>1,027.6</b>

Available-for-sale financial assets represent the Group's remaining investment in the fully-diluted share capital of Cairn India Limited, listed in India, which by its nature has no fixed maturity or coupon rate. These listed equity securities present the Group with an opportunity for return through dividend income and trading gains.

At 30 June 2013, the value of the investment in Cairn India Limited had fallen to US\$955.6m. As this represented a significant fall in value from its original recognition, the accumulated deficit of US\$267.5m in the available-for-sale reserve was recycled to the Income Statement and recorded as impairment. In the second half of the year the value of the asset increased by US\$72.0m. This increase is included within other comprehensive income.

During 2012, the Group disposed of 11.5% of its shareholding in Cairn India Limited in two separate transactions resulting in the recognition of a loss of US\$81.5m in the Income Statement, including US\$12.8m recycled from the reserves. The remaining minority holding of 10.3% is not held for trading and continues to be classified as non-current available-for-sale financial asset. The fair value of US\$1,027.6m (2012: US\$1,138.4m) is based on the closing market value at 31 December 2013 of INR 323.75 (2012: INR 319.10).

Subsequent to the year end, the Indian Income Tax department have placed a restriction on Cairn selling further shares in Cairn India Limited. As no restriction existed at the measurement date there is no impact on the closing valuation of the available-for-sale financial asset or on the results for the year. Full details are given in section 6.1.

## Section 3 – Financial Assets, Working Capital and Provisions

Continued

### 3.1 Available-for-sale Financial Assets – Continued

#### Sensitivity Analysis

At the year end the closing Cairn India Limited share price used to value the available-for-sale financial assets was INR 323.75/US\$5.24 (2012: INR 319.1/US\$ 5.80). The movement in the Cairn India Limited share price over the current and prior period is as follows:



The sensitivity analysis below has been determined based on the exposure to equity price risks at the reporting date, assuming all other variables are held constant. Sensitivities have been run based on the highest and lowest share prices measured in the preceding 12 month period. Those prices are determined using the closing INR share price converted to USD at the daily rate.

	Effect on loss for year US\$m	Effect on Equity US\$m
<b>As at 31 December 2013</b>		
Increase to the highest share price in 2013 – 340 INR (\$6.33)	–	167.7
Decrease to the lowest share price in 2013 – 274 INR (\$4.51)	(54.6)	(111.2)
<b>As at 31 December 2012</b>		
Increase to the highest share price in 2012 – 392 INR (\$7.96)	–	361.4
Decrease to the lowest share price in 2012 – 307 INR (\$5.52)	–	(16.4)

### 3.2 Net Funds

#### Accounting policies

##### Bank deposits

Bank deposits with an original maturity of over three months are held as a separate category of current asset.

##### Cash and cash equivalents

Cash and cash equivalents comprise cash at bank and short-term deposits with an original maturity of three months or less.

##### Loans and borrowings

Loans are initially measured at fair value less directly attributable transaction costs. After initial recognition, interest bearing loans are subsequently measured at amortised cost using the effective interest method. Interest payable is accrued in the Income Statement using the effective interest method.

	2013 US\$m	2012 US\$m
Bank deposits	0.3	2.3
Cash and cash equivalents	1,308.0	1,586.3
	1,308.3	1,588.6
Loans and borrowings	(55.3)	(29.6)
<b>Net funds</b>	<b>1,253.0</b>	<b>1,559.0</b>

## Section 3 – Financial Assets, Working Capital and Provisions

Continued

### 3.2 Net Funds – Continued

Cash and cash equivalents earn interest at floating rates based on daily bank deposit rates. Short-term deposits are made for varying periods from overnight deposits to three months depending on the cash requirements of the Group. Loans and borrowings represent amounts drawn under the Capricorn Norge AS (previously Agora Oil and Gas AS) revolving exploration loan facility. Subsequent to the year end, this loan has been repaid in full and the facility cancelled.

Cash and cash equivalents include US\$100.0m of cash placed with BNP Paribas to support a letter of credit issued on 22 July 2013 as required under the membership of the Oil Spill Response Scheme's 'Cap and Contain' arrangement. The Group's use of this cash is therefore restricted.

Cairn limits the placing of deposits, certificates of deposit and other investments to banks or financial institutions that have at least two A- or above ratings from Moody's, Standard & Poor's or Fitch unless a Sovereign Guarantee is available from an AAA rated Government. The counterparty limits vary between US\$50.0m and US\$200.0m depending on the ratings of the counterparty. No investments are placed with any counterparty with a five year CDS exceeding 250 bps. Investments in money market liquidity funds are only made with AAA rated liquidity funds and the maximum holding in any single fund is 5% of total investments.

### 3.3 Income Tax Assets

Income tax assets of US\$81.3m (2012: US\$65.1m) relate to cash tax refunds due from the Norwegian authorities on the tax value of exploration expenses incurred in Norway during the current year. The loans and borrowings noted in section 3.2 are secured against this tax refund.

### 3.4 Other Receivables

	2013 US\$m	2012 US\$m
Prepayments	5.2	12.2
Other receivables	86.2	34.3
Joint venture receivables	60.9	26.2
	<b>152.3</b>	72.7

Other receivables include costs incurred by Cairn awaiting recharge to joint ventures. Joint venture receivables include the share of joint venture accruals to be recovered from partners in joint ventures where Cairn is the operator. The increase in these balances reflects the drilling operations that were ongoing at the year end.

At 31 December 2013, no amount within the Group's other receivables or joint venture receivables were past due or impaired (2012: US\$nil).

There was no Group allowance for doubtful debts made in 2013. In determining the recoverability of other receivables, the Group carries out a risk analysis based on the type and age of the outstanding receivable.

### 3.5 Trade and Other Payables

	2013 US\$m	2012 US\$m
Trade payables	10.3	13.9
Other taxation and social security	6.4	18.2
Other payables	15.2	5.5
Joint venture payables	135.6	38.7
Accruals	33.5	6.1
	<b>201.0</b>	82.4

Joint venture payables include Cairn's share of the trade and other payables of joint ventures in which the Group participates. Where Cairn is operator of the joint venture, joint venture payables also includes amounts that Cairn will settle and recover from partners. The increase in joint venture payables reflects the drilling operations that were ongoing at the year end.

Accruals include US\$14.0m in relation to the share buy-back programme ongoing at the year end. See section 5.1.



## Section 3 – Financial Assets, Working Capital and Provisions

Continued

### 3.6 Provisions

	Abandonment provision US\$m	Other provisions US\$m	Total US\$m
At 1 January 2012	14.0	–	14.0
Additions from acquisitions during the year	–	6.6	6.6
Increase of provisions	14.4	8.1	22.5
At 1 January 2013	28.4	14.7	<b>43.1</b>
Provision utilised	(24.8)	(4.3)	<b>(29.1)</b>
<b>At 31 December 2013</b>	<b>3.6</b>	<b>10.4</b>	<b>14.0</b>
Current	3.6	7.8	<b>11.4</b>
Non-current	–	2.6	<b>2.6</b>
<b>At 31 December 2012</b>	<b>3.6</b>	<b>10.4</b>	<b>14.0</b>
Current	28.4	12.1	40.5
Non-current	–	2.6	2.6
At 31 December 2012	28.4	14.7	43.1

During 2013, US\$24.8m of provisions were utilised towards abandonment costs relating to wells drilled during the Group's 2011 Greenland exploration campaign.

### 3.7 Financial Instruments

#### Accounting policy

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.

Financial assets are categorised as financial assets held at fair value through profit or loss, held-to-maturity investments, loans and receivables and available-for-sale financial assets. The Group holds financial assets which are classified as either available-for-sale financial assets or loans and receivables.

Financial liabilities generally substantiate claims for repayment in cash or another financial asset. Financial liabilities are categorised as either fair value through profit or loss or held at amortised cost. All of the Group's financial liabilities are held at amortised cost.

Financial instruments are generally recognised as soon as the Group becomes party to the contractual regulations of the financial instrument.

Set out below is the comparison by category of carrying amounts and fair values of all the Group's financial instruments that are carried in the financial statements.

#### Financial assets

Carrying amount and fair value	2013 US\$m	2012 US\$m
<i>Loans and receivables</i>		
Bank deposits	<b>0.3</b>	2.3
Cash and cash equivalents	<b>1,308.0</b>	1,586.3
Joint venture receivables	<b>60.9</b>	26.2
Other receivables	<b>86.2</b>	34.3
<i>Available-for-sale financial assets</i>		
Listed equity shares	<b>1,027.6</b>	1,138.4
	<b>2,483.0</b>	2,787.5

All of the above loans and receivables are current and unimpaired.

## Section 3 – Financial Assets, Working Capital and Provisions

Continued

### 3.7 Financial Instruments – Continued

#### Financial liabilities

Carrying amount and fair value	2013 US\$m	2012 US\$m
<i>Amortised cost</i>		
Trade payables	10.3	13.9
Joint venture payables	135.6	38.7
Accruals	33.5	6.1
Other payables	15.2	5.5
Provisions	14.0	43.1
Bank loans	55.3	29.6
	<b>263.9</b>	136.9

The fair value of financial assets and liabilities, other than available-for-sale financial assets, has been calculated by discounting the expected future cash flows at prevailing interest rates.

#### Maturity analysis

All of the Group financial liabilities have a maturity of less than one year, other than the Group's provision of US\$2.6m (2012: US\$2.6m) that falls due after one year.

#### Fair value

The Group holds listed equity shares as a non-current available-for-sale financial asset. The Group determines and discloses the fair value of these by reference to the quoted (unadjusted) prices in active markets for those shares at the measurement date.

At 31 December 2013 the Group held the following financial instruments measured at fair value:

Assets measured at fair value – Level 1	2013 US\$m	2012 US\$m
<i>Available-for-sale financial assets</i>		
Equity shares – listed	1,027.6	1,138.4
	<b>1,027.6</b>	1,138.4

## Section 4 – Results for the Year

This section includes the results and performance of the Group, with segmental disclosures highlighting the core areas of the Group's operations in frontier and mature basin exploration activities within a balanced, sustainable portfolio including development projects.

This section also includes details of the Group tax credits in the year and deferred tax assets and liabilities held at the year end.

### Significant accounting judgements in this section:

#### Deferred taxation

The deferred tax liability relating to the Group's investment in Cairn India Limited, classified as an available-for-sale financial asset, is provided on the assumption that any future disposal will result in a tax liability.

At the year end Cairn recognised a deferred tax asset in respect of UK North Sea oil and gas assets. This deductible temporary difference represents eligible field allowances on the Kraken asset, offset by other taxable temporary differences. Cairn believes it is probable that UK North Sea assets will generate taxable profits to allow the temporary difference arising on the field allowances to be utilised in full.

