Cairn

Delivering a balanced business

from exploration and development

Cairn Energy PLC Annual Report and Accounts 2016

Cairn Energy PLC is an independent, UK-based oil and gas exploration and development company.

Cairn has explored, discovered, developed and produced oil and gas in a variety of locations throughout the world with more than 20 years' experience as operator and partner in all stages of the oil and gas lifecycle. Cairn is listed on the London Stock Exchange with its headquarters in Edinburgh and offices in London, Norway and Senegal.

Cairn's strategy is to deliver value for stakeholders by building and maintaining a balanced portfolio of exploration, development and production assets within the oil and gas lifecycle. Cairn's exploration focus is on frontier and emerging basins acreage from which the greatest value can be created. The Group's production assets provide the cash flow to sustain exploration and development activity.

Exploration focus

Senegal

6 wells

drilled (as at 31.12.16)

201.4 mmboe

2C resources (as at 31.12.16)

Development and future production focus

UK & Norway

Kraken & Catcher

~25,000 boepd

peak net targeted production to Cairn

51.5 mmboe

2P reserves (as at 31.12.16)

discover more at
cairnenergy.com/ar2016

Strategic Report

Leadership and Governance

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Additional Information

"We are committed to working responsibly as part of our strategy to deliver value for all stakeholders. This means working in a safe, secure, environmentally and socially responsible manner.

During 2016, we made good progress against our strategic objectives, increasing the recently discovered, significant Senegal resource base and progressing our North Sea developments through to first oil and future cash flow in 2017 and beyond."

IAN TYLER
Chairman

The Year at a Glance

Building a portfolio of exploration, development and production assets

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Business Model & Strategy

Working responsibly and managing risk are a key part of our strategy

Business model

To create, add and realise value for stakeholders through the exploration, development and production of oil and gas within a self-funding business model. Exploration offers material value upside potential to stakeholders and production provides the cash flow to sustain exploration and development.

Strategy

To deliver value for stakeholders by building and maintaining a balanced portfolio of exploration, development and production assets.

To maximise value, exploration is focused on frontier and emerging basins acreage from which the greatest value can be created. Cairn is currently focused on growing its Senegal resource base, and on progressing its North Sea developments to first oil and cash flow which is targeted in 2017.

Strategic objectives

Annual Key Performance Indicators (KPIs) identify the Company's strategic objectives and how they can be met, enabling the Company to measure its delivery of strategy.

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Managing risk

Cairn has a robust risk management process in place to identify, monitor and mitigate risk and to identify opportunities. This means first determining risk appetite, and then identifying the key risks.

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Working responsibly

52 Read more: Working Responsibly on P52-71

The 'Maintain licence to operate' KPI measures the Company's ability to work responsibly and means delivering value in a safe, secure, environmentally and socially responsible manner. Working responsibly means identifying and managing issues that are material not only to the Company but also to stakeholders.

Create Value
Cairn identifies assets it can add value to through exploration activity including 3D seismic and drilling as part of a focused exploration strategy. If successful, exploration activity can create material value.

Add Value
In order to add value Cairn looks to progress existing exploration assets through the appraisal and development stages or can acquire new assets at this point in the oil and gas lifecycle.

Realise Value
Cairn realises value by progressing development assets through to production and/or realising value through asset sales and either reinvesting the proceeds into the business to fund exploration and development activity or returning cash.

Value growth within the oil and gas lifecycle

Identify | **Explore** | **Appraise** | **Develop** | **Produce** | **Return & Reinvest**

Exploration
Frontier and emerging basin exploration acreage offshore Senegal, Morocco, the Republic of Ireland, Norway and Malta; mature exploration acreage in the UK and Norway

Read more: CEO's Review on P14-21

Development
Non-operated interest in two development projects in the North Sea (Kraken and Catcher)

Read more: CEO's Review on P14-21

Production
Kraken and Catcher, two of the largest UK North Sea development projects, are targeting production in 2017

Read more: CEO's Review on P14-21

2017 strategic objectives

Deliver exploration and appraisal success
Purpose: Grow the resources and reserves

Portfolio management
Purpose: Active portfolio management and acreage optimisation

Deliver operational excellence
Purpose: In all 2016 activities

Maintain licence to operate
Purpose: Deliver value in safe, secure, environmentally and socially responsible manner

Deliver a sustainable business
Purpose: Maintain a self-funding business plan

2016/2017 principal risks

- Exploration and appraisal
- Sustained low oil and gas price
- Securing new venture opportunities

- Health, safety, environment and security
- Stakeholder reaction to operations
- Fraud, bribery and corruption

- Delay in Catcher and Kraken production start-up schedule
- Operational and project performance
- Reliance on JV operators for asset performance

- Restriction on ability to sell CIL shareholding
- Political and fiscal uncertainties
- Access to internal or external funding
- Staff recruitment and retention

2016 material issues

- Economics and funding
- Contractors and supply chain
- Ethics, anti-bribery and corruption and transparency
- Social and economic benefit
- Human rights
- Major accident prevention and safety
- Climate change, emissions and discharges

Business Model & Strategy continued

Rebuilding the business: 2012-2017

Cairn's strategy is to build a balanced portfolio of exploration, development and production assets in order to create, add and realise value for shareholders.

Historically, Cairn focused on South Asia where it created significant value for shareholders and stakeholders, particularly through its discovery, development and production of oil in Rajasthan, India. This was the largest onshore discovery in India for more than 25 years with the potential to provide more than 30% of India's daily crude oil production and generate many billions of US dollars in revenue for India. In 2006 the Indian business was listed on the country's stock exchanges and in 2012 Cairn sold the bulk of its interests in India and set about rebuilding the portfolio. Between 2006 and 2012 Cairn returned US$4.5bn to shareholders.

Today, Cairn continues to offer growth opportunities through its frontier exploration success in Senegal and through future cash flow from its North Sea development assets which are targeting production in H2 2017 and which will fund future exploration and growth of the business.

Senegal – a new source of resource and future production
Since selling down the Indian business Cairn's exploration focus has been on frontier acreage along the Atlantic Margin. The Atlantic Margin was formed millions of years ago when the supercontinent 'Pangaea' broke up to form the continents as they are known today and provides a range of underexplored and mature hydrocarbon basins with common geology and promising opportunities for organic growth.

Between 2009 and 2010 Cairn drilled eight wells in Greenland which failed to find commercial quantities of hydrocarbons. In 2014 Cairn made a significant discovery offshore Senegal thereby opening a new hydrocarbon basin. Cairn was the first to drill in deepwater offshore Senegal which remains relatively underexplored with only 25 wells drilled offshore to date. Cairn is currently pursuing further exploration and appraisal of this significant resource base. Along the Atlantic Margin Cairn also holds exploration acreage offshore the Republic of Ireland and Morocco.

Cairn's development and production focus is on the mature basins of the UK and Norwegian North Sea. In 2012 Cairn acquired non-operated interests in two of the largest developments in the North Sea, Kraken and Catcher, which are targeting first oil and cash flow in 2017.

Cairn also holds exploration acreage in the UK and Norway including the Barents Sea which is believed to have high potential for commercial oil discoveries. The mix of mature and emerging basins along the UK and Norwegian continental shelves provides good opportunities for balanced portfolio growth and operational synergies. They also form part of an active market for the trading of assets, an important part of optimising value within the portfolio.

In order to deliver maximum value Cairn continues to actively manage its portfolio of assets, with the constant evaluation of new exploration opportunities as well as opportunities to acquire and trade assets within the existing portfolio to ensure they are delivering optimum value.

Cairn made a significant discovery offshore Senegal in 2014, thereby opening a new hydrocarbon basin.

Geographic focus

Senegal

1 Production Sharing Contract

Acreage
7,100km²

2C resources[1]
201.4 mmboe

UK

12 Licences

Acreage
792km²

2P resources[1]
51.5 mmboe

2C resources[1]
3 mmboe

Norway

24 Licences

Acreage
5,458km²

2C resources[1]
20.2 mmboe

Morocco

1 Production Sharing Contract

Acreage
33,748km²

Republic of Ireland

3 Licences

Acreage
2,399km²

2C resources[1]
14.6 mmboe

Malta

1 Exploration Study Agreement

Acreage
6,412km²

1 As at 31.12.16.

Business Model & Strategy continued

Track record of exploration, development and production

Cairn is an experienced oil and gas explorer, developer and producer.

Cairn has operated in a variety of locations around the world, making its biggest discovery in Rajasthan, India which it went on to develop and produce. In 2012 Cairn sold its Indian business and returned cash to shareholders as part of its business model to create, add and realise value for shareholders. Since then Cairn has focused on rebuilding the business to create, add and realise value once again through exploration, development and production. Today Cairn is focused on its recent frontier exploration discoveries in Senegal and its development projects in the North Sea which are targeting first oil and cash flow in 2017.

Exploration

Senegal

2013 Farm-in as operator to frontier acreage offshore Senegal

2014 Two wells drilled, two oil discoveries, one of which is largest global oil discovery of 2014

2015 3D seismic acquired, drilling recommences

2016 Four successful wells drilled, independently verified contingent in place gross oil resource upgrade to >2.7bn bbls

2017 Third phase of drilling commences

Development
UK & Norway

2012 Future production and cash flow secured through acquisition of two UK & Norway focused companies bringing Kraken and Catcher developments, Skarfjell discovery, near term exploration drilling, >30 licences

2013 Kraken Field Development Plan (FDP) approved, successful Skarfjell appraisal well

2014 Catcher FDP approved, Kraken Floating Production, Storage and Offloading (FPSO) construction starts

2015 Catcher FPSO construction starts, Kraken and Catcher development drilling starts

2016 Nearing cash flow and production from Kraken and Catcher, targeted in 2017

Exploration, development and production track record
Rajasthan, India

1997 Acquired interest in Rajasthan from Shell

1999 First Rajasthan discovery

2003 Second Rajasthan discovery

2004 Three major oil discoveries by 2004 including Mangala, the largest onshore oil find in India in 25 years

2007 Value realisation from Indian business following Initial Public Offering of Cairn India Limited (CIL) on Indian Stock Exchanges, US$1bn returned to shareholders

2009 Production commenced from Mangala field, Mangala Processing Terminal opened (~16,000 people involved at height of construction)

2010 World's longest pipeline taking oil to market completed

2012 Sale of 40% of CIL to Vedanta Resources Limited, US$3.5bn returned to shareholders; 10% interest in CIL retained

Our Culture

Delivering value in a safe, secure, environmentally and socially responsible manner for our stakeholders is a key part of our strategy and ensures we maintain our licence to operate.

At the heart of this is our culture which is based around a commitment to working responsibly. We measure our ability to work responsibly through our Key Performance Indicators, one of which ('Maintain licence to operate') is dedicated to working responsibly. It is also measured through our people management process which incorporates certain behaviours identified as critical to ensuring this culture exists.

A culture based on working responsibly means having the right values, principles and policies in place, that they are embedded throughout the organisation in our systems and processes and that they are upheld by our people. At the heart of our culture are our core values which are known as **the 3Rs**, and which stand for building respect, nurturing relationships and acting responsibly.

These core values are underpinned by our Business Principles, our Code of Business Ethics and a number of Corporate Responsibility policies.

Read more information at
www.cairnenergy.com/responsibility

The Business Principles identify the behaviours we expect and the Code of Business Ethics identifies the standards of business ethics and conduct which we expect. Both the Business Principles and the Code of Business Ethics must be applied not only by employees but by all other parties that work on the Company's behalf including contractors, suppliers and partners. They are integrated into our systems and processes of which the key ones include the Corporate Responsibility Management System (CRMS), the Cairn Operating Standards, the Group Risk Management Procedure and the Internal Control and Assurance Framework.

Our core values

At the heart of our culture are our core values which are known as the 3Rs, and which stand for:

Building Respect

Nurturing Relationships

Acting Responsibly

Our behaviours

The behaviours we expect from our people are based on the 3Rs:

- **Be Safe**
- **Be Entrepreneurial**
- **Be Focused**
- **Be a Leader**
- **Be Collaborative**
- **Be Open**
- **Be Empowered**

The behaviours we expect from our people are based on the 3Rs and are known as our High Performance Behaviours. They identify the behaviours we expect to see exhibited by our people in everything that we do, day to day. They are well promoted throughout the organisation and they ensure that everyone understands how they are expected to contribute to the success of the business.

They are:

- Be Safe
- Be Entrepreneurial
- Be Focused
- Be a Leader
- Be Collaborative
- Be Open
- Be Empowered

To further ensure these behaviours are adopted by our people and embedded in our culture, this year we included them as part of our performance management process with all individuals in the organisation measured on their performance against each of these behaviours.

This culture of working responsibly is also built upon global standards which we uphold and which consequently inform how we deliver strategy. These standards are part of valuable, global initiatives which promote responsible corporate behaviour and working practices.

We uphold and support the ten principles of the United Nations Global Compact, an initiative for businesses committed to aligning their strategies with ten universally accepted principles in the areas of human rights, labour, environment and anti-corruption. We are also committed to working to International Finance Corporation (IFC) Performance Standards on Social and Environmental Sustainability which are in line with the UN Global Compact principles.*

The Board has ultimate responsibility for ensuring this culture of working responsibly exists within the organisation and our assurance processes help the Board to ensure this. We have three levels of assurance within the organisation: firstly, our values, policies and principles and our processes and systems with which all employees are required to comply; secondly, internal oversight of their application by key committees including our Senior Leadership Team which includes our Chief Executive, Chief Financial Officer and Chief Operating Officer; and thirdly, external assurance audits and opinions. Our culture of working responsibly is embedded at the very heart of this assurance process in our values, policies and principles.

* The IFC, a member of the World Bank Group, is the largest global development institution focused exclusively on the private sector in developing countries.

This culture of working responsibly is also built upon global standards which we uphold and which consequently inform how we deliver strategy.

Industry Overview

Putting our industry in context

This industry overview provides an independent view of the industry context in which Cairn operates.

Introduction
World economic growth remained weak in 2016, with uncertainties such as the US elections, the UK Brexit vote, Eurozone financial fragility and Chinese economic rebalancing weighing heavily on the system. This in turn constrains the demand for oil, with oil supply continuing to exceed demand and producing another year of weak oil prices, with Brent crude averaging US$44 per barrel over 2016 after reaching a 12-year low of US$28 in January.

The end of the year saw a response to this in the form of an agreement in November to restrict production by both OPEC and certain non-OPEC producers, delivering cuts of 1.2 million barrels per day over the next 6 months (almost 1.5% of global output). Commencing in January 2017 this heralds a return to market price management, rather than share management. Futures prices for 2017 rose by more than US$10 per barrel in reaction to this potential crude deficit.

2016 saw significant policy movement towards a reduction in global carbon emissions, with the Paris agreement gaining sufficient signatories to enter force by November. Although unlikely to be enough to deliver the target global warming ceiling of 2°C, suggesting more policy changes to follow, this marks an important step change in the energy transition. With global energy demand expected to rise by over 30% in the next two decades, government and market incentives will be required to reduce the carbon impact.

Energy intensity will increase and accelerate, such that each energy unit will produce ever more output, but also the mix of energy carriers will shift towards those emitting less carbon. It is expected that renewables will grow fastest among all the energy carriers but that, given the much higher starting point, fossil fuels will be the largest contributors to the required growth in energy supply. Gas, emitting the least carbon per energy unit, is therefore expected to be the main source of this, at the expense of coal, and to a lesser extent oil[1].

Oil consumption is expected to continue to grow, but at a lower rate than total energy consumption, such that its relative share in the energy mix continues its long-term decline. This is not a view shared by all – in late 2016 Royal Dutch Shell issued another warning of peak oil over the next 5 to 15 years, signalling an important switch to demand becoming the binding constraint, rather than supply. Overall, therefore, the uncertainties around climate change and geopolitical considerations evolved rapidly through 2016, with the implications for the oil and gas industry still open to debate.