### Key estimates and assumptions in this section:

#### Deferred taxation

Deferred tax liabilities relating to UK and Norwegian North Sea assets are measured using the tax rates and laws that are expected to apply to the period when the assets are realised, based on the conditions that existed at the Balance Sheet date. Deferred tax liabilities are not adjusted for field allowances that certain assets in the UK may qualify for in future periods, but which are subject to Government approval of respective field development plans which did not exist at the Balance Sheet date.

## 4.1 Segmental Analysis

### Operating Segments

Cairn's operations focus on frontier exploration activities in areas within similar geological structures which have the potential to add material value to the Group, balanced by lower risk exploration and development assets in mature basins. For management purposes, the operations of the Group are organised based on geographical regions within either the frontier exploration or mature basin categories.

Geographical regions are combined into regional business units which form the Group's operating segments. Each business unit is headed by its own regional director (a regional director may be responsible for more than one business unit) and management monitors the results of each separately for the purposes of making decisions about resource allocation and performance assessment.

#### Frontier exploration

The Group's frontier exploration activities currently focus on the Atlantic Margin and the Mediterranean. The Atlantic Margin comprises two operating segments: the North Atlantic, with assets in Greenland and Republic of Ireland, and Africa, which includes Cairn's interests in Morocco, Senegal and Mauritania. The Group's current operated multi-well exploration drilling programme, which commenced in 2013 and will continue through 2014, includes exploration drilling offshore Morocco, Senegal and Republic of Ireland.

The Mediterranean operating segment includes licences in Spain, France and Malta which are at the early stages of exploration activity and have yet to incur significant costs.

#### Mature Basin

The mature basin assets are held in one operating segment in the UK and Norwegian North Sea. This segment includes the Catcher and Skarfjell fields held in intangible exploration/appraisal assets and the Kraken field, now included in property, plant & equipment – development/producing assets. Details of exploration wells drilled in 2013 can be found in section 2.1.

#### Other

The results of the Mediterranean operating segment are reported along with the Group's corporate assets in the 'Other Cairn Energy' reportable segment.

## Section 4 – Results for the Year

### Continued

#### 4.1 Segmental Analysis – Continued

##### Geographical information: Non-current assets

###### Frontier Exploration: Greenland and Republic of Ireland

2013	2012
<b>US\$38.2m</b>	US\$44.7m

Others	2012
2013	2012
<b>US\$5.1m</b>	US\$4.7m

###### Frontier Exploration: Mediterranean

2013	2012
<b>\$6.9m</b>	US\$3.8m

###### Mature Basin: UK and Norwegian North Sea

2013	2012
<b>US\$844.6m</b>	US\$1,407.3m

###### Frontier Exploration: Africa – Morocco, Senegal, Mauritania

2013	2012
<b>US\$73.1m</b>	US\$2.4m



Non-current assets for this purpose consist of intangible exploration/appraisal assets; property, plant & equipment – development/producing assets; intangible assets – goodwill; and other property, plant & equipment and intangible assets.

The segment results for the year ended 31 December 2013 are as follows:

	Frontier Exploration		Mature Basin	Other Cairn Energy Group US\$m	Total US\$m
	North Atlantic US\$m	Africa US\$m	UK and Norwegian North Sea US\$m		
Pre-award costs	(1.1)	–	(10.3)	(12.1)	<b>(23.5)</b>
Unsuccessful exploration costs	(23.6)	(107.4)	(81.3)	(0.8)	<b>(213.1)</b>
Depreciation	(0.1)	–	(0.5)	(1.1)	<b>(1.7)</b>
Amortisation	–	–	–	(2.8)	<b>(2.8)</b>
Other administrative expenses	(0.2)	(0.5)	(2.6)	(34.4)	<b>(37.7)</b>
Impairment of oil and gas assets	–	–	(251.4)	–	<b>(251.4)</b>
Loss on sale of oil and gas assets	–	–	(24.7)	–	<b>(24.7)</b>
Impairment of goodwill	–	–	(324.2)	–	<b>(324.2)</b>
<b>Operating loss</b>	<b>(25.0)</b>	<b>(107.9)</b>	<b>(695.0)</b>	<b>(51.2)</b>	<b>(879.1)</b>
Impairment of available-for-sale financial assets	–	–	–	(267.5)	<b>(267.5)</b>
Interest income	–	–	1.3	2.5	<b>3.8</b>
Interest expense	–	–	(2.5)	–	<b>(2.5)</b>
Other finance income and costs	0.4	–	(0.2)	46.2	<b>46.4</b>
<b>Loss before taxation</b>	<b>(24.6)</b>	<b>(107.9)</b>	<b>(696.4)</b>	<b>(270.0)</b>	<b>(1,098.9)</b>
Taxation credit	–	–	468.7	74.3	<b>543.0</b>
<b>Loss after taxation</b>	<b>(24.6)</b>	<b>(107.9)</b>	<b>(227.7)</b>	<b>(195.7)</b>	<b>(555.9)</b>
<b>Capital expenditure</b>	<b>17.3</b>	<b>177.9</b>	<b>204.9</b>	<b>8.4</b>	<b>408.5</b>

## Section 4 – Results for the Year Continued

### 4.1 Segmental Analysis – Continued

The segment results for the year ended 31 December 2012 are as follows:

	Frontier Exploration		Mature Basin	Other Cairn Energy Group US\$m	Total US\$m
	North Atlantic US\$m	Africa US\$m	UK and Norwegian North Sea US\$m		
Pre-award costs	(3.4)	-	(5.4)	(9.3)	(18.1)
Unsuccessful exploration costs	6.1	-	(159.0)	(5.8)	(158.7)
Depreciation	(0.1)	-	(0.6)	(0.8)	(1.5)
Amortisation	-	-	-	(2.0)	(2.0)
Other expenses and administrative expenses	(0.2)	-	(14.8)	(46.0)	(61.0)
Impairment	(5.8)	-	-	(0.2)	(6.0)
Operating loss	(3.4)	-	(179.8)	(64.1)	(247.3)
Loss on sale of available-for-sale asset	-	-	-	(81.5)	(81.5)
Interest income	-	-	1.2	4.9	6.1
Interest expense	-	-	(0.8)	-	(0.8)
Other finance income and costs	(0.2)	-	(0.9)	130.4	129.3
Loss before taxation	(3.6)	-	(180.3)	(10.3)	(194.2)
Taxation credit	-	-	122.3	144.5	266.8
(Loss)/profit after taxation	(3.6)	-	(58.0)	134.2	72.6
Capital expenditure	(2.1)	2.2	1,546.9	13.8	1,560.8

### 4.2 Finance Income

	2013 US\$m	2012 US\$m
Bank and other interest receivable	3.8	6.1
Dividends received	40.5	18.0
Exchange gain	6.3	111.8
	<b>50.6</b>	135.9

Dividends received were from Cairn India Limited. In 2013, the Group eliminated inter-company debt through a series of loan waivers and capital contribution. Eliminating the inter-company debt reduces the Group's Income Statement exposure to foreign exchange movements which is reflected in the fall in exchange gains from 2012 to the current year.

## Section 4 – Results for the Year

Continued

### 4.3 Taxation on Loss

#### Accounting policy

The total tax charge or credit represents the sum of current tax and deferred tax. The current tax is based on taxable profit or loss for the year. Taxable profit or loss differs from net profit or loss as reported in the Income Statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit or loss.

Deferred tax liabilities are recognised for all taxable temporary differences except in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets are recognised for deductible temporary differences that exist only where it is probable that taxable profits will be generated against which the carrying value of the deferred tax asset can be recovered.

A deferred tax asset or liability is not recognised if a temporary difference arises on initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

Current and deferred tax is calculated using tax rates and laws that have been enacted or substantively enacted by the Balance Sheet date.

#### a) Analysis of tax credit on loss in the year

	2013 US\$m	2012 US\$m
<b>Current tax credits:</b>		
Norwegian tax refunds receivable	(81.6)	(39.4)
Withholding taxes deducted at source	-	0.1
	<b>(81.6)</b>	<b>(39.3)</b>
<b>Deferred tax credit:</b>		
Norwegian deferred tax charge	20.3	(8.1)
Recognition of eligible field allowance on UK development asset	(211.9)	-
Release of provision on disposal of UK development asset	(32.8)	-
Release of provision on impairment of UK intangible exploration/appraisal asset	(152.2)	-
Other UK deferred tax credits	(10.3)	(74.8)
Recycled from other comprehensive income on impairment of financial assets	(74.5)	-
Release of provision on sale of available-for-sale financial asset	-	(144.6)
	<b>(461.4)</b>	<b>(227.5)</b>
<b>Total tax credit on loss</b>	<b>(543.0)</b>	<b>(266.8)</b>
<b>Tax included in Other Comprehensive Income:</b>		
Deferred tax (credit)/charge on valuation of financial assets	(48.8)	18.8
Deferred tax charge/(credit) on valuation movement recycled to Income Statement	74.5	(9.1)
<b>Total tax charge in Other Comprehensive Income</b>	<b>25.7</b>	<b>9.7</b>

Norwegian deferred tax charge includes a charge of US\$23.8m (2012: credit of US\$6.7m) on temporary differences in respect of non-current assets and a credit of US\$3.5m (2012: US\$1.4m) on losses and other temporary differences. Other UK deferred tax charges includes a charge of US\$59.0m (2012: US\$64.4m) on temporary differences in respect of non-current assets and a credit of US\$69.3m (2012: charge of US\$10.4m) on losses and other temporary differences.

## Section 4 – Results for the Year

### Continued

#### 4.3 Taxation on Loss – Continued

##### b) Factors affecting tax credit for the year

A reconciliation of income tax credit applicable to loss before income tax at the UK statutory rate to income tax credit at the Group's effective income tax rate is as follows:

	2013 US\$m	2012 US\$m
<b>Loss before taxation</b>	<b>(1,098.9)</b>	<b>(194.2)</b>
Loss before tax multiplied by the UK statutory rate of corporation tax of 23.25% (2012: 24.50%)	<b>(255.5)</b>	<b>(47.6)</b>
<b>Effect of:</b>		
Special tax rates and reliefs applying to oil and gas activities	<b>(200.6)</b>	<b>(81.1)</b>
Impact of field allowances on deferred tax	<b>(145.5)</b>	–
Additional deferred tax credit on disposal of development asset	<b>(27.0)</b>	–
Non-deductible impairment of goodwill	<b>72.3</b>	–
Adjustments in respect of prior periods	<b>(16.6)</b>	–
Temporary differences not recognised	<b>46.0</b>	<b>(16.7)</b>
Deferred tax credit on disposal of available-for-sale financial asset	–	<b>(124.6)</b>
Foreign exchange movements	<b>(12.1)</b>	<b>(0.6)</b>
Other	<b>(4.0)</b>	<b>3.8</b>
<b>Total tax credit on loss</b>	<b>(543.0)</b>	<b>(266.8)</b>

The reconciliation shown above has been based on the average UK statutory rate of corporation tax for 2013 of 23.25% (2012: 24.50%).