Frontier exploration

Activity in the North Sea

COP21/ stranded assets

The current oil price, and the future of oil demand, have continued to suppress the exploration spend, with 2016 levels down by 20% against the previous year and 60% against the high of 2014. The push for capital discipline and portfolio risk reduction has driven down exploration costs, such that the net effect on activity is not as deep as these numbers suggest. However almost all of this expenditure was on activity already contractually fixed with very little new, discretionary, spend.

Despite this gloomy background those companies with the balance sheet and risk appetite to open up new acreage are taking advantage of the opportunities associated with low contracting costs. Significant finds have been made in the US in shale oil, indeed the largest ever single US deposit of oil and gas was reported, but elsewhere the gas dominance of recent years has continued.

The recovery in North Sea production visible in 2015 continued into 2016, rising by over 6% year on year, driven by several new fields coming on stream and a reduction in maintenance downtime on existing facilities. However it is more appropriate to look behind the production numbers since a new regulatory regime requiring stakeholders to maximise economic recovery, rather than simply total volume, came into force in 2016.

Total operating costs for the North Sea have fallen by almost 27% since the highs of 2014, the most visible effect of which is the reduction in industry headcount. This reduction in expenditure, combined with the increase in production, resulted in a 45% fall in operating costs per barrel.

On the other hand, total capital expenditure has also fallen, and by further (40% since 2014), such that the medium- to long-term outlook is less positive.

This is also reflected in the significant proportion of assets up for sale with relatively few interested parties, partly a reflection of the complex challenge of apportioning the costs of end-of-life decommissioning.

The new regime brings in a more powerful regulatory body as well as closer collaboration with government on fiscal terms, but also will require, to a considerable extent, companies operating in the UK sector of the North Sea to make investment decisions for the benefit of the "oil province as a whole" and not solely their own economic benefit. This will mean companies cooperating and collaborating to maximise recovery or minimise costs throughout the project cycle in order to improve the long-term outlook.

The increasing policy stance to limit global temperature rise creates considerable uncertainty over the long term, but the medium-term effect is muted. The key target date of the Paris agreement is 2030, but IHS estimates suggest that 80% of the market value of the large international oil companies results from the proved reserves to be produced in the next 10 to 15 years[2]. Similarly, these oil companies control a minority of world oil reserves, with an average production-to-reserves ratio of 13 years as compared to a global average of 50 years[3]. Therefore, the main production and value proposition of these oil and gas companies lies within the transition period to a low carbon future rather than after it.

Over the longer term, however, current estimates[4] are that already discovered fossil fuel reserves would produce almost three times more carbon than permissible under the scenario for a maximum 2°C of global warming. This implies that a significant proportion will remain unexploited, or unexploitable – the problem of the 'stranded asset'. Whilst much debate has focused on the global energy mix required to meet the COP21 objectives, the real complexity for policy makers will lie in the inherent tension between these objectives and the role that fossil fuel extraction and consumption can play in the economic growth of developing countries.

The recovery in North Sea production visible in 2015 continued into 2016, rising by over 6%.

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Heriot-Watt University is one of the UK's leading universities for business and industry and has a reputation for innovative education, enterprise, and leading-edge research. Energy research is a core activity within Heriot-Watt University, and the Centre for Energy Economics Research and Policy (CEERP) is the latest evidence of the University's commitment to research in energy, economics, and policy. CEERP is based within the Institute of Petroleum Engineering at Heriot-Watt University, but forms a key point of support and collaboration among the University's Schools with affiliates from the School of Energy, Geoscience, Infrastructure, and Society; School of Social Sciences; and the Energy Academy as well as honorary academics outwith the University.

1 BP Energy Outlook 2035, January 2017.
2 IHS Energy, Do Investments in Oil and Gas Constitute Systemic Risk?, October 2016.
3 Stevens, P., International Oil Companies – The Death of the Old Business Model, Chatham House, May 2016, page 24.
4 McGlade, C & Elkins, P., "The geographical distribution of fossil fuels unused when limiting global warming to 2°C", Nature, Vol. 517, January 2015, pages 186 to 190.

CEO's Review

Positive progress

Cairn continues to deliver positive progress across its balanced portfolio.

2017 will see first oil from our North Sea developments and progression of an exciting ongoing exploration and appraisal drilling programme in Senegal, all against a backdrop of increased financial flexibility.

The company remains well-positioned to deliver further value for shareholders from multiple catalysts within the portfolio.

Over the last five years, the business has been considerably reshaped and advanced to establish a balanced exploration and production company. The year ahead will be eventful with a number of material catalysts which have potential to add further value to the company.

We have created a strong platform for future growth with active positions in six countries in almost 50 licences providing significant acreage positions of technical and commercial value. The discovery of the SNE field offshore Senegal in 2014 marked a return to exploration success for Cairn and provides an opportunity to implement our strategy of creating, adding and realising value for shareholders through a balanced, well-funded and sustainable company.

In Senegal, we have confirmed the scale and potential of this world class asset, and following the appraisal success and contingent resource upgrade in 2016, we have now commenced the third phase of evaluation activity. The JV also has plans for future exploration drilling.

Working responsibly is a key part of our strategy

We can only deliver value for all stakeholders by operating in a safe, secure and environmentally and socially responsible way. At the heart of this culture are our core values, the 3Rs, which stand for building respect, nurturing relationships and acting responsibly.

In practice, we implement the 3Rs by adhering to our robust Corporate Responsibility Management System (CRMS). Our values are also underpinned by internal policies and procedures, including our Business Principles and our Code of Business Ethics, as well as continuing external commitments to the Extractive Industries Transparency Initiative (EITI), the UN Global Compact and recognition of the UN Sustainable Development Goals.

To help shape our Corporate Responsibility (CR) strategy we identify issues material to the business through internal and external engagement as well as our risk management process. In 2016, our material issues were identified as:

- Economics and funding
- Contractors and supply chain
- Ethics, Anti-bribery and corruption and transparency
- Social and economic benefit
- Human rights
- Major accident prevention and safety
- Climate change, emissions and discharges

Across all our operations we recognise the need to prepare for the unlikely possibility of a high-impact event and have robust plans in place to manage potential incidents. We invest heavily in memberships to gain access to specialist equipment and techniques, and expertise that would be needed in such an event.

During the year Cairn has been focused on growing its significant Senegal resource base as operator and on progressing its North Sea developments as non-operator. Our most significant drilling activity during the year took place in Senegal. Our robust policies, including our Code of Business Ethics, of importance wherever we operate, ensure that we conduct risk-based due diligence on contractors in line with our zero-tolerance approach to bribery and corruption.

As part of our approach wherever we operate, we are committed to bringing lasting and positive social and economic benefits through new support industries, employment, training and improved education. We believe a successful oil and gas industry could generate significant income in Senegal. This could be used to support the country's development, improving infrastructure, providing affordable energy, driving inward investment and reducing reliance on solid fuels.

In the UK and Norway, we have high quality assets and have made significant progress in the last year. Both the Kraken and Catcher development projects are below budget and on schedule to target first oil this year. The start up of these developments is significant, as it will mark Cairn's first production since 2012 when we sold the majority stake in our Indian business and returned the proceeds to shareholders. The mature and emerging basins of the UK and Norway provide balance to Cairn's frontier exploration portfolio and will deliver the cash flow to sustain future exploration.

With a fully funded balance sheet, the company is well positioned to the prevailing oil price environment which presents challenges to the industry but also opportunities to allocate capital to value enhancing projects while benefitting from reduced operational costs.

We are taking advantage of the lower industry cost environment as we continue to shape the business for the future. We actively assess new ventures within the context of our balanced offering whether they be potential additions to our portfolio of future exploration opportunities or cash flow generating assets.

Corporate Responsibility remains at the heart of our business. During 2016, we continued to prioritise the health, safety, security and wellbeing of our people while promoting safe behaviours of contractors and partners. We remain committed to protecting the environment in the areas where we operate. Good governance is also important and we are committed to meeting all our obligations in a responsible and transparent manner.

We announced the appointment of Eric Hathon as Director of Exploration earlier this year. Eric has more than 25 years' industry experience and will join in April from Marathon Oil Corporation. Eric will succeed Richard Heaton who is retiring after 23 years' service with the company. I would like to welcome Eric and thank Richard for his significant contribution over his long career at Cairn where he has been a core member of the senior team. I was also delighted to welcome a new independent non-executive Director to the Board early this year: Nicoletta Giadrossi brings a wealth of international senior management and oil and gas industry experience to Cairn.

I would like to recognise and thank all our employees and contractors working both offshore and in our four international locations for their efforts, commitment and hard work during 2016 in what has been an extremely busy year. We look forward to another exciting year ahead.

SIMON THOMSON
Chief Executive
7 March 2017

During 2016 we continued to work closely with our joint venture partners on our North Sea developments to progress them towards targeted first oil and cash flow in 2017. As non-operator our focus is on ensuring joint venture operations are rigorously assessed against our CRMS and associated regulatory requirements.

We will continue to set CR objectives each year guided by the most material issues which are issues important not only to Cairn but also to our stakeholders, in keeping with our commitment to working responsibly.

"As part of our approach wherever we operate, we are committed to bringing lasting and positive social and economic benefits."

52 Read more: **Working Responsibly** on **P52-71**

CEO's Review continued
Operational review

Highlights of 2016

Senegal
Exploration & Appraisal

Seven successful wells drilled to date in Senegal: two discoveries, four wells in 2016 and a further appraisal well just completed.

SNE-5 appraisal well operations safely and successfully completed ahead of schedule and under budget.

Stena DrillMAX drill ship is moving location to shortly commence operations on the Vega-Regulus (VR-1) well, ~5 km to the west of the SNE-1 discovery with the exploration target underlying the SNE field.

VR-1 will also provide further appraisal data on the SNE field and results will help narrow field volumes and allow the Joint Venture (JV) time to integrate the results of SNE-5 prior to moving to SNE-6 to complete the planned interference test.

Current 2C in place resources more than 2.7 billion barrels and the ongoing programme will further define the recovery potential of the field.

Multiple exploration prospects have been identified: Cairn estimates further block wide exploration potential of ~500 mmbbls gross mean risked resource.

Prospect inventory includes numerous material targets across four play types identified within a 30 kilometres (km) tie back radius to SNE field.

Senegal
Development

Decision on development concept selection expected in 2017, current plans include a phased development to capture the potentially extensive resource base.

From 2018 onwards, Cairn and JV partners plan to submit the Exploitation Plan and proceed to a Final Investment Decision with first oil expected in the period 2021-2023.

Woodside Petroleum Ltd (Woodside) entered the JV in 2016 bringing extensive experience in developing and operating floating production, storage and offloading (FPSO) facilities.

Cairn's strategy is to deliver value for stakeholders by building and maintaining a balanced portfolio of exploration, development and production assets. Our exploration focus in on frontier and emerging basin acreage from which the greatest value can be created. The Group's production assets provide the cash flow to sustain future exploration and development activity.

We have made good progress against our strategic objectives, increasing the recently discovered resource base in Senegal and progressing our North Sea developments through to first oil and future cash flow.

Senegal – opening a new hydrocarbon basin

Cairn was the first company to drill deepwater wells offshore Senegal, which remains a relatively underexplored region of the world. The success of the Cairn discoveries has attracted the attention of the global oil industry with a number of high profile new entrants to Senegal during the year.

The management of Health, Safety, Security and Environment remains a high priority and we are aiming to build on our good performance in Senegal in the year ahead. Cairn has enjoyed excellent support from local services such as Dakar port where the company has now established a shore base facility to aid the growth of the oil sector in Senegal.

In 2016 Cairn opened a new supply base in Dakar international port.

Since the two initial basin opening discoveries in 2014, we have drilled five successful wells in the area. During 2016, subsurface data gathering was successfully completed on four wells, SNE-2, SNE-3, BEL-1 and SNE-4. With better than expected drilling performance and the lower cost environment, these four wells were essentially drilled and evaluated on the SNE field for the original budget of three wells.

In 2017, the third phase of evaluation is underway which is intended to improve the definition of the project and confirm volumes, connectivity and productivity. Operations and testing of the first of the appraisal wells, SNE-5, have recently been successfully completed, ahead of schedule and under budget. The well has been plugged and abandoned and the Stena DrillMAX has moved location to commence operations on the Vega-Regulus (VR-1) well. VR-1 will target the Vega-Regulus exploration prospect in the Aptian Carbonates underlying the SNE field which has potential gross mean consolidated prospective resource of more than 100 mmbbls. In addition, the well will provide further appraisal on the SNE field targeting potential incremental resources. The results will narrow the range of SNE field volumes and also allow the JV time to fully integrate the results of SNE-5 prior to moving to appraisal well SNE-6 to complete the planned interference test.

The prospectivity of Cairn's Senegal acreage, an area of more than 7,000 km^2 under licence, has high potential; the success of both the SNE discovery and follow on appraisal of the SNE field has proven there is a prolific source rock, excellent reservoir development and a good working seal. The new 3D seismic data has improved our ability to map traps along the extension of the SNE trend. Numerous, prospects have been identified in a wide variety of play types.

The JV has endorsed the foundation development concept of a standalone FPSO with subsea wells and expansion capability. This is established and proven technology in areas where Cairn can add value through recent experience in the Kraken and Catcher North Sea developments. The potential around SNE for further exploration success would transform the project into a multi-phase development.

The focus of the remaining appraisal activity is on improving our estimates of the scale and phasing of the overall field development including the balance between the number of drilling centres, type and number of wells and the subsea infrastructure.

Cairn and its JV partners submitted a three year evaluation work plan to the Government of Senegal in 2015. As part of this plan, we currently anticipate an outline timetable for development with an Exploitation Plan to be submitted in 2018, a Final Investment Decision within twelve months thereafter and first oil expected in the period 2021-2023.

Cairn (Operator) has a 40% Working Interest (WI) in the three blocks offshore Senegal (Sangomar Deep, Sangomar Offshore, Rufisque Offshore) alongside partners: Woodside 35% WI, Far Ltd 15% WI and the Senegal National Oil Company, Petrosen 10% WI.

H.E. Thierno Alassane Sall, Minister of Energy Senegal, on board Ocean Rig Athena drill ship used during Cairn's 2015/2016 Senegal drilling campaign.

CEO's Review continued
Operational review continued

Highlights of 2016

UK & Norway

Catcher (Cairn 20% WI) and Kraken (Cairn 29.5% WI) developments in the UK North Sea on track for first oil from 2017; peak net production to Cairn of ~25,000 boepd.

Skarfjell (Cairn 20% WI) development in Norway, subsea tie-back to nearby GjØa platform selected by JV as development concept.

Five new licences awarded in Norway in Q1 2016, including Cairn's first licence as Operator.

Entry to the Barents Sea, Norway with three new licences awarded in Q2 2016, including one as Operator; region believed to have high potential for commercial oil discoveries.

Seven new licences awarded in Norway in Q1 2017, including two as Operator and two existing licence extensions.

Participated in two non-operated exploration wells: Aurelia in the Barents Sea (Cairn 10% WI) was unsuccessful and Laverda in the UK (Cairn 36% WI) successful, though subsequently impaired.

Operated Licence application in the UK 29th Licensing Round, awards expected shortly.

UK & Norway

The mix of mature and emerging basins along the UK and Norwegian continental shelves provides good opportunities for balanced portfolio growth and operational synergies. Cairn has built a strong position in the UK and Norway by acquiring exploration, appraisal and development assets and participating in licensing rounds.

The UK and Norway are a key region of focus for the Group and during 2016 we have expanded the team and added 13 new licences and four licence extensions. The strategy is to maintain and grow a strong prospect inventory capable of increasing resources and reserves, providing material exploration upside and bringing discoveries into production. We are also looking to identify new venture opportunities and manage the portfolio in an active market for asset transactions.

Developments
Kraken and Catcher are two of the largest ongoing development projects in the UK North Sea. Both are core development projects along with the Skarfjell discovery in Norway, where the development concept has been selected. These three projects are a key part of our strategy to build steady future cash flows to sustain the business model and fund future international exploration.

Simon Thomson, Cairn Chief Executive, visiting the Kraken FPSO in Rotterdam, 2017.

Catcher FPSO.

Brita Holstad, Regional Director for UK & Norway, and Paul Mayland, Chief Operating Officer, visiting the Kraken FPSO in Singapore, 2016.

We have made significant progress on the UK developments in 2016 and both the Kraken and Catcher projects are below budget and remain on schedule to target first oil in 2017. Re-establishing a new cash generative production base is an important milestone for Cairn in 2017.

Kraken

In 2016, the Kraken development progressed well, finishing the year ahead of budget and the Operator targeting first oil in Q2 2017. Most significantly, through a combination of release of contingencies, contract re-negotiations and some reduction in scope, the Operator is now forecasting total gross capex at US$2.5bn which is ~22% lower than the sanctioned estimate.

At the year end, four producers and five injectors had been satisfactorily drilled and completed. The 2016 subsea scope was completed without any issues. The FPSO was essentially mechanically complete with the vast majority of systems commissioned. The vessel left the deep water anchorage of Singapore and arrived in the North Sea in early 2017, having completed its journey as scheduled. The vessel berthed in Rotterdam to make final preparations prior to sailing offshore to hook up the Submerged Turret Production (STP) buoy mooring system, risers and umbilicals. Handover of FPSO systems from commissioning to operations continued in Rotterdam prior to sailing away. On arrival at the field, the hook up of the STP buoy mooring system was completed and a full rotation test performed to ensure the vessel was on station and securely moored.

Commissioning work will continue on the topsides. Reconstruction of the turret area pipework and connection of the risers and umbilicals to the swivel stack is being undertaken followed by commissioning of the subsea infrastructure.

Catcher

The Catcher project progressed well in 2016, with the Operator targeting start-up and first oil in Q4 2017. The Operator is now forecasting total project capex at US$1.6bn which is ~29% lower than sanctioned estimate.

The drilling programme made excellent progress in 2016; efficient execution together with a well-executed subsea installation campaign, were key factors in the project capex reductions. To minimise rig moves during the winter months, the schedule was adjusted so that at the year end, four wells on Catcher, two wells on Burgman and two wells on Varadero were successfully drilled and tested with all wells coming in at, or better than, prognosis in terms of reservoir quality and well deliverability. Due to these good well results and well placement optimisation, the well count required to deliver the base plan has reduced to 20 firm wells, delivering further significant reductions to the forecast development capex.

Very good progress was made with the FPSO in the second half of the year, with the joining of the two hull 'mega blocks' and installation of the living quarters in Singapore. All of the topside modules were also safely lifted on and very good progress made with the topsides integration.

The majority of the project's subsea installation scope was also completed in 2016. Only short subsea campaigns will be required in 2017-19 to tie-in the new wells drilled and to support the hook up of the FPSO. The project focus is now on final mechanical completion of the FPSO and the pre-commissioning/commissioning work scopes. FPSO sail-away from Singapore is expected to be around mid-year 2017.

Skarfjell

The JV has selected a development concept for the Skarfjell field. Under the proposed solution, the reservoir will be connected to the nearby Gjøa platform via a subsea tie-back. The Operator has submitted the development concept to the Norwegian Ministry of Petroleum and Energy and now enters the define phase of the project, refining the technical and economic plan before committing to a final investment decision, planned for Q1 2018. Based on the proposed plan, hydrocarbons from the Skarfjell reservoir will be developed with two subsea templates tied back to the Gjøa platform for processing and export. Gjøa will also provide lift gas to the field and water injection for pressure support. Several studies will be conducted before the final investment decision and the plan for development and operation can be submitted to the Ministry.

Exploration

In 2016, Cairn secured three licences in the Barents Sea, including one as Operator. We believe the Barents Sea is a potential core exploration opportunity and our experience from operations in the Arctic will be relevant in the region. According to the Norwegian Petroleum Directorate, the region may contain as much as half the country's unexplored resources with yet-to-find hydrocarbon potential of 8.8 billion boe. In 2016, Cairn participated in two non-operated exploration wells (Aurelia in the Barents Sea 10% WI and Laverda in the UK 36% WI). Aurelia was unsuccessful in finding commercial quantities of oil at the primary horizon. Laverda did find potentially commercial quantities of oil at the primary horizon but was unsuccessful at the secondary target of the well.

CEO's Review continued
Operational review continued

Highlights of 2016

International

Western Sahara: Boujdour Maritime new Petroleum Agreement (Cairn 20% WI) with Operator Kosmos Energy, 3D seismic acquisition commences in 2017.

Ireland – Cairn awarded Licence Option (LO) 16/18 in the Atlantic Ireland Licencing Round in H1 2016. Additional farm-in to a 70% WI and Operatorship in the adjacent LO 16/19 with Europa Oil & Gas with plans for 3D seismic in 2017. Cairn farm-in to a 30% WI in Frontier Exploration Licence (FEL) 2/14 in Southern Porcupine Basin with Providence Resources and Sosina; with one firm well in 2017.

International

Cairn's exploration focus is on the Atlantic Margin where, in addition to Senegal, we have key interests offering the potential for material discoveries and high prospectivity.

In Western Sahara, we signed a new Petroleum Agreement with Operator Kosmos in 2016 and are acquiring 3D seismic in 2017. In Mauritania, we relinquished a licence in 2016, although we continue to be interested in exploring the region.

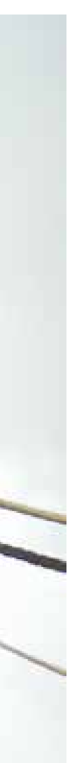
In Ireland, there have been a number of developments: Cairn agreed a farm-in to LO 16/19 with 70% WI and Operatorship with Europa Oil & Gas with plans for 3D seismic in 2017. Cairn has previously been awarded adjacent LO 16/18 in the Atlantic Licensing Round in H1 2016. The acquisition of 3D seismic is planned to be acquired over both licence option blocks in 2017 and processed in 2018. Cairn also agreed a farm-in to FEL 2/14 in the Southern Porcupine Basin with partners Providence Resources Plc (Providence) and Sosina. An exploration well will be drilled in 2017. The 53/6-A well is planned to spud in June 2017, subject to the necessary regulatory consents, using the Stena IceMAX drill ship targeting both large stratigraphic traps, Druid and the deeper independent Drombeg target.

Catcher FPSO.

This will result in the planned well, in 2,200m water depth, being deepened from ~3,900m to ~5,200m. As a result of the proposed transaction, the equity interests in FEL 2/14 will be Providence (Operator 56%), Cairn (30%) and Sosina (14%). Both agreements are subject to approval of the Government of Ireland.

Outlook

During 2017, Cairn will commence production, continue to deliver future development as well as define and explore significant growth opportunities from Senegal. We will continue to advance the business to create a balanced exploration portfolio across emerging and frontier basins in the Atlantic Margin and Barents Sea alongside mature basins in the North Sea. The Group will continue to evaluate new venture and growth opportunities to allow us to create value through successful exploration and discovered resources.



Group Booked Reserves and Resources

A total of 51.5 mmboe were booked as 2P Reserves and 239.1 mmboe as 2C Resources at 31 December 2016 on a net working basis.

Net 2P Reserves	31.12.15 mmboe	Revisions mmboe	Production mmboe	31.12.16 mmboe
UK	49.5	2.0	0.0	51.5
Totals	**49.5**	**2.0**	**0.0**	**51.5**
Net 2C Contingent Resources				
UK	1.5	1.5	0.0	3.0
Ireland	14.6	0.0	0.0	14.6
Norway	25.3	(5.1)	0.0	20.2
Senegal	155.1	46.3	0.0	201.4
Totals	**196.5**	**42.6**	**0.0**	**239.1**

The reserves revisions in the UK included the acquisition of an additional 4.5% working interest in Kraken from First Oil and changes to corporate oil price assumptions.

The revisions in Norway included updates in Skarfjell and the relinquishment of Titan.

The Senegal resources increased following the appraisal campaign in 2016.

Cairn in the UK & Norway

Nearing production and cash flow

When the Kraken development comes on stream in 2017, it will be the culmination of a project that began more than 30 years ago.

Dave Beck, Cairn's Development Manager, explains some of the history behind the Kraken development and Cairn's role in bringing it on stream. (Operator, EnQuest; Cairn 29.5% Working Interest).

Tell us about the history of the Kraken development.
The field was first discovered by Occidental Petroleum in 1985, but it was by accident rather than by design. It was not the discovery they were chasing. Occidental were targeting something deeper and drilled through the shallower Kraken discovery while looking for it. Their target turned out not to be there and so the well was abandoned. This was a time when companies were looking for the big, easy discoveries and heavy oil was considered difficult.

More recently a combination of fiscal incentives by the government to encourage investment and activity on smaller licences in the UK North Sea as well as the development of new industry technology have made the Kraken project very attractive and resulted in a small exploration company, Nautical Petroleum, picking up the acreage.

Nautical drilled the first new appraisal well in 2007. That was a success but was followed by another one that was not. I think that was the point when there was doubt about whether Kraken could be developed, but we went ahead and drilled a further two appraisal wells with side tracks of both. Fortunately, those were very successful and proved to us that the field could be commercial, and could be profitably and successfully developed.

By this time, the technology that the industry had access to had moved on significantly and with most of the bigger fields already operating, there was a lot more focus on other overlooked parts of the North Sea where there had been significant finds in the past.

How did Cairn get involved in Kraken and what is your role?
Nautical farmed out a majority stake in the project to EnQuest in 2012, and later the same year, Nautical itself was acquired by Cairn, which assumed its stake and became a partner working with EnQuest, as operator, to develop the project.

As Cairn is non-operator, my role is to protect our investment and to make sure that Cairn's interests are aligned with the operator. In practice that means collaborating with them, discussing options and priorities, making sure that the development and the construction of the FPSO (Floating Production Storage and Offloading) vessel in Singapore is proceeding well and according to schedule.

What have been some of the greatest challenges in bringing Kraken on stream?
One of the greatest challenges for the project was the development of the FPSO, the Armada Kraken. Each vessel is made bespoke to the field and the conditions it will be operating in and each is a fantastic feat of engineering. Making sure we got that right was a key part of the development.

The Kraken vessel will be one of the largest operating in the North Sea, with 90 beds and around 60 crew members aboard at any one time during normal operations. The vessel, which has already left the yard in Singapore where it was built, will remain in the same spot for the whole 25-year life of the Kraken field until all the recoverable oil has been extracted. The vessel can store 600,000 barrels of oil in its tanks at a time, ready for onward transportation once at capacity.

"Kraken is currently one of the biggest developments in the UK North Sea."

What is the significance of Kraken to Cairn and to the UK Continental Shelf?
Kraken sits in the East Shetland basin, approximately 125 km east of the Shetland Islands, and it is currently one of the biggest developments in the UK North Sea. The project features 25 wells on the seabed in four clusters, which will collectively pump around 50,000 barrels of oil per day to the FPSO at peak production. That will present a significant contribution to UK oil production, currently running at around 750,000 barrels of oil per day.

It's a shallow reservoir, which means the pressure is relatively low. That's why this will be only the second field in the world to use hydraulic submersible pumps. To add to that, when completed it will be the first fully subsea heavy oil development anywhere in the world.

The field will also have a meaningful economic impact. It is estimated that the Kraken development will support more than 20,000 UK jobs during the construction period of the project and an average of approximately 1,000 operational jobs in the UK for each year of the project's 25-year life.

How does Kraken compare to other developments that you have worked on?
I am a petroleum engineer by profession and have been in the industry for more than 30 years. During that time I have worked on developments as far afield as Syria, Ukraine, Kazakhstan, Sakhalin, and Venezuela. One of the striking things about working back in the UK has been the stringent regulations and the resources available that ensure such developments meet strict health, safety and environmental requirements.

When the project comes on stream, there will be a feeling of pride in a job well done. Of all the people currently working on the project, I'm the one who has been on it the longest, so yes it will be a real achievement when the project is completed.

What are the next big opportunities in the North Sea?
I'm confident in the future prospects for the North Sea. There are plenty of areas – particularly in the Norwegian North Sea and in the Barents – that are underexplored. There is still a lot to play for.

Cairn in Senegal

Senegal: discovering a new oil frontier

In 2012 Cairn embarked upon a frontier exploration drilling programme focused on the Atlantic Margin resulting in the discovery of oil in Senegal in 2014 which constituted the largest global offshore oil discovery of 2014. Cairn has now completed two drilling programmes in Senegal with a third underway and is focused on additional exploration and appraisal activity to further increase this already significant resource base.

Working in Senegal

Working in the Dakar office

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Working with the national oil company, Petrosen

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Working with local contractors

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Social Investment

Helping women in rural communities

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Supporting local entrepreneurship

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Supporting local business

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Cairn in Senegal continued

Working in Senegal

Cairn's strategy is to deliver value for our stakeholders from the oil and gas lifecycle. As part of this Cairn is committed to delivering lasting and positive social and economic benefits in countries where it operates.

Delivering value for stakeholders in Senegal
Stakeholders are those affected by Cairn's activities including employees, communities, contractors and suppliers and the government. Social and economic benefits include energy security, revenues from oil and gas activities, employment, development of infrastructure and social investment. As Cairn's operational activity in Senegal progresses so too does the level of its investment which has both direct and indirect benefits for local stakeholders. Cairn's belief is that the discovery and development of sustainable oil production in Senegal would greatly benefit the national economy and therefore the local population. To date Cairn has invested US$330.3million through its activities in Senegal.

In order to deliver the Company's operational programmes in Senegal Cairn has an office in Dakar and a recently built supply base in the international port of Dakar. This is part of Cairn's approach to operations in any country to deliver value in the country by maximising local participation which includes employing local people and working with local companies wherever possible.

Cairn Dakar office team.

Given that oil and gas activities are relatively new to Senegal, local industry expertise is just starting to develop and as such developing capacity through training and education is a key part of our operations. Not only does this develop the opportunity to participate in the international oil and gas business but it is important for promoting working responsibly.

As part of this, in our Dakar office we have offered a number of training opportunities including English language training, HSE training and organised visits to our headquarters in Edinburgh to reinforce our culture and to improve communications and cultural understanding.

We have provided training to more than 162 officers of the relevant regulatory authorities to support the oil and gas regulatory environment in Senegal. This training covered oil and gas industry awareness, HSE awareness, offshore safety, offshore emergency response including oil spill response, waste management and English language training. We have also provided English language training to 46 geoscience and technical students at the University of Dakar; this is part of our aim to build local participation for the future.

We have engaged local companies in logistics and supply base support, waste management services, aircraft handling services, transport services, fishing liaison, administration, accommodation and environmental and social consultancy services.

Saraou Kombo, Co-ordinator, Capricorn Senegal Limited, Dakar office

Working in the Dakar office

I joined Cairn in December 2015 as co-ordinator in our Dakar office as the second phase of exploration and appraisal drilling started. Previously I spent a number of years working for the British Embassy in Senegal. This is the first time I have worked in the oil and gas industry. At first it seemed difficult, with so much new to learn, understanding how the industry works, new regulations and new faces to get to know. But new things are also exciting. I have been pleased to find that so much of how we worked in the embassy is also true in a UK company – the emphasis on anti-bribery and corruption, behaviours based on honesty and integrity and compliance with rules and regulations.

A lot of my work has been focused on building good relationships with many of our stakeholders, communicating how we work with respect and responsibility. This is very important for the progress of Cairn in Senegal.