The UK main rate of corporation tax was 24% prior to 1 April 2013, and 23% from that date onwards. The reduction in the tax rate from 24% to 23% has resulted in an average rate of corporation tax of 23.25% for the year ended 31 December 2013, as shown above. The rate will reduce to 21% on 1 April 2014 and to 20% on 1 April 2015.

Special rates of tax apply to oil and gas activities in the UK and Norwegian North Sea operating segment. The applicable UK statutory tax rate applying to North Sea oil and gas activities is 62% and the applicable Norwegian rate applying to oil and gas activities is 78%.

##### c) Deferred tax asset and liabilities recoverable/due after more than one year

###### Reconciliation of movement in deferred tax assets/(liabilities):

	Temporary difference in respect of non-current assets US\$m	Losses US\$m	Other temporary differences US\$m	Total US\$m
<b>Deferred tax asset</b>				
At 1 January 2012 and 2013	–	–	–	–
Deferred tax credit through Income Statement	<b>(262.5)</b>	<b>109.3</b>	<b>211.9</b>	<b>58.7</b>
<b>At 31 December 2013</b>	<b>(262.5)</b>	<b>109.3</b>	<b>211.9</b>	<b>58.7</b>
<b>Deferred tax liabilities</b>				
At 1 January 2012	<b>(254.1)</b>	–	–	<b>(254.1)</b>
Deferred tax on fair value on corporate acquisitions (Appendix 1)	<b>(545.4)</b>	<b>51.0</b>	<b>0.7</b>	<b>(493.7)</b>
Deferred tax credit through Income Statement	<b>215.6</b>	<b>11.1</b>	<b>0.8</b>	<b>227.5</b>
Deferred tax charge through Other Comprehensive Income	<b>(9.7)</b>	–	–	<b>(9.7)</b>
Exchange difference arising	<b>(3.8)</b>	<b>0.6</b>	<b>2.3</b>	<b>(0.9)</b>
At 1 January 2013	<b>(597.4)</b>	<b>62.7</b>	<b>3.8</b>	<b>(530.9)</b>
Deferred tax credit through Income Statement	<b>448.4</b>	<b>(49.3)</b>	<b>3.7</b>	<b>402.8</b>
Deferred tax charge through Other Comprehensive Income	<b>(25.6)</b>	–	–	<b>(25.6)</b>
Exchange differences arising	<b>18.4</b>	<b>(12.4)</b>	<b>(0.3)</b>	<b>5.7</b>
<b>At 31 December 2013</b>	<b>(156.2)</b>	<b>1.0</b>	<b>7.2</b>	<b>(148.0)</b>

## Section 4 – Results for the Year

### Continued

#### 4.3 Taxation on Loss – Continued

##### Deferred tax asset/(liabilities) analysed by country:

	2013 US\$m	2012 US\$m
<b>Deferred tax asset:</b>		
UK	58.7	-
	<b>58.7</b>	-
<b>Deferred tax liabilities:</b>		
UK	-	(348.8)
Norway	(77.5)	(62.9)
India	(70.5)	(119.2)
	<b>(148.0)</b>	(530.9)

##### Recognised deferred tax assets

As at the Balance Sheet date, a net deferred tax asset of US\$58.7m (2012: deferred tax liability of US\$348.8m) has been recognised in the UK on other temporary differences and tax losses in excess of the UK deferred tax liability arising on temporary differences in respect of non-current assets attributable to UK Ring Fence trading activity. The UK other temporary difference of US\$211.9m (2012: US\$nil) represents field allowances on the Kraken development which will reduce future Ring Fence profits subject to Supplementary Charge. The eligible field allowances were confirmed when DECC approved the Kraken field development plan and will be claimed when production commences.

A deferred tax asset has also been recognised in respect of Norwegian tax losses of US\$7.3m (2012: US\$7.3m) against a Norwegian deferred tax liability arising on temporary differences in respect of non-current assets.

##### Unrecognised deferred tax assets

At the Balance Sheet date, the Group had a potential deferred tax asset of US\$0.3m (2012: US\$0.3m) in respect of future UK corporation tax deductions for equity-based remuneration. This asset has not been recognised as it is not considered probable that there will be sufficient profits to utilise these tax deductions.

In addition, no deferred tax liability has been recognised at the year end on UK fixed asset temporary differences of US\$163.8m (2012: US\$1,274.0m) and no deferred tax asset has been recognised on UK Ring Fence pre-trade losses of US\$16.1m (2012: US\$0.5m), UK non-Ring Fence pre-trade losses of US\$5.3m (2012: US\$37.8m), UK excess management expenses of US\$205.4m (2012: US\$319.6m), UK non-trade deficits of US\$53.2m (2012: US\$0.7m) and UK other temporary differences of US\$5.0m (2012: US\$0.6m) as it is not considered probable that the net deferred tax asset will be utilised in future periods.

##### d) Tax strategy and governance

The Group's tax strategy is fully aligned with its overarching business objectives and principles. Cairn commits to managing its tax affairs in a transparent and responsible manner and ensuring that all statutory obligations and disclosure requirements are met. We aim to comply with both the letter and spirit of the law in the relevant jurisdictions in which we operate, to ensure that the right amount of tax is paid, at the right time, within the right jurisdiction.

As the Group is currently at an early stage in the value creation cycle and the level of its exploration activities is high, there are currently no taxable profits in the UK. Taxable profits in other jurisdictions are also minimal, and as a result cash payments of corporation taxes are currently low.

Cairn's policy is to not enter into any artificial tax avoidance schemes and to build and maintain strong collaborative working relationships with all relevant tax authorities, based on honesty, integrity and proactive cooperation. The Group aims for certainty in relation to the tax treatment of all items, however we acknowledge that this will not always be possible, for example where transactions are complex and there is a lack of maturity in the tax regime in the relevant jurisdiction in which we are operating. In such circumstances the Group will seek external advice where appropriate and ensure that the approach adopted in any relevant tax return is supportable and includes full disclosure of the position taken.

#### 4.4 Earnings per Ordinary Share

Basic and diluted earnings per share are calculated using the following measures of (loss)/profit:

	2013 US\$m	2012 US\$m
<b>(Loss)/profit and diluted (loss)/profit attributable to equity holders of the parent</b>	<b>(555.9)</b>	72.6

The following reflects the share data used in the basic and diluted earnings per share computations:

	2013 '000	2012 '000
Weighted average number of shares	602,279	655,140
Less weighted average shares held by ESOP and SIP Trusts	(5,969)	(2,187)
<b>Basic weighted average number of shares</b>	<b>596,310</b>	652,953
Dilutive potential ordinary shares:		
Employee share options	389	445
<b>Diluted weighted average number of shares</b>	<b>596,699</b>	653,398



## Section 5 – Capital Structure and Other Disclosures

The disclosures in this section focus on the issued share capital, the share schemes in operation and the associated share-based payment charge to profit or loss. Other mandatory disclosures, such as details of related party transactions, can also be found here.

### Significant accounting judgements in this section:

There are no significant accounting judgements in this section.

### Key estimates and assumptions in this section:

#### Share-based payments

Charges for share-based payments are based on the fair value at the date of the award. The shares are valued using appropriate modelling techniques and inputs to the models include assumptions on lever rates, trigger points, discounts rates and volatility. See section 5.4.

## 5.1 Issued Capital and Reserves

### Called-up Share Capital

Group and Company	Number <sup>1/13P</sup> B shares '000	Number <sup>8/13P</sup> Ordinary '000	Number <sup>231/169P</sup> Ordinary '000	<sup>8/13P</sup> Ordinary US\$m	<sup>231/169P</sup> Ordinary US\$m
<b>Allotted, issued and fully paid ordinary shares</b>					
At 1 January 2012	–	1,407,601	–	13.9	–
Issued and allotted for employee share options pre-consolidation	–	68	–	–	–
Consolidation of shares	1,407,669	(1,407,669)	554,536	(13.9)	12.0
B shares repurchased and cancelled	(1,407,669)	–	–	–	–
Issued and allotted for employee share options post consolidation	–	–	1,062	–	–
Issued to shareholders of Agora	–	–	47,663	–	1.0
<b>At 1 January 2013</b>	–	–	<b>603,261</b>	–	<b>13.0</b>
Issued and allotted for employee share options	–	–	14	–	–
Shares repurchased and cancelled by Company	–	–	(8,218)	–	(0.2)
<b>At 31 December 2013</b>	–	–	<b>595,057</b>	–	<b>12.8</b>

### Share premium

Group and Company	2013 US\$m	2012 US\$m
At 1 January	486.9	483.7
Arising on shares issued for employee share options	–	3.2
<b>At 31 December</b>	<b>486.9</b>	486.9

### Share buy-back

Cairn announced a share buy-back in October 2013 and has entered into an irrevocable and non-discretionary arrangement with its brokers, Morgan Stanley and Jefferies, to repurchase on Cairn's behalf and within certain pre-set parameters, up to US\$300.0m of ordinary shares in the Company for cancellation, which will be reviewed by the Board on a quarterly basis. This share re-purchase arrangement follows shareholder approval for the Company to repurchase up to 14.99% of its issued share capital granted at the Company's Annual General Meeting on 16 May 2013, and in accordance with Chapter 12 of the UKLA Listing Rules and the Company's authorities to repurchase shares.

At the year end the first US\$50.0m irrevocable and non-discretionary arrangement with Cairn's brokers had been entered into. US\$36.3m of shares had been repurchased by the year end with the remaining US\$13.7m accrued. Estimated costs of this arrangement are US\$0.6m.

### Consolidation of shares and cash returned to shareholders

By special resolution effective from 6 February 2012 the share capital was subdivided and consolidated on the basis of 13 new ordinary shares of 231/169 pence for every 33 ordinary shares of 8/13 pence held. 1 B Share of 1/13 pence each was also issued for each ordinary share of 8/13 pence held at the time of the capital reorganisation. The B share scheme allowed Cairn to return to shareholders approximately US\$3.6 billion of cash in February and April 2012. All B shares were repurchased by Cairn and cancelled during 2012.

## Section 5 – Capital Structure and Other Disclosures

Continued

### 5.1 Issued Capital and Reserves – Continued

#### Shares held by ESOP Trust

Shares held by the ESOP Trust represent the cost of shares held by the Cairn Energy PLC Employees' Share Trust at 31 December 2013. The number of shares held by the Cairn Energy PLC Employees' Share Trust at 31 December 2013 was 4,965,135 (2012: 5,665,135) and the market value of these shares was £13.4m/US\$22.2m (2012: £15.0m/US\$24.4m).

#### Shares held by SIP trust

Shares held by the SIP Trust represent the cost of shares held by the Cairn Energy PLC Employees' Share Incentive Plan Trust at 31 December 2013. The number of shares held by the Cairn Energy PLC Share Incentive Plan Trust at 31 December 2013 was 938,846 (2012: 400,355) and the market value of these shares was £2.5m/US\$4.1m (2012: £1.1m/US\$1.8m).

#### Merger and capital reserves

The merger reserve of US\$255.9m arose in 2012 on shares issued by Cairn on the acquisition of Agora Oil and Gas AS. Capital reserves – non-distributable include non-distributable amounts arising on various Group acquisitions and the capital redemption reserve arising from the current share buy-back programme.

#### Available-for-sale reserve

The available-for-sale reserve represents fair value movements on the available-for-sale financial assets disclosed in section 3.1 less amounts recycled to the Income Statement as impairment.

#### Foreign currency translation

Unrealised foreign exchange gains and losses arising on consolidation of subsidiary undertakings are taken directly to reserves in accordance with IAS 21 'The Effects of Changes in Foreign Exchange Rates'. In accordance with IAS 21, foreign exchange differences arising on intra-group loans are not eliminated on consolidation; this reflects the exposure to currency fluctuations where the subsidiaries involved have differing functional currencies. These intra-group loans are not considered to be an investment in a foreign operation.

### 5.2 Capital Management

The objective of the Group's capital management structure is to ensure that there remains sufficient liquidity within the Group to carry out committed work programme requirements. The Group monitors the long-term cash flow requirements of the business in order to assess the requirement for changes to the capital structure to meet that objective and to maintain flexibility.

Cairn manages the capital structure and makes adjustments to it in light of changes to economic conditions. To maintain or adjust the capital structure, Cairn may buy-back shares, make a special dividend payment to shareholders, return capital, issue new shares for cash, repay debt, put in place new debt facilities or other such restructuring activities as appropriate. No significant changes were made in the objectives, policies or processes during the year ended 31 December 2013.

Capital and net debt were made up as follows:

	2013 US\$m	2012 US\$m
<b>Continuing operations</b>		
Trade and other payables	201.0	82.4
Loan and borrowings	55.3	29.6
Less cash and cash equivalents and bank deposits	(1,308.3)	(1,588.6)
Net funds less payables	(1,052.0)	(1,476.6)
Equity	3,187.8	3,641.7
Capital and net funds less payables	2,135.8	2,165.1
Gearing ratio	0%	0%

### 5.3 Staff Costs

	2013 US\$m	2012 US\$m
Wages and salaries	38.4	34.7
Social security costs and other taxes	4.8	3.6
Redundancy costs	0.3	5.4
Other pension costs	2.8	2.2
Share-based payments charge	14.0	9.3
	60.3	55.2

## Section 5 – Capital Structure and Other Disclosures

### Continued

#### 5.3 Staff Costs – Continued

Staff costs are shown gross before amounts recharged to joint ventures and include the costs of share-based payments. The share-based payments charge includes amounts in respect of both equity and cash-settled phantom options and associated National Insurance Contributions.

The average number of full time equivalent employees, including executive directors and individuals employed by the Group working on joint venture operations, was:

	Number of employees	
	2013	2012
UK	158	144
Norway	15	12
Spain	5	6
Greenland	12	12
Nepal	2	3
Morocco	1	-
Group	193	177

#### 5.4 Share-based Payments

##### Accounting Policy

The cost of awards to employees under Cairn's LTIP and share option plans are recognised over the three year period to which the performance relates. The amount recognised is based on the fair value of the shares as measured at the date of the award. The shares are valued using a Monte Carlo model with the exception of the SIP awards which have been valued using a Black Scholes model. Awards in prior years were valued using a binomial model.

The cost of equity-settled transactions is recognised, together with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award ('the vesting date'). The cumulative expense recognised for equity-settled transactions at each reporting date until the vesting date reflects the extent to which the vesting period has expired and the Company's best estimate of the number of equity instruments that will ultimately vest. The Income Statement charge or credit for a period represents the movement in cumulative expense as recognised at the beginning and end of that period.

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

The Group operates a number of share-based schemes for the benefit of its employees.

The number of share awards made by the Company during the year is given in the table below together with their weighted average fair value ('WAFV') and weighted average grant or exercise price ('WAGP/WAEP'):

	2013 WAFV £	2013 WAGP/ WAEP £	2013 Number of shares	2012 WAFV £	2012 WAGP/ WAEP £	2012 Number of shares
2010 SIP – free shares	2.50	2.82	129,578	2.40	2.80	122,100
2010 SIP – matching shares	2.50	2.79	121,474	2.40	2.95	100,374
2009 Approved Plan	0.72	2.78	485,814	1.24	2.86	378,900
2009 Unapproved Plan	0.72	2.78	4,277,846	1.24	2.88	3,739,577
2009 LTIP	1.35	2.78	5,648,805	1.15	2.88	4,877,721
2012 Share awards	-	-	-	3.35	3.05	300,000
			10,663,517			9,518,672

The analysis of the charge to the Income Statement in the year is:

	2013 US\$m	2012 US\$m
<b>Included within administrative expenses:</b>		
2010 SIP	0.9	0.3
2009 Approved Plan	0.6	0.7
2009 Unapproved Plan	3.6	2.3
2009 LTIP	8.3	5.4
2012 Share awards	0.6	1.1
	14.0	9.8

## Section 5 – Capital Structure and Other Disclosures

### Continued

#### 5.4 Share-based Payments – Continued

Details of those awards with a significant impact on the results for the current and prior years are given below together with a summary of the remaining awards.

Further details on assumptions and inputs applying to all share awards can be found in Appendix 4.

##### 2009 LTIP

The awards existing under the 2009 LTIP are detailed in the table below together with the weighted average grant price ('WAGP') at 31 December:

	2013		2012	
	Number	WAGP (£)	Number	WAGP (£)
Outstanding as at 1 January	9,337,452	3.50	8,987,604	3.33
Granted during the year	5,648,805	2.78	4,877,721	2.88
Lapsed during the year	(2,275,653)	4.29	(4,527,873)	2.49
<b>Outstanding at 31 December</b>	<b>12,710,604</b>	<b>3.04</b>	<b>9,337,452</b>	<b>3.50</b>
Weighted average remaining contractual life of outstanding awards	<b>1.6 years</b>		1.6 years	

##### Summary of all other LTIPs and share schemes

The awards existing under all share schemes other than the 2009 LTIP but including the SIP are detailed in the table below together with the weighted average of the grant price, exercise price and notional exercise prices ('WAGP/WAEP') at 31 December:

	2013		2012	
	Number	WAGP/WAEP (£)	Number	WAGP/WAEP (£)
Outstanding at 1 January	7,126,626	2.94	4,506,175	2.69
Consolidation of shares	-	-	(139,925)	3.93
Granted during the year	5,014,712	2.78	4,641,031	2.89
Vested/exercised during the year	(175,799)	2.94	(1,126,960)	1.84
Lapsed during the year	(953,713)	3.57	(753,695)	2.59
<b>Outstanding at 31 December</b>	<b>11,011,826</b>	<b>2.82</b>	<b>7,126,626</b>	<b>2.94</b>
Weighted average remaining contractual life of outstanding awards	<b>8.0 years</b>		7.8 years	

##### LTIP

The fair value of the 2009 LTIP scheme awards has been calculated using a binomial model, as described at Appendix 4. The main inputs to the model have been laid out in the appendix, though vesting percentages for LTIPs can be above 100%. For details on the vesting conditions attached to the LTIPs refer to the Directors' Remuneration Report on pages 94 to 96.

#### 5.5 Directors' Emoluments and Remuneration of Key Management Personnel

Details of each Director's remuneration, pension entitlements, share options and awards pursuant to the LTIP are set out in the Directors' Remuneration Report on pages 81 to 98. Directors' remuneration, their pension entitlements, and any share awards vested during the year is provided in aggregate in section 7.8.

##### Remuneration of key management personnel

The remuneration of the directors of the Company and of the members of the Management and Corporate teams who are the key management personnel of the Group is set out below in aggregate.

	2013 US\$m	2012 US\$m
Short-term employee benefits	10.2	10.0
Post-employment benefits	0.6	0.6
Share-based payments	5.3	0.7
	<b>16.1</b>	<b>11.3</b>

In addition employer's national insurance contributions for key management personnel in respect of short-term employee benefits were US\$1.3m (2012: US\$0.6m).

Share-based payments represent the cost to the Group of key management personnel's participation in the Company's share schemes, measured under IFRS 2.

## Section 5 – Capital Structure and Other Disclosures

Continued

### 5.6 Guarantees

It is normal practice for the Group to issue guarantees in respect of obligations during the normal course of business.

The Group provided the following guarantees at 31 December 2013:

- Various guarantees under the Group's bank facilities (see Appendix 3) for the Group's share of minimum work programme commitments for the current year of US\$33.8m (2012: US\$22.6m)
- Parent company guarantees for the Group's obligations under joint operating agreements and other contracts.

## Section 6 – Post Balance Sheet Events

---

### 6.1 Restriction on Sale of Available-for-sale Financial Asset

In January 2014, Cairn was contacted by the Indian Income Tax Department to provide information in relation to the year ending 31 March 2007. The information requested focused on the internal restructuring of the Cairn Group which took place prior to the IPO of Cairn India Limited in January 2007. Specifically, the Indian Income Tax Department is examining the taxable gain, if any, on the sale recorded in the 2006 year end accounts of the subsidiary that holds the Group's remaining ~10% interest in Cairn India Limited.

Cairn has re-confirmed with its advisers that throughout its history of operating in India the Group have been fully compliant with the tax legislation in force in each year. The Indian Income Tax Department are continuing their examination and presently there is no determination whether Cairn has any further liability to Indian taxation.

While interaction with the Indian Income Tax Department continues, Cairn has been restricted by the Indian Income Tax Department from selling its shares in Cairn India Limited.