In Senegal people are becoming excited about the recent discoveries and the benefits they could bring to our country including new support industries, employment and improved education. Transparency in this new industry is therefore important for the country and initiatives like the EITI (Extractive Industries Transparency Initiative) are a good thing. There are high expectations that the oil and gas industry will bring social and economic growth and one of our biggest challenges is helping communities understand how the oil and gas industry works and the timescales and stages involved. I think the biggest challenge for the industry will be achieving our goals to the satisfaction of government, partners and communities and we are working hard to manage expectations.

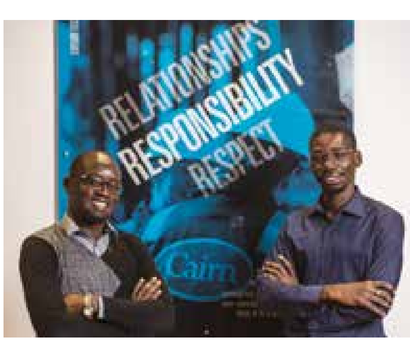
Much of my role is concerned with facilitating these training initiatives and engaging with the local companies we work with, promoting our high standards of responsible working practices and helping to ensure they are met.

"A lot of my work has been focused on building good relationships with many of our stakeholders, communicating how we work with respect and responsibility."

Saraou Kombo.

Mohamed Sonko and Daouda Tigampo

Working with the national oil company, Petrosen



Daouda Tigampo and Mohamed Sonko.

We have both been working at Petrosen as geologists for more than three years after studying in Morocco and Senegal respectively. We are a small team of eight geologists and two geophysicists and as the only national oil and gas company we work with all the oil and gas companies operating in Senegal. Petrosen has been waiting for a significant discovery for many years and people are very excited about the recent discoveries made by Cairn and its joint venture partners. Local people are excited because they see the opportunities for using income from oil and gas activities to support our economy and industries such as agriculture and our education system. Our biggest challenge at work is learning all about the industry which our partners help us with. We have received much training in the last few years.

One of the highlights was in 2014 when we went to London with Petrosen to visit a core lab. We have also received English language training through Cairn and the British Council. During 2016 we spent two weeks at Cairn's headquarters in Edinburgh trying to learn as much as possible in petrophysics, seismic data, modelling and software used in the industry. For us drilling is the most exciting part of the oil and gas lifecycle so we are looking forward to Cairn resuming drilling in 2017!

Cairn in Senegal continued
Working in Senegal continued

New supply base at Dakar port

Establishing a permanent facility

In September 2015 we opened a new supply base on the quayside of Dakar port to better meet our increasing operational needs in Senegal. The new supply base gives us a number of operational advantages including a dedicated quayside which means we are able to work uninterrupted in what is one of the biggest ports on the coast of West Africa. Its proximal location to our offshore acreage (approximately 60 nautical miles/111km in distance and six hours in travel time by vessel; helicopters transit from Dakar international airport with a flight time of around 25 minutes) is also a significant advantage. This new facility also demonstrates our commitment to working in Senegal and our increasing investment in the country. Oil and gas is an emerging industry for Senegal and this is the first time that a dedicated, permanent supply base infrastructure has been built in Dakar port. The process took 18 months and was handled by our key, local contractor Necotrans Senegal, a subsidiary of the international logistics and transport conglomerate Necotrans.

Working with Necotrans is part of our approach to maximising local content wherever we work. We employ, on a permanent basis, 16 Necotrans contractors and much of our work on the base focuses on training them to support our operations as well as to enable them to participate in the oil and gas industry in the longer term.

The supply base is the main hub for our activities in Senegal and is the main point of contact for our many contractors during and in preparation for drilling. We store critical equipment on site including oil spill response equipment and carry out activities including loading and unloading of offshore support vessels which supply our drill ships. In the handling of this equipment and the management of these activities specialist knowledge, oversight and a focus on safety at all times are required. As such one of our main focuses at the base is on health, safety and environment (HSE).

> **"The supply base is the main hub for our activities in Senegal and is the main point of contact for our many contractors and our activities during and in preparation for drilling."**

New Cairn supply base, Dakar port.

Simon Thomson, Chief Executive and Paul Mayland, Chief Operating Officer visiting Cairn supply base in Dakar port.

Working with so many contractors means careful management and providing training to ensure our HSE standards are met. This is overseen by our experienced team of industry experts on site which is made up of two supply base managers, two logistics supervisors, and one HSE adviser. All contractors are inducted on arrival at the supply base in our ten 'Life-Saving Rules' which they are obliged to apply and follow at all times and they are also required to attend morning meetings, pre-job 'toolbox talks', weekly safety review meetings and monthly 'Safety focus' meetings.

This supply base was built to and operates to UK Oil and Gas guidelines. For many of those who are working with us this is the first time they have had exposure to working in these types of conditions and they are acquiring valuable skills which we hope will benefit them in the future. As our key contractor Necotrans have been trained and mentored by our supply base team in activities including basic yard operations such as oil field inventory recognition, handling and inspection; boat loading; and discharging. We have also brought in external experts to provide training including North Sea Lifting, Oil Spill Response, St John Ambulance and the Dakar fire service.

Amadou Sakhir Gaye,
Logistics Co-ordinator, Necotrans

Working with local contractors

I have worked with Cairn since their first drilling campaign in Senegal in 2014. I first worked as an HSE Supervisor within the logistics team but in 2015 I was promoted to logistics co-ordinator. Necotrans provides logistics support to Cairn in the port of Dakar and I am the key link between the two companies. I am in charge of a team of stevedores, crane operators, fork lift truck operators, truck drivers and HSE supervisors who ensure Cairn's requests are met to their high standards – on time and in a safe manner.

Prior to working for Cairn I was a teaching assistant at a university, delivering HSE courses. As part of my BA, I had completed a dissertation on Corporate Social Responsibility but I had no oil and gas experience. As a result of my experience with Cairn I was able to complete my MA in Business Administration and HSE with a project on 'Risk Analysis in the Oil and Gas Industry'.

As an international oil and gas company Cairn has a lot of experienced people who are always happy to help me if I have any questions. This gives me confidence to do things I may not have done before because I can always find guidance. The support goes both ways; we work to deliver what Cairn needs and they help us to deliver it.

Training is a big part of our activities. We have received training in lifting, banksman and slinging, oil spill response, risk assessment, fire extinguishing and first aid. One of the biggest focuses in our day-to-day work is on HSE and understanding that people are more important than the job. If we identify a hazard, a danger to anyone, we understand that we can stop the job we are doing at any time.

As a Senegalese I am excited about the oil and gas industry in Senegal because I think it is a great opportunity for my country. Of course there are concerns that the development of this industry must be managed in a proper and transparent way and our country's leaders know they need to listen to the needs and concerns of their people. It is an opportunity to create a new sector in the country's economy, a source of energy and jobs for the young. I am proud to be one of the Senegalese people involved in this new sector.

"As a Senegalese I am excited about the oil and gas industry in Senegal because I think it is a great opportunity for my country."

Amadou Sakhir Gaye

Cairn in Senegal continued

Sharing Benefits in Senegal

In 2015, world leaders committed to the UN Sustainable Development Goals (SDGs) which set out 17 prioritised areas including ending poverty, ensuring access to energy, protection of ecosystems, addressing climate change and responsible working practices.

Although all SDGs may not be relevant to every company, we recognise a responsibility to look at our activities to identify both where our business adds value for society and where we may need to mitigate for potential negative impacts across environmental, social and governance related issues.

In June 2016, we commissioned a review based on the SDGs to identify, where relevant, any of our activities which could impact on or support any of these goals. This helped to inform our approach to delivering benefits for our stakeholders in Senegal and is set out in the three strands shown below.

Supporting Economic Growth and Good Governance

To deliver:

- Energy source
- Foreign investment
- Transparent payments to government
- Common principles
- Informed regulators
- Shared knowledge

Approach

- Institutional capacity building
- EITI
- UNGC

2016 Performance

- 208 Institutional stakeholders participated in CSL sponsored capacity building
- US$5.1 million payments to the Senegalese Government
- Part of EITI MSG

Link to SDGs

- **7. Affordable and clean energy**
- **16. Peace, justice and strong institutions**

Promoting Local Participation

To deliver:

- Local employment
- Local business development
- Decent work standards
- Improved infrastructure

Approach

- Recruitment policy
- Procurement policy
- Contractor and supplier capacity building
- Workforce skills development
- Partnerships

2016 Performance

- 93% of Dakar office personnel were Senegalese nationals
- 22% of project staff in or offshore Senegal were Senegalese nationals

Link to SDGs

- **8. Decent work and economic growth**
- **9. Industry, innovation and infrastructure**

Social Investment

Proactive contributions or actions we take to help bring benefits to communities where we operate

Approach

- Social investment plan
- Education and training
- Enterprise development
- Community development
- Charitable giving partnerships

2016 Performance

- US$137,839 social investment expenditure

Link to SDGs

- **3. Good health and well-being**
- **4. Quality education**
- **5. Gender equality**

Social Investment

Targeted social investment is a big part of our activity in Senegal in keeping with our wider Group strategy to deliver value for all stakeholders.

We seek to make a positive social impact in every area that we work. We have a group Corporate Social Responsibility Policy which states that Cairn 'will assist in the development of local community programmes where it operates, in consultation with local government, the public and stakeholders'. As part of this we have developed a social investment plan specific to Senegal which supports the four areas the business has identified for social investments across the Group, being: enterprise development; education and training; environment, health and well-being; and charitable giving and humanitarian aid.

As well as providing English language and oil and gas awareness training we have also supported the following community projects: the British Council's Great Entrepreneur project, a competition for local projects with training and coaching for the winner; ECOBAG, a local business which collects plastic waste and recycles it into plastic pellets for onward sale; and The Hunger Project, a women-led microfinance project. During 2016 our social investment expenditure in Senegal amounted to US$137,839.

Great Entrepreneur competition

Supporting local entrepreneurship

In 2015 we supported a project sponsored by the British Council called the Great Entrepreneur competition with a contribution of US$30,000 which went towards the 2016 competition. This competition selects a shortlist of projects in Senegal whose winners are then given a range of training and coaching opportunities to build their business. From these an eventual winner is chosen. The aim of the competition is to promote opportunities for young entrepreneurs in Senegal and develop their skills to progress their ideas. This is in line with some of the attributes we look to promote amongst our own workforce, namely the high performing behaviour 'Be Entrepreneurial'.

Marieme Mbaye.

In 2016 the winner of the competition was Marieme Mbaye from Greenwash Africa who was awarded approximately US$14,000. Marieme co-founded Greenwash Africa which is an eco-friendly car wash that uses no water, uses only biodegradable products and also cleans home furnishings. It aims to reduce water consumption and improve environmental awareness in Africa. It also aims to help street car washers, thereby contributing to job creation. The aim is to grow the business to offer a service in other African countries including Mali and Cote d'Ivoire. Since winning the Great Entrepreneur competition Greenwash has increased its number of clients significantly due to the publicity it has received.

Cairn in Senegal continued
Social Investment continued

The Hunger Project

Helping women in rural communities

The Hunger Project (THP) is a global, non-profit, organisation committed to ending hunger and poverty with sustainable, women-led solutions. We have supported THP in Senegal since 2015.

Senegal was the first country of intervention for THP in Africa which has been working there since 1991. In Africa, The Hunger Project works to build sustainable community-based programmes through epicentres which are community buildings around which communities can organise and provide central services.

The epicentre brings together clusters of rural villages giving them more influence with local government than a single village is likely to have and increasing a community's ability to collectively utilise resources and access basic services. In Senegal THP have been working with 10 epicentres that cumulatively serve a population of over 178,000 people and over 200 villages.

Part of our support for THP goes towards their programme to create a women-led microfinance programme that includes financial management training for the whole community, training facilitators, rural bank lenders and technical staff and provides savings facilities and microloans for income-generating activities based around small-scale trading and farming.

With the initial funding received from Cairn, THP have been able to run this microfinance programme (incorporating funding and capacity building) in all the Senegal epicentres. The focus is to develop the microloans programme into a genuinely member-owned and operated initiative, recognised by the government or regulatory body as a financial cooperative. THP's aim is to support the rural epicentres to become self-reliant. In 2016, one of the 10 epicentres reached self-reliance. Cairn has committed to support THP in 2017 to support further progress towards self-reliance for the remaining nine epicentres. Cairn has contributed a total of US$116,790 to THP over the course of 2015 and 2016.

"In Senegal THP have been working with 10 epicentres that cumulatively serve a population of over 178,000 people and over 200 villages."

ECOBAG

Supporting local business

Cairn first became involved in the Great Entrepreneur competition through its support of the ECOBAG project. ECOBAG won the Great Entrepreneur competition in 2014. ECOBAG collects plastic waste from neighbourhoods and recycles it into plastic pellets to sell on to producers of plastic products. The project promotes waste recycling and a community refuse collection system. Cairn committed to support ECOBAG in 2015 up to the value of US$25,000. Cairn's funding contributed to the purchase of machines to wash and crush the plastic waste in 2016. With our support the founder of ECOBAG, Amy Mbengue, has succeeded in growing the business, increasing plastic pellet production from one to three tons per month and going from employing five workers to employing an additional 15 workers, 80% of whom are female.

Amy Mbengue, founder of ECOBAG

I started ECOBAG at the end of 2014 with the aim of tackling the environmental problems facing Senegal, especially those caused by plastic. ECOBAG's objective is to develop a circular waste economy and to fight against youth unemployment. Cairn was a critical financial and non-financial support for ECOBAG, helping me to build the business through the acquisition of new equipment.

I came up with the idea of ECOBAG in 2011. We were able to start the business almost four years later despite the many difficulties along the way. It was a big challenge for me. Today I feel a great sense of pride when I see my dream come true even if there is still so much more I want to achieve with ECOBAG. My parents and my family feel great pride also.

The workers I employ have a job that allows them to take charge of themselves and which especially allows the empowerment of women.

My goal is to extend ECOBAG at a national, regional and international level but also to start the second phase of development.

ECOBAG team on site.

"The workers I employ have a job that allows them to take charge of themselves and which especially allows the empowerment of women."

Amy Mbengue, founder of ECOBAG

Recipient of funding from The Hunger Project
Madame Bolo Sow,
Namarel Epicentre, Senegal

I first became involved in the Namarel epicentre in 2012. With the advice of the manager of the rural bank of Namarel I took out my first loan in order to generate income. I bought four sheep and after nine months of livestock farming I sold them at a profit. During the period I succeeded in paying off my credit and saving my profit before taking out a new loan. I continue to be involved in livestock activity but I am also now involved in trading detergent products in the villages and surrounding settlements and with a new loan I have started to sell women's shoes ordered from Dakar. The Hunger Project is an organisation which really helps women, empowering them to take charge of their own affairs and giving them access to credit in isolated areas where there are no financial institutions.

> **"With the advice of the manager of the rural bank of Namarel I took out my first loan in order to generate income."**
>
> Madame Bolo Sow, Namarel Epicenter, Senegal

Bolo Sow.

What next?
Further exploration and appraisal drilling

Drilling offshore Senegal resumed in January 2017 as part of Cairn's third phase of the exploration and appraisal campaign in Senegal. As Cairn's activities in Senegal develop, acting responsibly in all our relationships with local stakeholders remains a key focus for the business in order to progress and deliver value from the significant resource base discovered offshore Senegal alongside Cairn's joint venture partners.

Key Performance Indicators
2016

2016 Key Performance Indicators (KPIs)

Cairn has both financial and non-financial KPIs in place which are used to monitor progress in delivering the Group's strategy.

The 2016 KPIs, which were set out on page 24 of the Annual Report and Accounts 2015, related to delivering exploration and appraisal success, portfolio management, delivering operational excellence, maintaining licence to operate and delivering a sustainable business.

The final scoring of the 2016 KPIs was made at the Remuneration Committee meeting in March 2017 and subsequently approved by the Board.