Cairn classifies the remaining investment in Cairn India Limited as a non-current available-for-sale financial asset. This asset is measured at fair value at the Balance Sheet date. As the restriction was not effective at the year end, no adjustment is made to the fair value reflected in the Group's 31 December 2013 Balance Sheet.

### 6.2 Farm-down of Senegal Licences

On 9 January 2014, Cairn received formal approval for the farm-down agreement entered into with ConocoPhillips for 25% of its three contiguous blocks, Rufisque Offshore, Sangomar Offshore and Sangomar Deep, located offshore Senegal, West Africa where a 2,050km<sup>2</sup> 3D seismic survey has been used to identify prospects.

Cairn will operate the exploration phase with a reduced 40% working interest. The planned two well exploration programme will commence on completion of the operated drilling offshore Morocco using the Cajun Express rig. In the event of a commercial success, ConocoPhillips would have the option to apply to operate the future development of the resource.

Under the agreement, ConocoPhillips will pay Cairn a payment inclusive of a portion of back costs on the blocks, along with promoted terms of future exploration expenditure.

## Company Balance Sheet

As at 31 December 2013

	Section	2013 US\$m	2012 US\$m
<b>Non-current assets</b>			
Investments in subsidiaries	7.6	1,649.7	916.9
		<b>1,649.7</b>	916.9
<b>Current assets</b>			
Other receivables	7.3	309.9	1,060.7
Cash and cash equivalents	7.2	882.9	1,196.4
		<b>1,192.8</b>	2,257.1
<b>Total assets</b>		<b>2,842.5</b>	3,174.0
<b>Current liabilities</b>			
Trade and other payables	7.4	19.8	23.1
<b>Total liabilities</b>		<b>19.8</b>	23.1
<b>Net assets</b>		<b>2,822.7</b>	3,150.9
<b>Equity</b>			
Called-up share capital	5.1	12.8	13.0
Share premium	5.1	486.9	486.9
Shares held by ESOP/SIP Trusts		(28.0)	(28.7)
Capital reserves – non-distributable		0.3	0.1
Merger reserve		255.9	255.9
Retained earnings		2,094.8	2,423.7
<b>Total equity</b>		<b>2,822.7</b>	3,150.9

The financial statements on pages 133 to 146 were approved by the Board of Directors on 17 March 2014 and signed on its behalf by:



**Jann Brown**  
Managing Director & CFO



**Simon Thomson**  
Chief Executive

## Company Statement of Cash Flow

For the year ended 31 December 2013

	Section	2013 US\$m	2012 US\$m
<b>Cash flows from operating activities</b>			
(Loss)/profit before taxation		(291.6)	1,291.3
Share-based payments charge		4.0	3.3
Loss on disposal of investment in subsidiary		-	79.1
Impairment of investment in subsidiary		336.7	-
Net finance income		(59.8)	(1,383.0)
Interest paid		-	(0.1)
Other receivables movement		(324.6)	(434.4)
Trade and other payables movement		(0.4)	(1.8)
<b>Net cash used in operating activities</b>		<b>(335.7)</b>	<b>(445.6)</b>
<b>Cash flows from investing activities</b>			
Consideration paid for business combinations		-	(196.2)
Dividend received		57.7	1,313.6
Interest received		1.8	3.8
<b>Net cash from investing activities</b>		<b>59.5</b>	<b>1,121.2</b>
<b>Cash flows from financing activities</b>			
Return of cash to shareholders		-	(3,575.2)
Cost of shares purchased		(36.6)	(27.0)
Proceeds from exercise of share options		-	3.2
<b>Net cash flows used in financing activities</b>		<b>(36.6)</b>	<b>(3,599.0)</b>
Net decrease in cash and cash equivalents		(312.8)	(2,923.4)
Opening cash and cash equivalents at beginning of year		1,196.4	4,055.8
Exchange (losses)/gains on cash and cash equivalents		(0.7)	64.0
<b>Closing cash and cash equivalents</b>	7.2	<b>882.9</b>	<b>1,196.4</b>



## Company Statement of Changes in Equity

For the year ended 31 December 2013

	Equity share capital US\$m	Shares held by ESOP Trust and SIP Trust US\$m	Merger and capital reserves US\$m	Retained earnings US\$m	Total equity US\$m
At 1 January 2012	497.6	(1.7)	0.1	4,696.4	5,192.4
Profit for the year	-	-	-	1,291.3	1,291.3
Total comprehensive income for the year	-	-	-	1,291.3	1,291.3
Exercise of employee share options	3.2	-	-	-	3.2
Share-based payments	-	-	-	9.9	9.9
Shares issued for acquisitions	1.0	-	255.9	-	256.9
Return of cash to shareholders	(1.9)	-	-	(3,573.9)	(3,575.8)
Cost of shares purchased	-	(27.0)	-	-	(27.0)
At 31 December 2012	499.9	(28.7)	256.0	2,423.7	<b>3,150.9</b>
Loss for the year	-	-	-	(291.6)	<b>(291.6)</b>
Total comprehensive income for the year	-	-	-	(291.6)	<b>(291.6)</b>
Shares repurchased and cancelled	(0.2)	-	0.2	(50.6)	<b>(50.6)</b>
Share-based payments	-	-	-	14.0	<b>14.0</b>
Cost of shares vesting	-	0.7	-	(0.7)	-
<b>At 31 December 2013</b>	<b>499.7</b>	<b>(28.0)</b>	<b>256.2</b>	<b>2,094.8</b>	<b>2,822.7</b>

## Section 7 – Notes to the Company Financial Statements

This section contains the notes to the Company Financial Statements.

The issued capital and reserves of the Company are consistent with Cairn Energy PLC Group Financial Statements. Refer to section 5.1 of the Group Financial Statements.

### Key estimates and assumptions in this section:

#### Impairment testing of investments in subsidiaries

The Company's investments in subsidiaries have been tested for impairment by comparison against the underlying value of the subsidiaries' exploration/appraisal assets based on fair value calculated using the same assumptions as noted for the testing of goodwill impairment in section 2.4.

### 7.1 Basis of Preparation

The Financial Statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union.

The Company applies consistent accounting policies as applied by Group. To the extent that an accounting policy is relevant to both Group and Company Financial Statements, refer to the Group Financial Statements for disclosure of the accounting policy. Material policies that apply to the Company only are included as appropriate.

Cairn has used the exemption granted under s408 of the Companies Act 2006 that allows for the non-disclosure of the Income Statement of the parent company. The loss attributable to the Company for the year ended 31 December 2013 was US\$291.6m (year ended 31 December 2012: profit of US\$1,291.3m).

### 7.2 Net Funds

	2013 US\$m	2012 US\$m
Cash and cash equivalents	882.9	1,196.4
<b>Net funds</b>	<b>882.9</b>	<b>1,196.4</b>

### 7.3 Other Receivables

	2013 US\$m	2012 US\$m
Prepayments	0.3	0.4
Other receivables	1.8	0.5
Amounts owed by subsidiary undertakings	307.8	1,059.8
	<b>309.9</b>	<b>1,060.7</b>

As at 31 December 2013, no amount of the Company's other receivables and amounts owed by subsidiary undertakings were past due or impaired (2012: US\$1,059.8m > 120 days beyond due date; US\$5.0m between 30 and 120 days beyond due date).

During 2013 a provision for doubtful debts of US\$689.2m made in prior year was released when the net debt due from the subsidiary was capitalised. Refer to section 7.6 for further details on the capital contribution.

### 7.4 Trade and Other Payables

	2013 US\$m	2012 US\$m
Trade payables	0.1	0.2
Amounts owed to subsidiary undertakings	4.2	21.0
Other taxation and social security	1.1	1.5
Accruals	14.4	0.4
	<b>19.8</b>	<b>23.1</b>

Accruals include US\$14.0m in relation to the share buy-back programme. See section 5.1.

## Section 7 – Notes to the Company Financial Statements

### Continued

#### 7.5 Financial Instruments

Set out below is the comparison by category of carrying amounts and fair values of all the Company's financial instruments that are carried in the Financial Statements.

	2013 US\$m	2012 US\$m
<b>Financial assets: Carrying amount and fair value</b>		
<i>Loans and receivables</i>		
Cash and cash equivalents	882.9	1,196.4
Other receivables	1.8	0.5
Amounts owed by subsidiary undertakings	307.8	1,059.8
	<b>1,192.5</b>	<b>2,256.7</b>

All of the above financial assets are current and unimpaired with the exception of amounts owed by subsidiary undertakings to the Company. Details of the ageing of trade and other receivables are provided in section 7.3.

	2013 US\$m	2012 US\$m
<b>Financial liabilities: Carrying amount and fair value</b>		
<i>Amortised cost</i>		
Trade payables	0.1	0.2
Accruals	14.4	0.4
Amounts owed to subsidiary undertakings	4.2	21.0
	<b>18.7</b>	<b>21.6</b>

The fair value of financial assets and liabilities has been calculated by discounting the expected future cash flows at prevailing interest rates.

#### Maturity analysis

All of the Company's financial liabilities have a maturity of less than one year (2012: less than one year).

#### 7.6 Investments in Subsidiaries

##### Accounting policy

The Company's investments in subsidiaries are carried at cost less provisions resulting from impairment. In testing for impairment the carrying value of the investment is compared to its recoverable amount, being its fair value less costs of disposal. The fair value is based on the discounted future net cash flows of oil and gas assets held by the subsidiary, using estimated cash flow projections over the licence period. For exploration assets, the discounted cash flows are risk-weighted for future exploration success.

Discounted future net cash flows for IAS 36 purposes are calculated using an estimated short and long-term oil price of US\$90 per boe (2012: short and long-term oil price of US\$90 per boe), or the appropriate gas price as dictated by the relevant gas sales contract, escalation for prices and costs of 2.5%, and a discount rate of 10% (2012: 2.5% and 10% respectively).

	Subsidiary undertakings US\$m	Total US\$m
<b>Net book value</b>		
At 1 January 2012	536.3	536.3
Additions	459.8	459.8
Disposals	(79.2)	(79.2)
At 1 January 2013	916.9	<b>916.9</b>
Additions	1,069.5	<b>1,069.5</b>
Impairment	(336.7)	<b>(336.7)</b>
<b>At 31 December 2013</b>	<b>1,649.7</b>	<b>1,649.7</b>

Details of the Company's principal subsidiaries at the Balance Sheet date are included in appendix 2. A full list of subsidiaries can be found on the Annual Return.

## Section 7 – Notes to the Company Financial Statements

### Continued

#### 7.6 Investments in Subsidiaries – Continued

Additions during the year included US\$1,059.8m capital contribution by Cairn Energy PLC which reduced the amounts owed to the Company by Capricorn Oil Limited.

A further US\$9.7m (2012: US\$6.7m) was recognised as additions relating to Capricorn Oil Limited for the award of share options of the Company to the employees of Capricorn Energy Limited (a principal subsidiary of Capricorn Oil Limited).

During 2012, the Company acquired 100% of the share capital of Agora Oil and Gas AS. Subsequently, this subsidiary was transferred to Capricorn Oil Limited through a share-for-share exchange. Additions during 2012 therefore include US\$453.1m on the acquisition of Agora. Disposals represents the fall in the fair value of Agora Oil and Gas AS at the time of the transfer to Capricorn Oil Limited, which issued 240,051,347 shares of £1 each at par as consideration for the transaction.

Consideration of US\$453.1m for the purchase of Agora Oil and Gas AS included US\$196.2m settled in cash.

At the year end, investments in subsidiaries were reviewed for indicators of impairment and impairment tests conducted where indicators found. Cairn Energy PLC's investment in Capricorn Oil Limited was impaired to reflect the fair value of the underlying assets of the Capricorn Oil Group. A charge of US\$336.7m was made to the Company's Income Statement.

#### 7.7 Capital Management

The objective and management of the Company's capital structure is consistent with the Group. Refer to section 5.2.

Capital and net debt were made up as follows:

	2013 US\$m	2012 US\$m
Trade and other payables	19.8	23.1
Less cash and cash equivalents	(882.9)	(1,196.4)
Net funds less payables	(863.1)	(1,173.3)
Equity	2,822.7	3,150.9
Capital and net funds less payables	1,959.6	1,977.6
Gearing ratio	0%	0%

#### 7.8 Related Party Transactions

The Company's principal subsidiaries are listed in Appendix 2. The following table provides the Company's balances which are outstanding with subsidiary companies at the Balance Sheet date:

	2013 US\$m	2012 US\$m
Amounts owed from subsidiary undertakings	307.8	1,059.8
Amounts owed to subsidiary undertakings	(4.2)	(21.0)
	303.6	1,038.8

The amounts outstanding are unsecured, repayable on demand and will be settled in cash. Interest, where charged, is at market rates. No guarantees have been given.

During the year the Company made a capital contribution to Capricorn Oil Limited (a subsidiary) of US\$1,059.8m which reduced the amounts owed to the Company by Capricorn Oil Limited.

A further US\$9.7m (2012: US\$6.7m) was recognised as additions to investments relating to Capricorn Oil Group for the award of share options of the Company to the employees of Capricorn Energy Limited (a principal subsidiary of Capricorn Oil Limited).

The following table provides the Company's transactions with subsidiary companies recorded in the loss (2012: profit) for the year:

	2013 US\$m	2012 US\$m
Amounts invoiced to subsidiaries	8.4	8.7
Amounts invoiced by subsidiaries	2.2	6.4
Dividend received from subsidiary	57.7	1,313.6

## Section 7 – Notes to the Company Financial Statements

Continued

### 7.8 Related Party Transactions – Continued

#### Directors' Remuneration

The remuneration of the directors of the Company is set out below. Further information about the remuneration of individual directors is provided in the audited part of the Directors' Remuneration Report on pages 91 to 97.

	2013 US\$m	2012 US\$m
Emoluments	4.8	5.1
	4.8	5.1

Pension contributions were made on behalf of directors in 2013 of US\$0.2m (2012: US\$0.2m).

No share awards to directors vested during 2013 (2012: none).

#### Other transactions

During the year the Company did not make any purchases in the ordinary course of business from an entity under common control (2012: US\$nil).

# Appendices to the Group and Company Financial Statements

## Appendix 1 – Prior Year Corporate Acquisitions

### Agora Oil & Gas AS

On 9 May 2012, Cairn Energy PLC completed the acquisition of 100 per cent of the issued share capital of Agora Oil & Gas AS. Agora Oil & Gas AS was a private Norwegian company with non-operated exploration assets in both the Norwegian North Sea and, through its wholly owned subsidiary Agora Oil and Gas (UK) Limited, in the United Kingdom North Sea. The acquisition included Agora's 15% stake in the Catcher asset and its 20% interest in the Skarfjell discovery.

### Nautical Petroleum plc

On 8 August 2012, Capricorn Energy completed the acquisition of 100 per cent of the issued share capital of Nautical Petroleum plc. Nautical was an independent oil and gas exploration and production company, incorporated in England and Wales and headquartered in London. Nautical's assets include exploration assets nearing development in the United Kingdom North Sea (including interests in the Catcher, Kraken and Mariner fields) and further exploration licences in the United Kingdom, Ireland, France and Morocco. The acquisition increased Cairn's equity position in the Catcher area by a further 15%, taking Cairn's overall interest to 30%.

Recognised amounts of identifiable assets and liabilities acquired	Agora Oil and Gas AS Fair value US\$m	Nautical Petroleum plc Fair value US\$m
Intangible exploration/appraisal assets	411.0	565.5
Property, plant and equipment – other	0.5	-
Income tax assets	30.4	-
Other receivables	25.7	11.3
Bank deposits	-	7.8
Cash and cash equivalents	41.4	82.5
Trade and other payables	(48.7)	(2.4)
Bank loan	(6.2)	-
Provisions	-	(6.6)
Deferred tax liability	(215.3)	(269.4)
<b>Total identifiable assets</b>	<b>238.8</b>	<b>388.7</b>
Goodwill	214.3	259.6
<b>Total consideration</b>	<b>453.1</b>	<b>648.3</b>
Satisfied by:		
Cash	196.2	648.3
Equity instruments (47,662,603 ordinary shares of Cairn Energy PLC)	256.9	-
<b>Total consideration transferred</b>	<b>453.1</b>	<b>648.3</b>
Net cash outflow arising on acquisition:		
Cash consideration	(196.2)	(648.3)
Less: cash and cash equivalent balances acquired	41.4	82.5
	<b>(154.8)</b>	<b>(565.8)</b>

## Appendices to the Group and Company Financial Statements

Continued

### Appendix 1 – Prior Year Corporate Acquisitions – Continued

#### Goodwill

The goodwill of US\$214.3m recognised on the acquisition of Agora Oil and Gas AS arises largely from deferred tax provided of US\$196.6m on the temporary taxable difference between the fair value of intangible exploration/appraisal assets acquired and their respective tax base costs.

Similarly, the goodwill of US\$259.6m recognised on the acquisition of Nautical also arises largely from deferred tax provided of US\$269.4m on the temporary taxable difference between the fair value of intangible exploration/appraisal assets acquired and their respective tax base costs.

None of the goodwill is expected to be deductible for income tax purposes.

#### Consideration and costs of acquisition

The fair value of the 47,662,603 ordinary shares issued as part of the consideration paid for Agora Oil and Gas AS (US\$256.9m) was determined on the basis of Cairn Energy PLC's closing share price on 9 May 2012 of £3.39 (US\$5.39). All other consideration was settled in cash.

Acquisition costs of US\$11.2m are included within other expenses. US\$4.3m relates to the acquisition of Agora with the remaining US\$6.9m relating to Nautical.

#### Impact on profit for the year

The Group's profit has been reduced by the Agora Group loss of US\$53.7m and reduced by the Nautical Group loss of US\$4.4m for the period between the respective dates of acquisition and 31 December 2012.

Had the results of both Nautical Petroleum plc and Agora Oil and Gas AS and their subsidiaries been included in the full year's results to 31 December 2012, Cairn's profit for the year would have been US\$60.6m.

## Appendices to the Group and Company Financial Statements

Continued

### Appendix 2 – Principal Subsidiary Undertakings

The Company's principal subsidiaries as at the Balance Sheet date are set out below. A full list of subsidiaries can be found on the Annual Return. The Company holds 100% of the voting rights and ordinary shares of the following Companies:

	Principal activity	Country of incorporation	Country of operation
<b>Direct holdings</b>			
Capricorn Oil Limited	Holding company	Scotland	Scotland
Cairn UK Holdings Limited	Holding company	Scotland	Scotland
<b>Indirect holdings – Capricorn Oil Limited Group</b>			
Capricorn Energy Limited	Holding company	Scotland	Scotland
Cairn Energy Dhangari Limited	Exploration	Scotland	Nepal
Cairn Energy Karnali Limited	Exploration	Scotland	Nepal
Cairn Energy Lumbini Limited	Exploration	Scotland	Nepal
Cairn Energy Malangawa Limited	Exploration	Scotland	Nepal
Cairn Energy Birganj Limited	Exploration	Scotland	Nepal
Capricorn Spain Limited	Exploration	Scotland	Spain
Capricorn Malta Limited	Exploration	Scotland	Malta
Capricorn Greenland Exploration A/S	Exploration	Greenland	Greenland
Capricorn Exploration and Development Company Limited	Exploration	Scotland	Morocco
Capricorn Mauritania Limited	Exploration	Scotland	Mauritania
Capricorn Senegal Limited	Exploration	Scotland	Senegal
Capricorn Ireland Limited	Exploration	Scotland	Ireland
Capricorn Norge AS	Exploration	Norway	Norway
Nautical Petroleum Limited	Exploration	England	UK
Nautical Petroleum AG	Exploration and development	Switzerland	UK
Agora Oil and Gas (UK) Limited	Exploration	Scotland	UK



## Appendices to the Group and Company Financial Statements

Continued

### Appendix 3 – Financial Risk Management: Objectives and Policies

#### Group and Company

The main risks arising from the Company's and the Group's financial instruments are liquidity risk, credit risk and market risk arising including equity price fluctuations, interest rate risk and foreign currency risk. The Board of Cairn Energy PLC reviews and agrees policies for managing each of these risks and these are summarised below.

The Group's treasury function and Executive Team as appropriate are responsible for managing these risks, in accordance with the policies set by the Board. Management of these risks is carried out by monitoring of cash flows, investment and funding requirements using a variety of techniques. These potential exposures are managed whilst ensuring that the Company and the Group have adequate liquidity at all times in order to meet their immediate cash requirements. There are no significant concentrations of risks unless otherwise stated.

The primary financial instruments comprise bank loans, cash, short and medium-term deposits, certificates of deposit, money market liquidity, listed equity shares, intra-group loans and other receivables and financial liabilities held at amortised cost. The Group's strategy has been to finance its operations through a mixture of retained profits and bank borrowings. Other alternatives such as equity and other forms of non-investment-grade debt finance are reviewed by the Board, when appropriate.