Strategic objective:
Deliver exploration and appraisal success

Purpose Grow the resources and reserves base to provide a basis for future growth

2016 KPI and measurement	2016 performance	KPI Remuneration Committee decision
Progress the Senegal SNE discovery through the prudent investment of capital funds, de-risking the path to commerciality in a cost-effective and timely manner. 2C resource valuation;	Four wells successfully drilled and evaluated on the SNE field for a cost within the original three well budget;	**Substantially achieved**
	Net resources upgraded from 155.1 mmboe to 201.4 mmboe at year-end;	
3C/1C ratio;	P10/P90 gross resources ratio narrowed;	
Cumulative E&A investment divided by the 2C resources (US$/bbl).	E&A investment level at <$4/bbl.	
	14 Read more: CEO's Review on P14-21	
Invest in exploration opportunities with due consideration to finding efficiency. Invest E&A funds within budgetary guidance to add new volumes at industry leading finding costs.	Bellatrix-1 dual-target exploration and appraisal well was unsuccessful at primary target but discovered gas in shallower horizons;	**Not achieved**
	Laverda exploration well encountered 13ft net oil pay in a single Tay sand with recoverable P50 volumes estimated at between 2 and 3 mmbbls. The deeper Fulmar play was dry;	
	Farm-in to the Aurelia prospect in Barents Sea. The well failed on reservoir quality and hydrocarbon type.	
	14 Read more: CEO's Review on P14-21	

Strategic objective: Portfolio management

Purpose Active portfolio management and acreage optimisation

2016 KPI and measurement	2016 performance	KPI Remuneration Committee decision
Develop an inventory of exploration and appraisal opportunities, including prospects and leads which meet Cairn's technical and commercial criteria and can provide drilling opportunities for the period 2017 onwards. Mature a minimum of four new independent 'drill-ready' prospects which meet investment criteria and which could be considered for drilling in 2016 or 2017.	Awarded seven blocks, including two as operator, in the 2016 APA (offshore Norway); Award of one licence option in 2015 Atlantic Margin Oil and Gas Exploration Licensing Round in the Porcupine Basin, offshore Ireland; Target of securing/maturing four or more new independent opportunities that met our investment criteria was not achieved.	**Partially achieved**

14 Read more: CEO's Review on P14-21

Strategic objective: Deliver operational excellence

Purpose Deliver operational excellence in all 2016 activities

2016 KPI and measurement	2016 performance	KPI Remuneration Committee decision
Deliver all operated and non-operated E&A projects (technical studies, surveys and seismic) on schedule and budget, with full data recovery. Projects and products delivered to the quality required, on schedule and within budget.	Four wells successfully drilled and evaluated on the SNE field for the original budgeted price of three; Sangomar-Rufisque 3D seismic on schedule for delivery in Q1 2017; Boujdour Maritime 3D seismic completed; Final interpreted volumes for the Horda 3D in Norway and the West of Kraken 3D in UK completed.	**Substantially achieved**

14 Read more: CEO's Review on P14-21 and Financial Review on P48-51

2016 KPI and measurement	2016 performance	KPI Remuneration Committee decision
Progress North Sea development projects, on time and budget. Ensure projects remain within capital guidance and first oil schedule remains within base case estimates with key milestones met.	Kraken development remains on schedule with first oil anticipated in H1 2017. The latest capex estimate is over 10% lower than the sanction estimate (>US$300m); Key milestones on Kraken set for 2016 have been accomplished including the completion of four producer and four injector wells; full subsea installation; safety case approval; and the FPSO sail-away from the shipyard in Singapore for UK waters; Operator is targeting first oil in H2 2017 on Catcher; Significant progress has been made on Catcher including the completion of eight wells with further drilling ongoing; substantial completion of the offshore installation; and the FPSO hull has been delivered and fabrication of the topside modules is progressing well; Provided input and assurance to Operator on concept selection decision on Skarfjell.	**Substantially achieved**

14 Read more: CEO's Review on P14-21 and Financial Review on P48-51

Key Performance Indicators continued
2016 continued

Strategic objective: Maintain licence to operate

Purpose Deliver value in a safe, secure and environmentally and socially responsible manner

2016 KPI and measurement	2016 performance	KPI Remuneration Committee decision
Minimise injuries and environmental incidents in 2016 operated activities: Total Recordable Injury Rate (TRIR) target of less than 2.0 TRI/million hours. No oil spills to the environment.	TRIR of 1.04; Approximately 1 bbl of oil was released to the environment during testing of SNE appraisal wells in Senegal. 52 Read more: Working Responsibly on P52-71	**Partially achieved**
Achieve targets for HSE leading performance indicators (LPIs) linked to elements of the HSE culture framework. Progress against HSE LPIs. Further embedding of HSE culture and behaviours.	Improvements made to the CRMS with revision of CR policies, emergency and business continuity plans and travel risk assessments, security and support; OSPAR reverification completed without issue; Work ongoing on HR People Management Manual and roll out of management training. 52 Read more: Working Responsibly on P52-71	**Substantially achieved**

Strategic objective: Deliver a sustainable business

Purpose Maintain a self-funding business plan

2016 KPI and measurement	2016 performance	KPI Remuneration Committee decision
Maintain liquid reserves including undrawn committed banking facilities to meet planned funding commitments plus a cushion at all times. Development of a funding strategy to ensure ability to execute value-generative plan, maintaining liquid reserves to meet planned commitments whilst retaining a funding cushion.	Funding headroom cushion maintained at all times; Significant cost reductions or deferrals achieved from original 2016 work programme will allow enlarged drilling programme and pursuit of new venture opportunities to be fully funded. 48 Read more: Financial Review on P48-51	**Substantially achieved**
Make tangible progress on Cairn India Limited (CIL) shares freeze by progress of action under the UK-India Investment Treaty. Milestones in the arbitration including filing of the Statement of Claim and India's filing of its Statement of Defence.	Statement of claim submitted on schedule; India's statement of defence submitted in February 2017; Agreement of Indian tax office in December 2016 that dividends are not restricted. 48 Read more: Financial Review on P48-51	**Substantially achieved**

2017 Key Performance Indicators (KPIs)

The 2017 Group KPIs in the table below were set by the Board in December 2016 and are based on the Group's current portfolio, prospects and objectives set out in the 2017 Business Plan.

Strategic objective: Deliver exploration and appraisal success

Purpose Grow the resources and reserves base to provide a basis for future growth

Objective	2017 KPI
Maximise value in Senegal	Safely, cost effectively and successfully drill, evaluate and flow test appraisal wells on the SNE field in Senegal to allow preparation of the Evaluation Report and update our estimate of resources and capital required to develop the field in a timely manner.
Achieve exploration success through discovery or addition of commercial hydrocarbons in 2017	Efficiently discover commercial quantities of hydrocarbons through maturation and drilling of select exploration and appraisal wells across the portfolio. Measured by: new commercial discoveries based on 2C resources found; cumulative net volumes found versus group target; and finding efficiency expressed in US$/bbl versus industry benchmarks.

Risks to the achievement of KPI

- Exploration and appraisal
- Operational and project performance
- Political and fiscal uncertainties
- Reliance on JV operators for asset performance
- Staff recruitment and retention

39 Read more: **How We Manage Risk** on **P39-47**

Strategic objective: Portfolio management

Purpose Active portfolio management and acreage optimisation

Objective	2017 KPI
Portfolio optimisation and replenishment	Develop an inventory and timeline of exploration and appraisal opportunities which meet Cairn's technical and commercial criteria. Measured by increasing the prospect inventory by securing or maturing new independent opportunities from within or outwith our portfolio.

Risks to the achievement of KPI

- Securing new venture opportunities
- Access to internal or external funding
- Sustained low oil and gas price volatility

39 Read more: **How We Manage Risk** on **P39-47**

Key Performance Indicators continued
2017 continued

Strategic objective: Deliver operational excellence

Purpose Deliver operational excellence in all 2017 activities

Objective	2017 KPI	Risks to the achievement of KPI
Successfully complete operated and non-operated 2017 work programme	Successfully progress our development and production projects against key milestones including, as appropriate, capex, opex and sales volume targets.	Delay in Kraken and Catcher production start-up schedule Operational and project performance Reliance on JV operators for asset performance Staff recruitment and retention

39 Read more: How We Manage Risk on P39-47

Strategic objective: Maintain licence to operate

Purpose Deliver value in a safe, secure and environmentally and socially responsible manner

Objective	2017 KPI	Risks to the achievement of KPI
Deliver activities with a focus on the safety of people and the environment	Achieve leading HSSE indicators linked to four categories within the Group's Corporate Responsibility Management System (Business Relationships, Society & Communities, People and the Environment). Achieve lagging HSSE indicators linked to the International Association of Oil & Gas Producers (IOGP) targets and guidelines. Investing in People & Systems.	Health, safety, environment and security Stakeholder reaction to operations Fraud, bribery and corruption Staff recruitment and retention

39 Read more: How We Manage Risk on P39-47

Strategic objective: Deliver a sustainable business

Purpose Maintain a self funding business plan

Objective	2017 KPI	Risks to the achievement of KPI
Manage balance sheet strength	Develop and implement a funding strategy that allows a value generative plan to be executed and ensures a minimum headroom cushion from existing sources of funding is maintained.	Political and fiscal uncertainties Delay in Kraken and Catcher production start-up schedule
	Make tangible progress under the UK-India bilateral treaty arbitration.	Access to internal or external funding Sustained low oil and gas price Restriction on ability to sell CIL shareholding

39 Read more: How We Manage Risk on P39-47

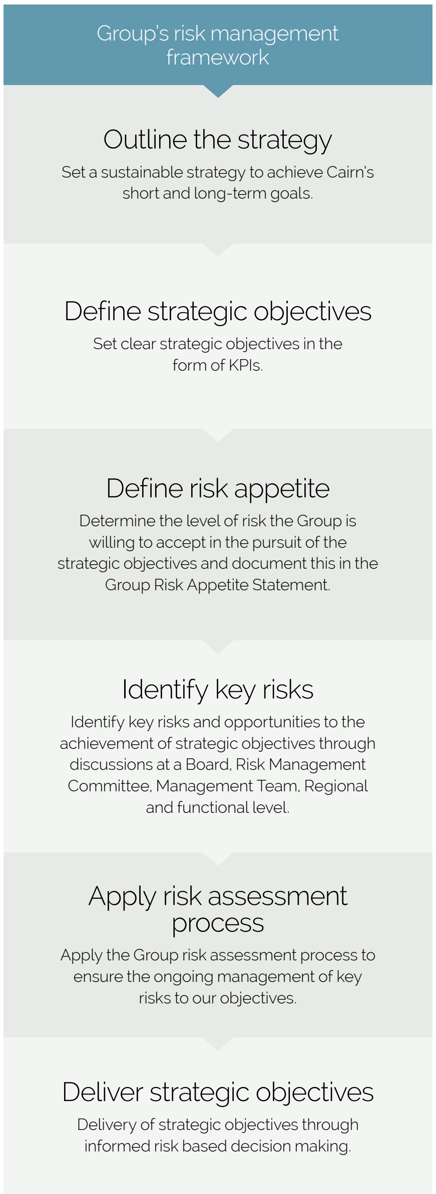
How We Manage Risk

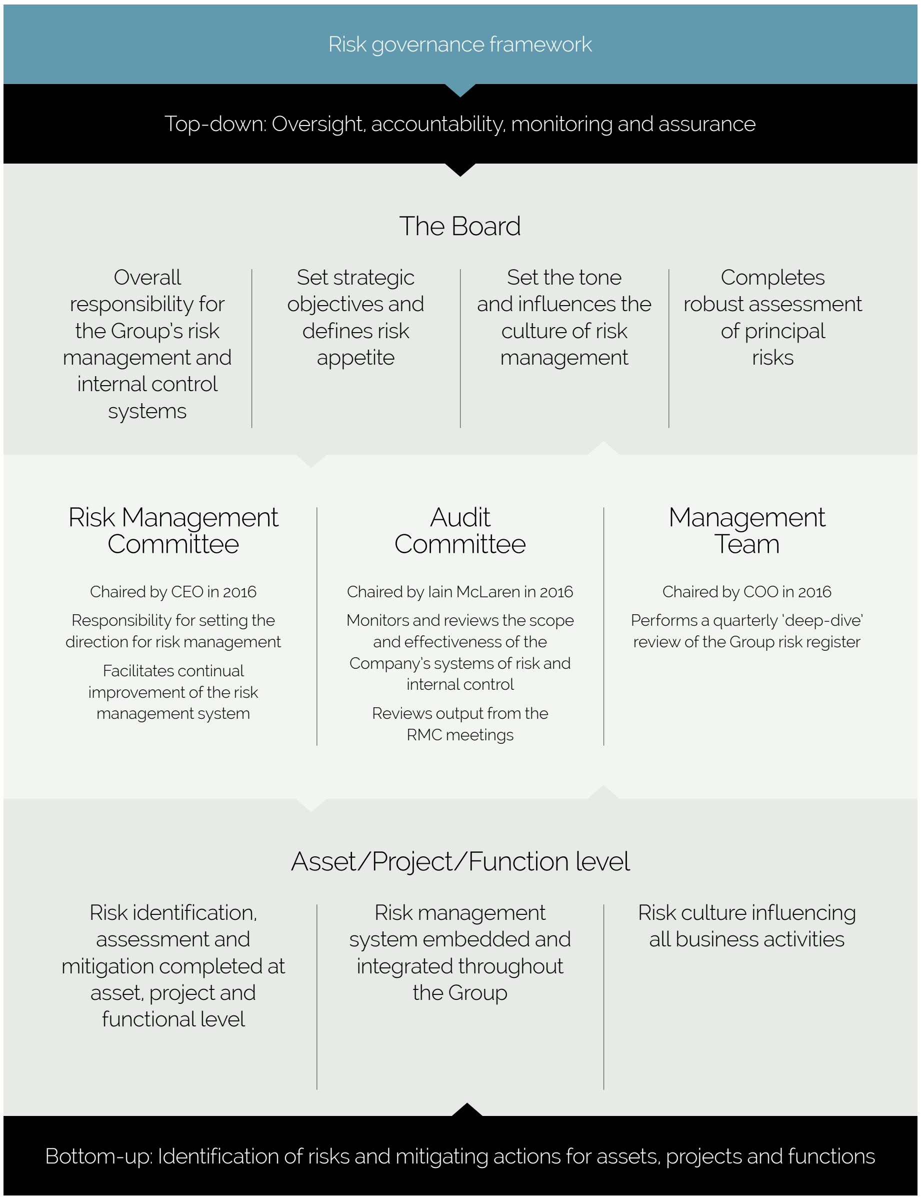
Managing business risks
Managing risks and opportunities is a key consideration in both determining and delivering the strategy. This approach to risk management is not intended to eliminate risk entirely, but provide a means to identify, prioritise and manage risks and opportunities and enable the Group to effectively deliver its strategic objectives in line with the Group's appetite for risk.

Strategic objectives in the form of KPIs are set annually. Determining the level of risk the Group is willing to accept in the pursuit of these objectives and then identifying and managing these risks and opportunities to an acceptable level is a fundamental component of the Group's risk management framework. As outlined below, the management of risk and opportunity plays a key role in the successful delivery of the Group's strategy.

Risk governance
The Group's framework for risk management promotes a bottom-up approach to risk management with top-down support and challenge. The risk register is central to the risk management process and forms the basis for capturing and discussing risk throughout the organisation. Risks and opportunities are identified, assessed and managed at an asset (e.g. Catcher), project (e.g. new ventures opportunity) and functional level (e.g. information systems team). Reporting of these risks within the organisation is structured so that risks are escalated through various internal management and Board committees and, when appropriately material, to the Board itself.

The Board has overall responsibility for ensuring the Group's risk management and internal control frameworks are appropriate and embedded throughout the organisation. Principal risks are reviewed at each Board meeting and, at least once a year, the Board undertakes a risk workshop to complete a robust assessment of the principal risks. This includes determining and setting the Group's risk appetite and associated tolerance levels which are considered acceptable in the pursuit of strategic objectives. This integrated approach to risk management has been and continues to be critical to the delivery of strategic objectives.