#### Liquidity risk

The Group currently has surplus cash which it has placed in a combination of money market liquidity funds and term deposits with a number of international and UK financial institutions, ensuring sufficient liquidity to enable the Group to meet its short/medium-term expenditure requirements. The Group is conscious of the current environment and constantly monitors counterparty risk. Policies are in place to limit counterparty exposure and maturity. The Group monitors counterparties using published ratings and other measures. Repayment of principal is the overriding priority and this is achieved by diversification and shorter maturities to provide flexibility.

At the year end the Group has a NOK 500m Exploration Finance Facility with SEB (Stockholm's Enskilda Bank) based on floating NIBOR ('Norwegian InterBank Offered Rate') rates. Cairn entered into this facility through the acquisition of Agora Oil and Gas AS, now Capricorn Norge AS. Under the facility Capricorn Norge AS can draw 95% of the tax refund due on Norwegian exploration expenditure in the year. At the year end US\$55.3m (NOK 335m) was drawn under this facility. The facility was repaid in full and cancelled on 20 January 2014.

At 31 December 2012 Cairn Energy PLC Group had a total of US\$55.0m of facilities in place to cover the issue of performance guarantees. During the year these facilities were increased to US\$60.0m. Fixed rates of bank commission and charges applied to these facilities. US\$33.8m was utilised as at 31 December 2013. On 21 February 2014 the facilities were further increased to US\$100.0m.

Cairn Energy PLC also issued a US\$100.0m letter of credit on 22 July 2013 as required under the membership of the Oil Spill Response Scheme's 'Cap and Contain' arrangement. This guarantee is cash backed with US\$100.0m being placed with BNP Paribas to support the letter of credit.

#### Interest rate risk

Surplus funds are placed on short/medium-term deposits at floating rates. It is Cairn's policy to invest with banks or other financial institutions that first of all offer what is perceived as the greatest security and, second, the most competitive interest rate. Managing counterparty risk is considered the priority.

Short/medium-term borrowing arrangements are generally entered into at floating rates. From time to time the Group may opt to manage a proportion of the interest costs by using derivative financial instruments like interest rate swaps. At this time, however, there are no such instruments (2012: none).

The following table demonstrates the sensitivity of the Group's loss before tax to a change in interest rates (through the impact on floating rate borrowings and investments).

	2013 Effect on equity and loss before tax US\$m	2012 Effect on equity and loss before tax US\$m
50 point increase in interest rates	8.9	12.8
50 point decrease in interest rates	(2.1)	(3.8)

#### Foreign currency risk

Cairn manages exposures that arise from non-functional currency receipts and payments by matching receipts and payments in the same currency and actively managing the residual net position. Generally the exposure has been limited given that receipts and payments have mostly been in US dollars and the functional currency of most companies in the Group is US dollars.

The Group also aims where possible to hold surplus cash, debt and working capital balances in functional currency which in most cases is US dollars, thereby matching the reporting currency and functional currency of most companies in the Group. This minimises the impact of foreign exchange movements on the Group's Balance Sheet.

## Appendices to the Group and Company Financial Statements

Continued

### Appendix 3 – Financial Risk Management: Objectives and Policies – Continued

Where residual net exposures do exist and they are considered significant the Company and Group may from time to time, opt to use derivative financial instruments to minimise its exposure to fluctuations in foreign exchange and interest rates.

The following table demonstrates the sensitivity to movements in the US\$:GBP exchange rates, with all other variables held constant, on the Group's and the Company's monetary assets and liabilities. The Group's and the Company's exposure to foreign currency changes for all other currencies is not material.

Group	2013		2012	
	Effect on loss before tax US\$m	Effect on Equity US\$m	Effect on loss before tax US\$m	Effect on Equity US\$m
10% increase in Sterling to US\$	9.2	41.4	112.1	74.6
10% decrease in Sterling to US\$	(9.2)	(41.4)	(112.1)	(74.6)

Company	2013		2012	
	Effect on loss before tax US\$m	Effect on Equity US\$m	Effect on profit before tax US\$m	Effect on Equity US\$m
10% increase in Sterling to US\$	93.5	93.5	91.0	91.0
10% decrease in Sterling to US\$	(93.5)	(93.5)	(91.0)	(91.0)

#### Credit risk

Credit risk arises from cash and cash equivalents, deposits with banks and financial institutions and joint ventures.

Joint venture partners are subject to a risk assessment using publicly available information and credit reference agencies, with follow up due diligence and monitoring if required.

Investment credit risk for investments with banks and other financial institutions is managed by the Group Treasury function in accordance with the Board approved policies of Cairn Energy PLC. Investments of surplus funds are only made with approved counterparties who meet the appropriate rating and/or other criteria, and are only made within approved limits. The Board continually re-assesses the Group's policy and updates as required. The limits are set to minimise the concentration of risks and therefore mitigate financial loss through counterparty failure.

At the year end the Group does not have any significant concentrations of bad debt risk. As at 31 December 2013 the Group had investments with 33 counterparties (2012: 32) to ensure no concentration of counterparty investment risk. The maturity of these investments ranged from instant access to three months.

The maximum credit risk exposure relating to financial assets is represented by the carrying value as at the Balance Sheet date.

#### Market risk: equity price risk

The Group is exposed to equity price risks arising from the listed equity investments it holds in Cairn India Limited. Equity investments are held for strategic rather than trading purposes and the Group does not actively trade these investments, which are classified as available-for-sale.

Movements in the fair value during the year are recognised directly in equity and are disclosed in the Statement of Comprehensive Income. The cumulative gain or loss that arises on disposal of available-for-sale financial assets is recycled through the Income Statement.

Further details on the impact of equity price movements on the fair value of the available-for-sale financial assets are included in section 3.1.

## Appendices to the Group and Company Financial Statements

Continued

### Appendix 4 – Share-based Payments

#### Cairn Energy PLC Group and Company

The schemes below apply for both Group and Company.

Cairn Energy PLC share options were exercised on a regular basis throughout the year, subject to the normal employee dealing bans imposed at certain times by the Company. The weighted average share price during the year was £2.753 (2012: £2.987).

The Cairn Energy PLC share awards during 2013 were valued using a Monte Carlo model with the exception of the SIP awards which were valued using a Black Scholes model. Awards in prior years were valued using a binomial model.

The main inputs to the models include the number of options, share price, leaver rate, trigger points, discount rate and volatility.

- Leaver rate assumptions are based on past history of employees leaving the Company prior to options vesting and are revised to equal the number of options that ultimately vest.
- Trigger points are based on the length of time after the vesting periods for awards in 2013. Awards in prior years have trigger points based on the profit points at which the relevant percentage of employees are assumed to exercise their options.
- The risk-free rate is based on the yield on a zero coupon Government bond with a term equal to the expected term on the option being valued.
- Volatility was determined as the annualised standard deviation of the continuously compounded rates of return on the shares of a peer group of similar companies selected from the FTSE, as disclosed in the Directors' Remuneration Report on page 96, over a 10 year period to the date of award.

The following assumptions and inputs apply to the share plans detailed in section 5.4:

Scheme name	Volatility	Risk-free rate per annum	Lapse due to withdrawals per annum
2010 Share Incentive Plan	34% – 52%	0% – 0.69%	5%
2009 Approved and Unapproved Plans	34% – 52%	0.29% – 4.4%	5%
2009 LTIP	34% – 52%	0% – 0.29%	0% – 5%
2012 Share awards	34% – 52%	–	5%

#### Employee exercise trigger point assumptions

For 2013 awards, the assumption used for all schemes other than the SIP is that employees will exercise half of the awards on the vesting date and the remaining half will be exercised equally each year over the following seven years. The assumption used for the valuation of the SIP is that employees will withdraw shares five years after the award date.

The following assumptions on employee exercise trigger points are applicable to all awards made before 31 December 2012:

	25% profit	50% profit	75% profit	100% profit	125% profit	No trigger
Percentage of employees exercising options	15%	25%	25%	15%	10%	10%

For details on the vesting conditions attached to the LTIPs refer to the Directors' Remuneration Report on pages 94 to 96.

# Appendices to the Group and Company Financial Statements

Continued

## Appendix 5 – Auditors' Remuneration

Cairn put its external audit services contract out to tender in September 2012 and in March 2013 PwC LLP were appointed auditors of the Group, replacing Ernst & Young LLP. The analysis below analyses the fees paid to each firm during their time as auditor.

	2013 US\$'000	2012 US\$'000
<b>Ernst &amp; Young LLP</b>		
Fees payable to the Group's auditors and its associate firms for:		
Audit of parent company and consolidated financial statements	86	278
Audit of Group companies pursuant to legislation	258	301
Tax advisory and other services	66	366
<b>PwC LLP</b>		
Fees payable to the Group's auditors and its associate firms for:		
Audit of parent company and consolidated financial statements	246	-
Audit of Group companies pursuant to legislation	139	-
Tax advisory and other services	13	-

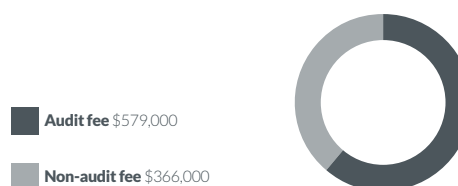
The Group has a policy in place for the award of non-audit work to the auditors which, in certain circumstances, requires Audit Committee approval (see the Report of the Audit Committee on page 80).