How We Manage Risk continued

Responding to the changing risk environment in 2016
As part of the Group's commitment to ensuring risk continues to be managed effectively, it seeks to continually improve our risk management system. As part of this, the following activities were completed in 2016.

- the Board, as it has in previous years, completed a risk workshop to undertake a robust assessment of the principal risks and opportunities impacting the delivery of the Group's strategic objectives. As part of the workshop, the Board confirmed that the risk appetite and supplementary risk tolerance levels remained appropriate;
- the Group's risk management policy and procedure were revised and updated to ensure risks are being managed in a consistent manner across the Group, regardless of geography. The procedure was rolled out in Q1 2016;
- the Group's three regions (Senegal, UK & Norway and International) held monthly risk review meetings to consider risks, mitigations and actions;
- a more rigorous and standardised approach to managing risks was adopted across the Group with a focus on performing more detailed reviews on those risks requiring further treatment. This review focused on ensuring actions were being implemented and tracked;
- the Group undertook a review of potential risk management software suppliers with the remit of assessing the benefits of implementing a software application across the Group. The purpose of the application is to make the process more systematic and structured and further enhance the Group's bottom-up approach to risk management; and
- EY, the Group's internal auditor, delivered the annual internal audit plan which consisted of a number of risk areas identified from the risk register. The Group has been working through the year to implement the identified improvements.

Viability Statement

Strategy, business model and context
The Group's strategy and business model are described on page 4 of this report.

Following the significant oil discovery offshore Senegal in 2014 the group is focused on appraising this significant resource base and from 2018 onwards, Cairn plans to submit the exploitation plan. This exploitation plan will set out a proposed development scheme for the Senegal discovery and an anticipated timeline to first production.

The Group also holds interests in two UK North Sea developments where production is forecast to commence in H1 2017. This production will generate significant operating cash flows which will be deployed, in the near term, on the continued appraisal of Senegal and across the Group's wider exploration and appraisal portfolio.

Assessment process and key assumptions
The Group's prospects are assessed primarily through its annual business planning process. This process includes a Board strategy session, led by the Senior Leadership Team, at which the performance and prospects of the business are examined and capital allocation decisions are made. The outputs from the business planning include a set of Key Performance Objectives, the group risk matrix, the anticipated future work programme and a set of financial forecasts that consider the sources of funding available to the Group against the capital requirements of the anticipated future work programme (the base plan).

Key assumptions which underpin the annual business planning process include forecast oil and gas prices, forecast cost levels for oil & gas services and capital projects, production profiles of the UK North Sea development projects and the availability of debt under the Groups lending facilities.

The Board recognises that a significant part of the anticipated work programme is dependent on the results of future exploration or appraisal activity and also that it is the Group's strategy to actively manage its licence portfolio to optimise its planned capital allocation. Consequently, reflecting this inherent variability in the longer term work programme, the Board has determined that three years is the appropriate period over which to assess the Group's prospects.

Viability
The Principal risks and uncertainties that affect the board's assessment of the Group's viability in this period are:
- development project schedule and budget risk;
- the effect of sustained lower oil prices on the business and on our partners financial position;
- restriction on ability to sell Cairn India shareholding; and
- lack of exploration or appraisal success.

The base plan incorporates assumptions that reflect the impact of these Principal risks as follows:
- material budget contingencies and allowances are included for development projects as well as appropriate delay assumptions;
- projected operating cash flows assume oil and gas prices in line with the current forward curve;
- whilst the resolution of the Cairn India dispute remains a strategic priority, the funding plan does not include monetisation of the Group's shares in Cairn India Limited; and
- lack of exploration or appraisal success would impact on the delivery of Cairns strategy but would not be expected to impact on the Groups ability to fund its committed work programme.

The Board also considers further scenarios around the base plan. These primarily reflect a more severe impact of the principal risks, both individually and in aggregate, as well as the additional capital requirements that would result from future exploration or appraisal success or the acquisition of new assets.

The directors consider the impact that these Principal risks could, in certain circumstances, have on the company's prospects within the assessment period, and accordingly assess the opportunities to actively manage its licence portfolio and planned capital allocation as well as to bring in additional sources of funding at key milestones in asset development.

Based on the actions available to them, the directors have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the three year period of their assessment.

Principal risks to the Group in 2016/2017

Principal risks & uncertainties
During 2016, through a number of internal forums such as the Group Risk Management Committee and Management Team, the Group regularly reviewed the risks which could adversely impact on the achievement of strategic objectives. The Board also receive a risk report, highlighting the key risks and movements in risks, at each Board meeting. The tables below provide a summary overview of the principal risks to the Group at the end of 2016, the potential impacts, the mitigation measures, the risk appetite and the KPIs or strategic objectives the risks may impact on.

The Board confirm that a robust assessment of the principal risks facing the Company, including those that would threaten the business model, future performance, solvency or liquidity was completed in 2016.

Strategic objective: Deliver exploration and appraisal success

Principal risk: Exploration and appraisal
Owner: Director of Exploration

2015-2016 movement	No change
Risk appetite	High – Exposure to exploration and appraisal failure is inherent in accessing the significant upside potential of a successful discovery and this has been, and remains, a core value driver for Cairn. The Group invests in data and exploits the strong experience of Cairn's technical teams to mitigate this risk.

Impact	Mitigation	Risk information	2017 KPI objectives
Loss of investor confidence	Active programme for high-grading new areas through licence rounds, farm-ins and other transactions.	Completion of four successful appraisal and exploration wells in the SNE field in H1 2016 which led to an increase in the estimated gross recoverable oil resource.	Maximise value in Senegal
Limited or no value creation	Inventory of prospects and leads that offer opportunities with a balance of geological and technical risks.	Exploration and appraisal wells completed in the UK North Sea Greater Catcher Area and the Barents Sea.	Achieve exploration success through discovery or addition of commercial hydrocarbons in 2017
Failure of the balanced portfolio business model	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.	The Group will continue to assess and rank opportunities for future drilling in 2017 and beyond.	
	Establishment of Exploration Leadership Team to undertake peer reviews and assurance.		

Principal risk: Sustained low oil and gas price
Owner: Chief Financial Officer

2015-2016 movement	No change
Risk appetite	Medium – Exposure to commodity prices is fundamental to the Group's activities. However, the Group manages its investment programme to ensure that a threshold economic return is delivered and the business model is funded even in sustained downside price scenarios.

Impact	Mitigation	Risk information	2017 KPI objectives
Reduction in future cash flow	Sensitivity analysis conducted to assess robustness of projects and development decisions.	The low oil price has driven down industry costs for both development and exploration projects.	Manage balance sheet strength
Value impairment of development projects	Operators' cost initiatives delivering material cost reductions on development projects.	Debt available under the Group's RBL facility remains at a level consistent with the end of 2015.	Portfolio optimisation and replenishment
JV partner capital constraints	Exploit the low service cost environment for E&A activities.	Cairn increased its working interest in Kraken by 4.5% to 29.5%. Cairn acquired the increased interest from First Oil plc for a nominal amount and assumed working capital liabilities of US$16m.	

How We Manage Risk continued
Principal risks to the Group in 2016/2017 continued

Strategic objective: Portfolio management

Principal risk: Securing new venture opportunities
Owner: Director of Exploration

2015-2016 movement	Increased
Risk appetite	Medium – Building and maintaining a balanced portfolio of current and future exploration, development and production assets is core to the Group's strategy. New opportunities must first meet the Group's strict investment criteria and successfully securing them will be dependent on the prevailing competitive environment.

Impact	Mitigation	Risk information	2017 KPI objectives
Loss of investor confidence Loss of competitive edge Failure to replenish the portfolio	Geoscience, new ventures and commercial teams work closely to review and identify prospects. Experience and knowledge throughout the organisation in recognising prospective opportunities. Risk assessments and due diligence process undertaken on all potential new country entries. Development of discretionary capital allocation and opportunity ranking system.	Pre-qualified as an Operator in Norway in late 2015 and were awarded the Group's first operated licence in H1 2016. Awarded seven blocks, including two as Operator, in the 2016 APA and one licence option in the 2015 Atlantic Margin Oil and Gas Exploration Licensing Round. Several new prospects and leads have been matured in existing acreage in Senegal. Despite the low oil price environment, acquiring quality new venture opportunities has been competitive and it is anticipated that this will remain the same for 2017.	Portfolio optimisation and replenishment

Strategic objective: Maintain licence to operate

Principal risk: Health, safety, environment and security

Owner: Chief Executive

2015-2016 movement	No change
Risk appetite	Low – The Group continuously strives to reduce risks that could lead to an HSSE incident to as low as reasonably practicable.

Impact	Mitigation	Risk information	2017 KPI objectives
Serious injury or death	Effectively managing health, safety, security and environmental risk exposure is the first priority for the Board, Senior Leadership Team and Management Team.	The Group's safety performance has been effective overall in 2016 and achieved Total Recordable Injury Rate (TRIR) of 1.05. The Group's target was less than 2.0 per million hours. The rate in 2015 was 0 per million hours.	Deliver activities with a focus on the safety of people and the environment
Environmental impacts	HSE training is included as part of all staff and contractor inductions.	Approximately 1 bbl of oil was released to the environment during testing of appraisal wells.	
Reputational damage	Detailed training on the Group's Corporate Responsibility Management System (CRMS) has been provided to key stakeholders to ensure processes and procedures are embedded throughout the organisation and all operations.	With ongoing operations in a number of countries in 2017, the Group will continue to work responsibly as part of our strategy to deliver value for all stakeholders.	
Regulatory penalties and clean-up costs	Process in place for assessing an operator's overall operating and HSE capabilities, including undertaking audits to determine the level of oversight required.		
	OSPAR reverification completed in 2016.		
	Emergency and oil spill response procedures and equipment are maintained and regularly tested to ensure the Group is able to respond to an emergency quickly, safely and effectively.		
	Third party specialists in place to assist with security arrangements and travel risk assessments.		
	HSE Leading Performance Indicators and targets developed in line with industry guidelines.		
	Findings from 'Lessons learned' reviews are implemented from other projects.		

How We Manage Risk continued
Principal risks to the Group in 2016/2017 continued

Strategic objective: Maintain licence to operate continued

Principal risk: Stakeholder reaction to operations
Owner: Director of Corporate Affairs

2015-2016 movement	No change
Risk appetite	Medium – The Group's strong reputation and licence to operate are core assets for the Group. However, where stakeholder objectives are not aligned, the Group seeks to balance these conflicting objectives when considering investment decisions in line with the Group's strategy.

Impact	Mitigation	Risk information	2017 KPI objectives
Reputational damage	Cairn's aim 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.	Norge Bank divested their interest in Cairn as a result of the Group's operations in Western Sahara. The Group continues to engage with all stakeholders to address any concerns.	Deliver activities with a focus on the safety of people and the environment
Loss of investor confidence	Comprehensive stakeholder management and communication plans have been developed and executed for all operations.		
Loss of licence to operate	Work closely with JV partners to ensure transparency and social responsibility.		
Delays in work programmes	Actively monitor steps being taken by regulators and industry through participation in industry bodies such as the International Association of Oil & Gas Producers and Oil & Gas UK.		

Principal risk: Fraud, bribery and corruption
Owner: Chief Executive

2015-2016 movement	No change
Risk appetite	Low – Cairn is committed to maintaining integrity and high ethical standards in all of the Group's business dealings. The Group has no tolerance for conduct which may compromise its reputation for integrity.

Impact	Mitigation	Risk information	2017 KPI objectives
Legal fines	Business Code of Ethics and bribery and corruption policies and procedures.	Group Code of Business Ethics and ABC procedures updated in 2016.	Deliver activities with a focus on the safety of people and the environment
Criminal prosecution	Due diligence process and questionnaire developed for assessing potential third parties.	Bribery and corruption e-learning training module rolled out across the Group and bespoke bribery and corruption training delivered to the Board in 2016.	
Reputational damage	Annual training programme for all employees, contractors and selected service providers.	The Group's Code of Business Ethics will continue to be applied to all operations across the Group.	
	Extensive financial procedures in place to mitigate against fraud.		

Strategic objective: Deliver operational excellence

Principal risk: Delay in Catcher and Kraken production start-up schedule

Owner: Regional Director, UK & Norway

2015-2016 movement	Decreased
Risk appetite	Low – Operating cash flow from Kraken and Catcher will provide the Group with funding to sustain future exploration and development activity. The Group works closely with all JV partners to mitigate the risk and impact of any operational delay.

Impact	Mitigation	Risk information	2017 KPI objectives
Delay or reduction in future cash flow	Actively engage with all our JV partners early to ensure highly effective working relationships.	Kraken development remains on schedule with first oil anticipated in H1 2017. Key milestones on Kraken set for 2016 have been accomplished including the completion of four producer and four injector wells; full subsea installation; safety case approval; and the FPSO sail-away from the shipyard in Singapore for UK waters.	Successfully complete operated and non-operated 2017 work programme
Increased costs	Actively participate in technical meetings to challenge, apply influence and/or support our partners to establish a cohesive JV view and ensure operational activity is executed in a safe and secure manner.	Catcher is targeting first oil in H2 2017.	
Portfolio replenishment	Frequent site visits to key contractor sites to increase focus on quality assurance performance.	Significant progress has been made on Catcher and several key milestones have been achieved.	
Reduction in debt capacity	Work closely with the Kraken and Catcher operators to monitor and review progress of key milestones.		

Principal risk: Operational and project performance

Owner: Chief Operating Officer

2015-2016 movement	No change
Risk appetite	Low – Delivering operational excellence in all the Group's activities is a strategic objective for the Group. The Group has a low appetite for operational risks which may lead to delays and/or increased costs.

Impact	Mitigation	Risk information	2017 KPI objectives
Increased well costs	Comprehensive set of criteria that must be met before contracting and accepting any rig.	Significant operational milestones achieved in the Group's development projects and Senegal drilling.	Successfully complete operated and non-operated 2017 work programme
Project delays	Work closely with the rig contractors to exert influence and impose our performance expectations.	Seismic processing successfully completed in Senegal (Sangomar-Rufisque), Western Sahara (Boujdour Maritime), Norway (Horda) and the UK (Kraken West).	Deliver activities with a focus on the safety of people and the environment
HSE incident	Management and influence of drilling contractors to ensure Cairn management systems are fully embedded in operations.	There are potential operational threats in 2017 due to the level of the Group's operations and the number of rigs on hire (Stena Drillmax in Senegal, Transocean Leader in Kraken and the Ensco-100 in Catcher).	
Reputational damage	Positive and regular engagement with JV operators and partners to share knowledge and offer support.		

How We Manage Risk continued
Principal risks to the Group in 2016/2017 continued

Strategic objective: Deliver operational excellence continued

Principal risk: Reliance on JV operators for asset performance
Owner: Chief Operating Officer

2015-2016 movement	No change
Risk appetite	Medium – The Group seeks to operate assets which align with the Group's core areas of expertise but recognise that a balanced portfolio will also include non-operated ventures. The Group accepts that there are risks associated with a non-operator role and will seek to mitigate against these risks by working with partners of high integrity and experience and maintaining close working relationships with all JV partners.

Impact	Mitigation	Risk information	2017 KPI objectives
Cost/schedule overruns Poor performance of assets HSE performance Delay in first oil from development projects Impact on asset value	Actively engage with all JV partners early to establish good, trusting working relationships. Actively participate in technical meetings to challenge, apply influence and/or support partners to establish a cohesive JV view. Application of the Group risk management processes and non-operated ventures procedure. Active engagement with supply chain providers to monitor performance and delivery.	The sustained low oil price continues to have a financial impact across the industry and the risk remains that the Group's JV partners may not be able to fund work programme expenditures and/or reprioritise projects. The Group's two development projects and several exploration projects are operated by joint venture partners and the ability to influence can sometimes be limited. The Group continues to work closely with a number of partners in the UK & Norway, Senegal and International regions.	Successfully complete operated and non-operated 2017 work programme Deliver activities with a focus on the safety of people and the environment

Strategic objective: Deliver a sustainable business

Principal risk: Restriction on ability to sell CIL shareholding
Owner: Chief Financial Officer

2015-2016 movement	No change
Risk appetite	Medium – The Group faces an uncertain macroeconomic and regulatory environment in some countries of operation. The Group is willing to invest in countries where political and/or fiscal risks may occur provided such risks can be adequately managed to minimise the impact where possible.

Impact	Mitigation	Risk information	2017 KPI objectives
Restriction in the funding capacity of the Group	Committed work programme is fully funded from existing sources of funding, principally Group cash and committed debt facilities. Continued engagement with the Indian Government. Initiation of arbitration proceedings.	Restriction on monetising assets in India remains in place. Arbitration proceedings have commenced to resolve the Indian tax dispute and a number of milestones have been achieved including the appointment of an arbitration panel; the filing of the statement of claim; and India's filing of its statement of defence.	Manage balance sheet strength

Principal risk: Political and fiscal uncertainties

Owner: Chief Financial Officer

2015-2016 movement	No change
Risk appetite	Medium – The Group faces an uncertain macroeconomic and regulatory environment in some countries of operation. The Group is willing to invest in countries where political and/or fiscal risks may occur provided such risks can be adequately managed to minimise the impact where possible.

Impact	Mitigation	Risk information	2017 KPI objectives
Loss of value	Operate to the highest industry standards with regulators and monitor compliance with the Group's licence, Production Sharing Contract and taxation requirements.	Cairn has not entered into any new territories in 2016 so the risk has remained static. The Group will continue to monitor changes in fiscal regimes in the areas of operation.	Manage balance sheet strength
Uncertain financial outcomes	External specialist advice consulted on legal and tax issues as required.		
	Maintain positive relationships with governments and key stakeholders.		
	Ongoing monitoring of the political and regulatory environments in which we operate.		

Principal risk: Access to internal or external funding

Owner: Chief Financial Officer

2015-2016 movement	No change
Risk appetite	Low – The Group seeks to develop and implement a funding strategy that allows a value generative plan to be executed and ensures a minimum headroom cushion from existing sources of funding is maintained.

Impact	Mitigation	Risk information	2017 KPI objectives
Work programme restricted by reduced capital availability	Committed work programme is fully funded from existing sources of funding, principally Group cash and debt funding.	Non-core E&A expenditure has been deferred, development costs for future production base have been reduced and Cairn has secured significantly lower costs for ongoing exploration activity.	Manage balance sheet strength
Loss of value	Disciplined allocation of capital across portfolio.	Continued to rationalise the portfolio with the disposal of non-core assets.	
	Continue to assess other forms of financing and pursue release of Indian assets.	Debt available under the Group's RBL facility remains at a level consistent with the end of 2015.	

Principal risk: Staff recruitment and retention

Owner: Group HR Manager

2015-2016 movement	Decreased
Risk appetite	Low – The Group relies on motivated and high quality employees to deliver the Group's strategic objectives and is committed to developing and supporting all employees.

Impact	Mitigation	Risk information	2017 KPI objectives
Inadequate resource to deliver work programme	Regional Directors and Departmental Heads agree resource requirements as part of the annual work programme and budget processes.	Staff retention remains strong, providing stability and consistency in the delivery of current and future projects.	Successfully complete operated and non-operated 2017 work programme
Loss of key knowledge and experience	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.	Prevailing market conditions have allowed the Group to attract a number of highly experienced personnel for key positions in the Group.	
	Succession planning is in place for all areas of the business.		
	Rewarding performance process and benefits programme.		

Financial Review
James Smith, Chief Financial Officer

Significant progress

Significant progress has been made on the Group's two North Sea development projects and, with the Kraken FPSO now on location, first oil production is targeted for Q2 2017. Cairn successfully completed a four well programme in 2016 in Senegal and a further exploration and appraisal programme is currently underway.

Highlights of 2016

Financial

- US$335 million (m) Group net cash at 31 December 2016.
- Norwegian tax receivable of US$26m at 31 December 2016.
- Reserve Based Lending bank facility remains undrawn with peak availability expected to reach US$350m to US$400m.
- Forecast development expenditure on Catcher and Kraken for 2017 is US$150m and committed drilling E&A expenditure for 2017 is estimated at US$170m, predominantly in Senegal. At 31 December 2016, remaining cash outflows in respect of activities undertaken in 2016 were expected to be US$37m.

Subsequent to year end:

- US$75m funding from FlowStream Commodities Ltd (FlowStream) in exchange for the proceeds from 4.5% of Kraken production, stepping down to 1.35% after 10% return achieved.
- NOK 500m (~US$60m) three year Norwegian Exploration Finance Facility, allowing the company to borrow against future Norwegian exploration tax refunds.

Overview

Subsequent to year-end, Cairn executed two financing arrangements further enhancing the Group's liquidity.

A NOK 500 million (~US$60m) Exploration Finance Facility allows the Company to borrow against any Norwegian tax refunds from future exploration.

Related to the additional 4.5% Kraken working interest acquired in 2016, the Group also secured funding of US$75m from FlowStream in exchange for the proceeds from 4.5% of Kraken production. FlowStream's entitlement to Kraken production reduces to 1.35% if FlowStream achieves a 10% return and reduces to 0.675% after FlowStream achieves a 15% return. An additional tranche of US$125m in return for a further proceeds from production across Kraken and Catcher is available, subject to mutual consent, at Cairn's option. FlowStream's sole recourse for the funding is to its production rights from the assets.

Confirmation received via the international arbitration that accrued dividends of US$51m are no longer restricted, immediate release of this sum has been requested from CIL.

Cash

Cairn had cash and cash equivalents of US$335m at 31 December 2016, representing a net cash outflow of US$268m over the year.

Cash outflows in the period included Senegal exploration costs of US$105m related to the completion of a four well exploration and appraisal programme which commenced in 2015.

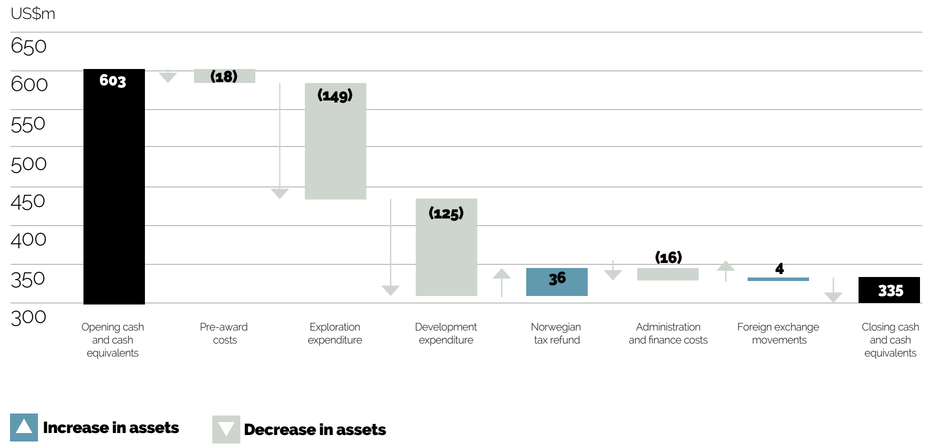
Development expenditure primarily related to costs of the Kraken development as Cairn's share of capital expenditure on Catcher remained carried throughout the year.

Forecast development expenditure for 2017, taking the UK development projects through to cashflow generation, is US$150m; and remaining currently committed drilling exploration and appraisal expenditure for 2017 is estimated at US$170m, predominantly in Senegal.

Cairn remains fully funded to meet all existing commitments at the balance sheet date. Cairn's Reserve Based Lending bank facility remains undrawn, with peak availability expected to reach US$350m to US$400m.

Cash

2016 Net Funds Movements

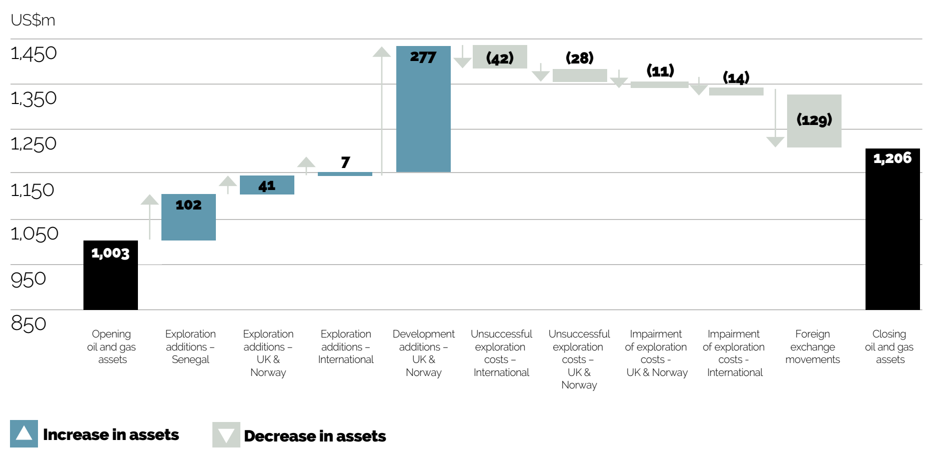


Analysis of the cash flow movements on assets to additions in the financial statements is as follows:

	Exploration				Development
	Senegal US$m	UK & Norway US$m	International US$m	**Total US$m**	**UK & Norway US$m**
Additions	102	41	7	**150**	**277**
Working capital and provisions movements	3	3	(2)	**4**	**(87)**
Carried (non-cash)	–	(5)	–	**(5)**	**(65)**
Cash outflow	**105**	**39**	**5**	**149**	**125**

Oil and Gas Assets

2016 Movements in Oil and Gas assets



Financial Review continued

Highlights of 2016

Resources & Reserves

A total of 51.5 mmboe booked as 2P reserves and 239 mmboe booked as 2C Contingent Resources on a net working interest basis at 31 December 2016.

India Tax Dispute

Confirmation received via the international arbitration that dividends of US$51m due from Cairn India Limited (CIL) are no longer restricted, Cairn has requested the immediate release of the sum from CIL.

International arbitration proceedings are progressing in respect of Cairn's claim under the UK-India Bilateral Treaty with the main Statement of Claim and the Statement of Defence now submitted.

Exploration and Appraisal Assets

Senegal

Additions in 2016 included US$78m of drilling costs predominantly relating to the SNE-2, SNE-3, SNE-4 and BEL-1 appraisal wells completed in the year. A further US$5m was incurred in advance of the 2017 SNE-5 and SNE-6 appraisal wells.

UK & Norway

Cairn completed two exploration wells in the UK and Norway region during 2016. The UK Laverda exploration well, located in the Greater Catcher Area, successfully discovered commercial volumes of hydrocarbons, though these were not sufficient to support previously capitalised costs and an impairment of US$11m was charged in the year. Cairn's share of cash expenditure of the Laverda well was carried.

The second well, the Aurelia exploration well in the Norwegian Barents Sea was unsuccessful and costs of US$10m have been charged to the income statement.

Further charges of US$10m were made on licences to be relinquished and costs of US$8m on the prior year Kraken West appraisal well were written off as the discovery is no longer considered commercially viable.

International

During 2016, the Group relinquished the C-19 licence in Mauritania and expensed previously capitalised costs of US$32m. Further costs of US$14m relating to the Spanish Point appraisal prospect were impaired. The Group's remaining assets in the International segment are located in Ireland, Malta and Boujdour Maritime, Western Sahara where exploration activity remains at an early stage.

Development Assets

In Kraken, Cairn acquired an additional 4.5% working interest in January for nominal consideration bringing the Group's total working interest to 29.5%. US$16m is included within additions representing working capital balances related to the 4.5% increase. Further Kraken additions in the year were US$165m, including an increase of US$26m in the decommissioning asset.

Cairn's share of capital expenditure on the Catcher development was carried by Dyas BV under the terms of the 2015 farm down. Thus additions of US$96m were largely non-cash and also include an increase of US$27m in the decommissioning asset.

The Group's development assets were tested for impairment, with the Group reducing its long term oil-price assumption to US$70 per barrel. The Group's three year short term assumption remains linked to the forward curve. No impairment charge was recorded.

The Group's development assets are held in a GBP functional subsidiary, which is translated to US$ on consolidation. With the fall in GBP following the EU referendum result, significant foreign currency exchange losses of US$121m are recorded on development assets.

Available-for-Sale Financial Asset – Cairn India Investment and Dividends
Cairn is currently unable to access the value in its ~10% residual shareholding in Cairn India Limited valued at US$656m at 31 December 2016, though the Company is seeking remittance of accrued dividend payments due of US$51m.

International arbitration proceedings are progressing in respect of the Group's claim under the UK-India Bilateral Investment Treaty. Cairn is seeking restitution for losses resulting from the attachment of its shares in CIL and failure to treat the Company and its investments fairly and equitably. Cairn has a high level of confidence in its case under the Treaty and, in addition to resolution of the retrospective tax dispute, its statement of claim to the arbitration panel is seeking damages equal to the value of Group's residual shareholding in CIL at the time it was attached (approximately US$1 billion).

Unsuccessful exploration costs
Unsuccessful exploration costs of US$28m in the UK and Norway region included the cost of two wells (Aurelia, Barents Sea and Kraken West, UK North Sea) and relinquished licences. Further unsuccessful exploration costs in the International region of US$42m included US$32m of costs in Mauritania and a US$7m charge following the relinquishment of acreage offshore Ireland. The remaining US$3m represented costs incurred closing licences in Morocco and Greenland.

Administrative expenses and other costs
The year-on-year increase in administrative expenses and other costs reflected costs incurred on the CIL arbitration and an increase in non-cash share-based payment charges.

Taxation
As the Group's activities continue to focus on assets in the exploration, appraisal and development phases, the Group currently generates no production income and as such no corporation tax was payable in the year.

A cash tax refund is received in Norway in respect of 78% of qualifying exploration and overhead spend. US$36m was received during the current period, with a further US$26m receivable based on 2016 qualifying expenditure. Norwegian deferred tax liabilities at the year-end of US$63m reflect timing differences on the carrying value of exploration assets where a tax refund has been claimed.

The Group's tax credit for the year consisted of a UK deferred tax credit of US$43m and net Norwegian tax credits of US$13m, linked to the tax refund. The UK tax credit followed the recognition of deferred tax assets to offset deferred tax liabilities arising on development asset additions under the Catcher carry. UK deferred tax assets are recognised only to the extent that they offset liabilities and no net UK deferred tax asset or liability exists at the year end.

At 31 December 2016, Cairn had total UK ring fence losses of US$683m. US$514m of losses were recognised as deferred tax assets to fully offset deferred tax liabilities of US$206m. The remaining US$169m of losses represented an unrecognised deferred tax asset of US$68m. With no taxable income and a tax charge distorted by balance sheet additions, the effective tax rate of the Group does not provide a meaningful measure of Cairn's current tax position: the effective tax rate of the Group was 37.3% in the year (2015: (3.5)%).

Results for the Year

	2016 US$m	2015 US$m
Pre-award costs	**(18)**	(35)
Unsuccessful exploration costs	**(70)**	(97)
Administrative expenses and other costs	**(35)**	(31)
Related tax credit	**13**	37
Operational and administrative expenses	**(110)**	(126)
Net finance costs	**(3)**	(1)
Impairment of financial asset	**–**	(319)
Related tax credit	**–**	10
CIL investment and impairment	**–**	(309)
Gain in disposal of oil and gas assets	**–**	27
Impairment of oil and gas assets	**(25)**	(43)
Asset related tax credit/(charge)	**43**	(64)
Oil and gas asset sales and impairment	**18**	(80)
Loss for the year	**(95)**	(516)

Working Responsibly
Introduction

Working responsibly to deliver our strategy

Our commitment to working responsibly is a key part of our strategy, which is to deliver value for our stakeholders by building a balanced portfolio of exploration, development and production assets within the oil and gas lifecycle.