The split of audit fees to non-audit fees payable to the auditor is as follows:

### 2013 Fees to auditors



### 2012 Fees to auditors



## Cairn Group Licence List

As at 31 December 2013

Country	Block/Licence	Operator	Cairn Interest (%)
<b>Mauritania</b>	Block C19	Chariot	35.00
<b>Morocco</b>	Juby Maritime (I, II, III)	Cairn	37.50
<b>Morocco</b>	Foum Draa Offshore (1, 2, 3)	Cairn	50.00
<b>Nepal</b>	Blocks 1, 2, 4, 6 & 7	Cairn	100.00
<b>Senegal</b>	Rufisque Offshore, Sangomar Offshore and Sangomar Deep	Cairn	40.00
<b>France</b>	Gex	eCORP	20.00
<b>France</b>	St. Laurent	Egdon	22.00
<b>Greenland</b>	2002/15 (Atammik)	Cairn	87.50
<b>Greenland</b>	2005/06 (Lady Franklin)	Cairn	87.50
<b>Greenland</b>	2008/10 (Sigguk)	Cairn	87.50
<b>Greenland</b>	2008/11 (Eqqua)	Cairn	87.50
<b>Greenland</b>	2008/13 (Saqqamiut)	Cairn	92.00
<b>Greenland</b>	2008/14 (Kingittoq) (See Note 10)	Cairn	92.00
<b>Greenland</b>	2009/10 (Uummannarsuaq) (See Note 10)	Cairn	92.00
<b>Greenland</b>	2009/11 (Salliit)	Cairn	92.00
<b>Greenland</b>	2011/13 (Pitu)	Cairn	56.875
<b>Greenland</b>	2011/16 (Napariaq) (See Note 13)	Cairn	87.50
<b>Greenland</b>	2011/17 (Ingoraq) (See Note 13)	Cairn	87.50
<b>Republic of Ireland</b>	FEL 2/04	Cairn	38.00
<b>Republic of Ireland</b>	FEL 4/08	Cairn	38.00
<b>Republic of Ireland</b>	LO 11/2 (See Note 4)	Cairn	38.00
<b>Malta</b>	Area 3 (Blocks 1, 2, 3)	Cairn	60.00
<b>Spain</b>	B	Cairn	100.00
<b>Spain</b>	G	Cairn	100.00
<b>Spain</b>	AM 1	Cairn	100.00
<b>Spain</b>	AM 2	Cairn	100.00

## Cairn Group Licence List

As at 31 December 2013

Continued

Country	Block/Licence	Operator	Cairn Interest (%)
Norway	PL159c (Block 6507/3)	Statoil	18.00
Norway	PL299 (Block 2/1)	Talisman	28.50
Norway	PL378 (Block 35/12)	Wintershall	20.00
Norway	PL378b (Block 35/12)	Wintershall	20.00
Norway	PL418 (Blocks 35/8 and 35/9)	Wintershall	20.00
Norway	PL497 (Blocks 7/7, 7/8 and 7/11)	DNO	15.00
Norway	PL497B (Blocks 7/8 and 7/11)	DNO	15.00
Norway	PL630 (Blocks 31/1 and 35/10)	Statoil	20.00
Norway	PL632 (Block 33/9)	Statoil	40.00
Norway	PL665 S (Blocks 2/2, 2/3 and 3/1)	Faroe Petroleum	20.00
Norway	PL682 (Block 35/9)	Bayerngas	10.00
UK (Onshore)	PEDL005 (Blocks TF/38b and TF/49b)	Egdon	10.00
UK (Onshore)	PEDL118 (Blocks SK/65c and SK/66d)	Egdon	15.00
UK (Onshore)	PEDL203 (Block SK/65b)	Egdon	15.00
UK (Offshore)	P218 (Block 15/21a GAMMA)	Premier	21.00
UK (Offshore)	P1077 (Block 9/2b)	EnQuest	25.00
UK (Offshore)	P1430 (Blocks 28/9a and 28/10c)	Premier	30.00
UK (Offshore)	P1463 (Block 14/30a)	Premier	20.00
UK (Offshore)	P1482 (Blocks 113/26b and 113/27c)	Serica	10.00
UK (Offshore)	P1632 (Block 211/8c)	Ithaca	40.00
UK (Offshore)	P1633 (Blocks 211/11b and 211/16b)	MPX North Sea	27.78
UK (Offshore)	P1655 (Block 15/21g)	Premier	21.00
UK (Offshore)	P1659 (Block 20/7a)	Nexen	19.00
UK (Offshore)	P1759 (Block 9/1a)	Cairn	100.00
UK (Offshore)	P1763 (Blocks 9/9d, 9/14a and 9/15d)	MPX North Sea	30.00 (See Note 5)
UK (Offshore)	P1887 (Blocks 12/16b and 12/17b)	First Oil	20.00

## Cairn Group Licence List

As at 31 December 2013

Continued

Country	Block/Licence	Operator	Cairn Interest (%)
<b>UK (Offshore)</b>	P1918 (Blocks 97/14, 97/15 and 98/11)	Infrastrata	10.00 (See Note 2)
<b>UK (Offshore)</b>	P1995 (Blocks 210/25b, 211/21b and 211/26b)	TAQA	50.00
<b>UK (Offshore)</b>	P2075 (Blocks 211/19b and 211/24c)	Statoil	40.00
<b>UK (Offshore)</b>	P2070 (Block 28/4a)	Premier	46.00
<b>UK (Offshore)</b>	P2077 (Block 28/8)	Premier	46.00
<b>UK (Offshore)</b>	P2086 (Blocks 28/9b and 28/14)	Premier	35.00 (See Note 8)
<b>UK (Offshore)</b>	P2040 (Block 29/11)	Premier	35.00 (See Note 9)
<b>UK (Offshore)</b>	P1976 (Blocks 8/5 and 9/1b)	EnQuest	40.00
<b>UK (Offshore)</b>	P1991 (Block 14/30c)	Endeavour	20.00
<b>UK (Northern Ireland Onshore)</b>	PL1/10	Infrastrata	20.00 (See Note 12)

### Notes

- Cairn has entered into a new licence P2123 for blocks 111/1, 111/2, 111/7, 125/30 and 126/26. Cairn is operator and holds a 40% interest. An agreement has been reached to transfer this 40% interest and operatorship to InfraStrata, subject to government approval.
- Cairn completed the transfer of this 10% interest in P1918 to InfraStrata on 28 February 2014.
- Cairn has entered into a farm-in agreement with Kosmos Energy and the Moroccan National Oil Company for a 20% non-operated interest in the Cap Boujdour block offshore North West Africa which is scheduled for drilling in H2 2014. This is now subject to government approval.
- The Irish Government has accepted an application to convert licence option 11/2 to an exploration licence (FEL 1/14) (Cairn has a 38% working interest and will be Operator).
- Cairn has agreed to acquire a 2.5% working interest in Licence P1763 on the United Kingdom Continental Shelf from MPX.
- Cairn has agreed to acquire a 20% working interest in Licence PL248C on the Norwegian Continental Shelf from Statoil. This is subject to partner and government approval.
- Cairn has agreed to acquire a 20% working interest in Licence PL420B on the Norwegian Continental Shelf from Statoil. This is subject to partner and government approval.
- Cairn has agreed to transfer 25% of its working interest in UKCS Licence P2086 to Statoil. This is subject to partner and government approval.
- Cairn has agreed to transfer 25% of its working interest in UKCS Licence P2040 to Statoil. This is subject to partner and government approval.
- Cairn has issued a relinquishment notice in respect of Greenland Licences 2008/14 (Kingittoq) and 2009/10 (Ummannarsuaq) and these relinquishments are currently being considered by the regulatory authorities.
- Cairn has successfully received three awards from three applications in the 2013 APA licensing round in the Norwegian North Sea.
- Cairn has entered into an agreement to transfer this 20% interest in PL1/10 to InfraStrata and this is now subject to government approval.
- Cairn has issued a relinquishment notice in respect of Greenland Licences 2011/16 (Napariaq) and 2011/17 (Ingoraq) and these relinquishments are currently being considered by the regulatory authorities.

## Glossary

The following are the main terms and abbreviations used in this announcement:

Corporate		Other	
Board	the Board of Directors of Cairn Energy PLC	2C	best estimate of contingent resources
Cairn	Cairn Energy PLC and/or its subsidiaries as appropriate	2D/3D	two dimensional/three dimensional
Cairn India/CIL	Cairn India Limited and/or its subsidiaries as appropriate	2P	proven plus probable
Capricorn	Capricorn Oil Limited and/or its subsidiaries as appropriate	AGM	Annual General Meeting
Company	Cairn Energy PLC	ALARP	as low as reasonably practicable
Group	the Company and its subsidiaries	APA	awards in predefined area
		bbl	barrel
		boe	barrel(s) of oil equivalent
		boepd	barrel(s) of oil equivalent per day
		bopd	barrels of oil per day
		CR	Corporate Responsibility
		CRMS	Corporate Responsibility management system
		DC	drill centre
		DECC	Department of Energy and Climate Change
		ESA	exploration study agreement
		EIA	Environmental Impact Assessment
		EITI	Extractive Industries Transparency Initiative
		ESIA	Environmental and Social Impact Assessment
		FDP	field development plan
		FEED	front end engineering design
		FEL	frontier exploration licence
		FPSO	floating production, storage and offloading
		GMT	Greenwich Mean Time
		HSE	Health, safety and environment
		IFRS	International Financial Reporting Standards
		JV	joint venture
		KPI	key performance indicator
		LTI	lost time incident/injury
		mmbbls	million barrels of oil
		mmboe	million barrels of oil equivalent
		mmbopd	million barrels of oil per day
		mmscfd	million standard cubic feet of gas per day
		ONHYM	Office National des Hydrocarbures et des Mines
		PCDP	Public Consultation and Disclosure Plan
		PDP	Project Delivery Process
		TVDSS	total vertical depth sub sea
		UKCS	UK Continental Shelf
		US\$	US dollar
		WI	working interest



## Notes

## Notes

## Company Information

### Financial Advisers

#### **N M Rothschild & Sons Limited**

New Court  
St Swithin's Lane  
London  
EC4N 8AL

### Secretary

#### **Duncan Wood LLB**

### Solicitors

#### **Shepherd and Wedderburn LLP**

1 Exchange Crescent  
Conference Square  
Edinburgh  
EH3 8UL

### Auditor

#### **PricewaterhouseCoopers LLP**

141 Bothwell Street  
Glasgow  
G2 7EQ

### Stockbrokers

#### **Jefferies**

Vintners Place  
68 Upper Thames Street  
London  
EC4V 3BJ

#### **Morgan Stanley**

20 Bank Street  
Canary Wharf  
London  
E14 4AD

### Registrars

#### **Equiniti**

Aspect House  
Spencer Road  
Lancing  
West Sussex  
BN99 6DA  
T 0871 384 2030

#### **Overseas shareholder helpline number**

T +44 121 415 7047

[www.shareview.co.uk](http://www.shareview.co.uk)



Printed on FSC-recognised paper, produced from sustainably managed forests. This report was printed with vegetable oil-based inks by an FSC-recognised printer that holds an ISO 14001 accreditation.

These materials contain forward-looking statements regarding Cairn, our corporate plans, future financial condition, future results of operations, future business plans and strategies. All such forward-looking statements are based on our management's assumptions and beliefs in the light of information available to them at this time. These forward-looking statements are, by their nature, subject to significant risks and uncertainties and actual results, performance and achievements may be materially different from those expressed in such statements. Factors that may cause actual results, performance or achievements to differ from expectations include, but are not limited to, regulatory changes, future levels of industry product supply, demand and pricing, weather and weather-related impacts, wars and acts of terrorism, development and use of technology, acts of competitors and other changes to business conditions. Cairn undertakes no obligation to revise any such forward-looking statements to reflect any changes in Cairn's expectations with regard thereto or any change in circumstances or events after the date hereof.