Ensuring we work responsibly is embedded in our strategy. This means delivering value in a safe, secure and environmentally and socially responsible manner.

In order to deliver our strategy we set a series of Key Performance Indicators (KPIs) annually.

There are elements of working responsibly in each of those KPIs with one of them, the Maintain Licence to Operate KPI, dedicated to working responsibly.

In order to support achievement of the Maintain Licence to Operate KPI, we have a series of Corporate Responsibility (CR) objectives; CR is how we describe our working responsibly practices. Our CR objectives are set annually and are grouped under four themes, being: Business Relationships; Society and Communities; People; and Environment. These are illustrated on page 54.

Working responsibly means identifying issues that are material not only to the business but also to stakeholders. We do this through our risk management process which identifies the issues that are material to the business and our stakeholder engagement processes which identify those material to stakeholders.

How we assess material issues

One of our CR objectives this year was to further improve the transparency of the methodology used to identify our material issues for the year. To do so we compiled a list of 15 potentially material issues to Cairn and our stakeholders based on IOGP, UN Sustainable Development Goals and GRI international reporting requirements. Each of those 15 issues has linked sub-issues each of which was ranked to indicate its level of importance to Cairn and to stakeholders (high, significant, medium, low, insignificant).

The importance to Cairn used the latest risk register and Cairn risk criteria. The worst-case sub-issue linked to an issue ranking was used as the overall ranking for the issue as a whole.

The rankings for importance to stakeholders were based on objective criteria which include Cairn's experiences and communications with stakeholders during the course of the year. In 2015 a cohort of stakeholders was used to validate the stakeholder classifications; this will be repeated every other year based on specialist advice.

An external specialist[1] reviewed the issues in 2016 and feedback from the review of methodology and stakeholder expectations was incorporated with actions for improvement into our CR Objectives.

The materiality process is discussed in more detail on our website www.cairnenergy.com/materiality

1 Julie McDowell, former head of Standard Life Sustainability team.

Stakeholder Engagement
Delivering value for our stakeholders is at the core of our approach to working responsibly. Therefore understanding who our stakeholders are and engaging with them to understand what their concerns and priorities are is important.

We have well-structured stakeholder engagement procedures in place at a corporate and project level which enables us to identify and assess issues amongst our stakeholders and then address and respond to them. We do this through tailored engagement with specific stakeholders, disclosure of information and monitoring of stakeholder opinions and actions.

When considering a new project and involvement in a country where we have not worked previously, identifying our

Seven issues were found to be of high or significant importance to both Cairn and stakeholders and thereby deemed material. These issues are analysed in detail in this Working Responsibly section.

Materiality Matrix

We plot issues important to Cairn and important to stakeholders on a materiality matrix.

- High materiality
- Medium materiality
- Low materiality

The 15 potentially material issues appearing on the materiality matrix are listed on page 54, grouped into the four themes identified in our business principles. This has changed some of the issue titles from last year.

Compared to 2015 we have seen an increasing emphasis on business ethics, human rights, climate change and social and economic benefits for our business and stakeholders.

Importance to Cairn	Insignificant	Low	Medium	Significant	High
High				Economics and Funding	
Significant		Employees	Communities Health and Well-being Security	Contractors and Supply Chain Human Rights Social and Economic Benefit	Major Accident Prevention and Safety Ethics, ABC and Transparency
Medium			Equality and Diversity Resource Use		Climate Change, Emissions and Discharges
Low				Biodiversity	
Insignificant	Product Stewardship				

Importance to Stakeholders

stakeholders is one of our priorities and we undertake a stakeholder identification exercise. We draw on the knowledge of our local staff, corporate staff and external agencies, partners and consultants to do this. Using this knowledge we then develop a Public Consultation and Disclosure Plan (PCDP). PCDPs identify stakeholder concerns and issues, the materiality of issues and the associated risks to the business. This enables us to identify actions to mitigate those risks and this also forms part of the PCDP. Stakeholder engagement plans are bespoke to each project and regularly updated to reflect changing stakeholders and their concerns around a project.

Our stakeholder engagement model follows the principles of 'Materiality', 'Inclusivity' and 'Responsiveness' as defined in AccountAbility's AA1000 Accountability Principles Standard (AA1000 APS). AccountAbility is a global organisation providing solutions to challenges in corporate responsibility and sustainable development. This ensures that we engage with internal and external stakeholders, identify and assess our most important CR issues, and address and respond to them in a structured way.

Working Responsibly continued
Our Corporate Responsibility Priorities

15 potentially material issues
7 were found to be of high or significant importance

The fifteen potentially material issues are listed below, grouped into the four themes.

Business Relationships

Economics and Funding H
- Funding
- Investment
- Reserves valuations and capital expenditures

Contractors and Supply Chain H
- Culture and leadership
- Selection
- Competency, training and education

Ethics, ABC and Transparency H
- Principles, policies, CRMS
- Risk and material issues
- Strategy and operations
- Accountability and responsibility
- Advocacy and lobbying
- Cairn ABC practices
- Contractors and suppliers
- Government and authorities
- Whistleblowing
- Communications
- Remuneration
- Tax and payments to government
- Fines and prosecutions
- Non-operated joint ventures and international investments

Society and Communities

Social and Economic Benefit H
- Shared value
- Benefits and impacts to communities
- Local content
- Social investment
- Government relations

Human Rights H
- Working conditions/T&Cs
- Freedom of association
- Modern slavery/security
- Complicity
- Grievance
- Non-discrimination

Communities M
- Local community
- Stakeholders
- Indigenous peoples
- Local labour
- Community health
- Cultural heritage
- Displacement

People

Major Accident Prevention and Safety H
- Asset integrity
- Major accident prevention
- Major oil spill prevention
- Workplace safety

Health and Well-being M
- Workplace health
- Infectious diseases
- Well-being and health support

Security M
- Office
- Personnel
- Local assets
- Travel
- Cyber security

Employees M
- Culture and leadership
- Selection
- Succession
- Workforce planning

Equality and Diversity M
- Anti-discrimination
- Equal pay
- Equal opportunities and diversity

Environment

Climate Change, Emissions and Discharges H
- Energy use and alternative sources
- GHGs
- Other emissions
- Flaring and venting
- Strategic carbon risk
- Discharges/disposals to water and land
- Spills
- Reuse. recycling and waste management
- Stranded assets

Biodiversity M
- ESIA, environmental surveys and ecosystem services
- Biodiversity action plans

Resource Use M
- Water abstraction and use
- Local resources
- Materials

Product Stewardship L
- Oil and gas sales and impacts

Materiality significance (see page 53)

Key:
- H High
- M Medium
- L Low

Business Relationships

Material issue 1 of 7: **Economics and Funding**

Success in this area directly contributes to deliver against the following

Strategic Objectives

Shown in **bold**

Delivering exploration and appraisal success

Portfolio management

Deliver operational excellence

Maintain licence to operate

Deliver a sustainable business

4 Read more: Business Model and Strategy on P4-5

These issues have the potential to impact our mitigation of these

Principal Risks

Shown below

Operational and project performance

Delay in Catcher and Kraken production start-up schedule

Securing new venture opportunities

Sustained low oil and gas price

Access to internal or external funding

Political and fiscal uncertainties

41 Read more: Risk Management on P41-47

Our 2017 plans to manage this material issue are set out in these 2017

CR Objectives

Strengthen link between CRMS and business risk management

Improve CR risk register

Annual CRMS audit

Enhance CR content of Investment Proposals and support new ventures

Maintaining CR standards

The sustained low oil price continues to be one of our principal risks. This means that the business remains focused on delivering opportunities to cut costs across operations. However, in pursuing cost reductions in this environment we do not compromise our commitment to working responsibly.

In Senegal we identified and implemented initiatives during the year to reduce our operational cost. These included extensive assessment of rig and other contractors to achieve the most cost-effective solution for further exploration and appraisal of our Senegal blocks. However, before commercial bids were assessed, CR and technical requirements had to be fulfilled. Our joint venture partners in the North Sea, EnQuest and Premier Oil, were also diligent in delivering cost reductions on our Kraken and Catcher projects by taking advantage of improved contractor market conditions all the while maintaining a focus on safe delivery and working responsibly. We monitor this through formal joint venture meetings and special working groups, promoting our business principles and sharing lessons learned.

In September we opened a new supply base in Dakar to meet our operational needs in Senegal. This supply base, which is developed to a UK regulatory standard, could have been completed at a lesser cost but at the expense of meeting the standards we set for ourselves. Previously our supply base arrangements were focused around a number of storage yards and shared facilities with associated road hazards, access and handling issues. The new base not only reduces safety and environmental risks associated with our previous supply base arrangements, but will also improve equipment handling and save time, ultimately being cost-effective.

28 Read more: Establishing a permanent facility, P28 Cairn in Senegal

Evaluating new opportunities

We continue to assess new venture opportunities within the context of our existing financial commitments to our key projects in Senegal and the North Sea and in a low oil price environment which means restricted funding is an issue for the oil and gas industry as a whole. Some opportunities may be financially attractive, but unacceptable due to associated ethical, safety or environmental concerns.

Working Responsibly continued
Our Corporate Responsibility Priorities continued

Business Relationships continued
Material issue 1 of 7: **Economics and Funding** continued

Evaluation process for new ventures
Through our CRMS we rigorously assess new venture opportunities. As part of the Cairn Operating Standards we develop Investment Proposals (IPs) which identify and evaluate the risks associated with the investment; these risks include any CR related concerns. All significant new venture projects require Board approval and are considered relative to the Group strategy and risk appetite. All IPs submitted in 2016 included appropriate assessment of CR considerations.

Using high standards to secure opportunity
Investors continue to scrutinise not only our financial position, but also our working responsibly practices and we continue to communicate how we achieve this and how we manage CR and the benefits of doing so. Our commitment to working responsibly, and our strong track record in this area, assists in retaining investment and securing opportunities when considering a new venture or licence application.

In 2016 we were awarded operatorship of one block and non-operated interests in additional blocks in Norway, which has stringent HSE regulatory requirements. We hold exploration interests in the Republic of Ireland where as an oil and gas operator we are required to meet the high environmental management standards of the Oslo/Paris Convention for the Protection of the Marine Environment of the North-East Atlantic (OSPAR) as a licence to operate prerequisite, and under which we retained our verification (to OSPAR recommendation 2003/5) in 2016.

In 2016 we were awarded operatorship of one block and non-operated interests in additional blocks in Norway, which has stringent HSE regulatory requirements.

Stena drillMAX drill ship contracted for Cairn's 2017 drilling campaign offshore Senegal.

Business Relationships continued

Material issue 2 of 7: **Contractors and Supply Chain**

Success in this area directly contributes to deliver against the following

Strategic Objectives

Shown in **bold**

Deliver exploration and appraisal success

Portfolio management

Deliver operational excellence

Maintain licence to operate

Deliver a sustainable business

4 Read more: Business Model and Strategy on P4-5

These issues have the potential to impact our mitigation of these

Principal Risks

Shown below

Health, safety, environment and security

Operational and project performance

41 Read more: Risk Management on P41-47

Our 2017 plans to manage this material issue are set out in these 2017

CR Objectives

Run contractor workshops in Senegal with themes including Life-Saving Rules and MSA

Support other programmes planned across the Group

Our business is highly reliant on the use of specialist contractors and suppliers, typically not retained in house due to variation in demand and high cost, and as such they contribute to the delivery of our strategy. In 2016 61% of our workforce were contractor personnel amounting to 64% of hours worked. Good management of contractors and suppliers, and ensuring they meet our high standards of responsible working practices, is therefore critical in maintaining those standards. Where we can we seek to maximise local participation in the workforce and supply chain.

Wherever we operate we look to work with local companies as part of our commitment to delivering value for our stakeholders. This commitment to maximising local participation where possible is made without compromising our high standards of CR. Our recruitment policies seek to employ personnel local to our host countries where they are suitably qualified and we encourage our contractors to do the same. We also give preference to local suppliers through our contracting and procurement policies and procedures where they are able to meet our CR requirements. In addition, we are looking to build local capacity through partnership with local organisations and academic institutions (see also **Social and Economic Benefit**). Our stakeholders continue to take an interest in opportunities for local contracting services and we anticipate that this interest will grow in the coming years. We are pleased to be able to report, at these early stages of the Senegal project, that local personnel in Senegal represented 22% of our workforce.

Rigorous selection process

We continue to consider responsible working in the entire contracting lifecycle from selection and management of our contractors to applying lessons learned in new programmes. In 2016 we concluded the second phase of our exploration and appraisal programme in Senegal and planning commenced for the third phase. Our contractor selection process was reviewed at the end of phase two and lessons learned were applied by further embedding CR matters, including human rights issues (see also **Human Rights**), as pre-qualifying requirements for all key contractors. Based on IOGP good practice the phase three contractor assessment process consisted of initial review against key criteria and the issue of a CR questionnaire alongside invitations to tender (ITTs). Returned ITTs were assessed to determine whether our standards were met. Contractors which passed this assessment progressed to the next round and were subject to further follow-up including site visits to verify responses before further assessment and selection.

Working Responsibly continued
Our Corporate Responsibility Priorities continued

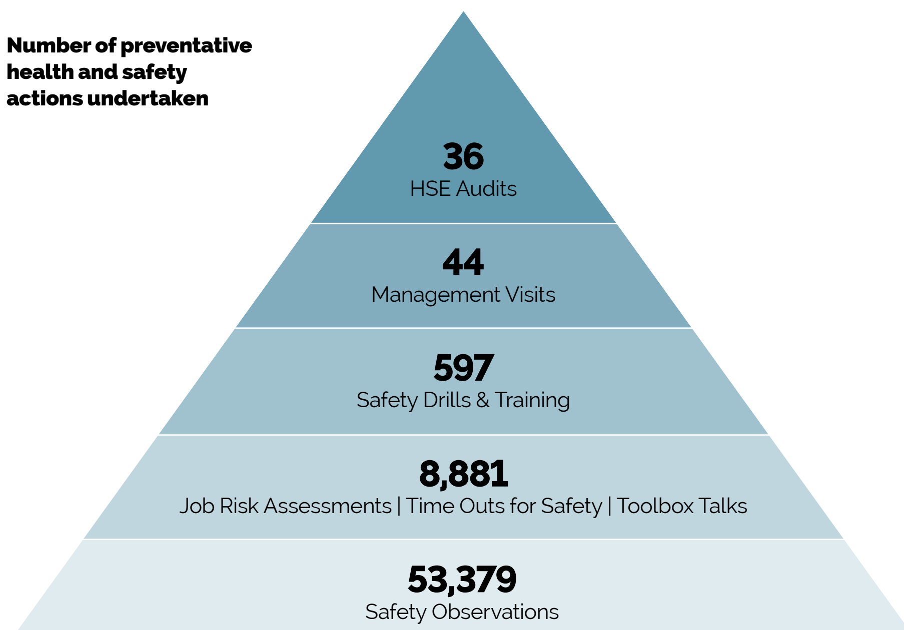
Business Relationships continued
Material issue 2 of 7: **Contractors and Supply Chain** continued

Effective management and control
We commissioned independent specialists to audit rigs, vessels and aviation before we contracted them for the phase three Senegal programme to ensure effective management was in place before operations commenced in January 2017. Some operational activities are managed directly by Cairn whereas others are the responsibility of the contractor, although the contractor remains accountable to Cairn at all times. For example rig contractors perform drilling activities under agreed procedures whereas Cairn retains assurance processes including, reporting, performance measures, audits and reviews. The allocation of duties and responsibilities is part of our Project Delivery Process and bridging arrangements. These are in place to ensure our CR management systems and those of our contractors remain effective and clarify which party maintains primacy over an activity.

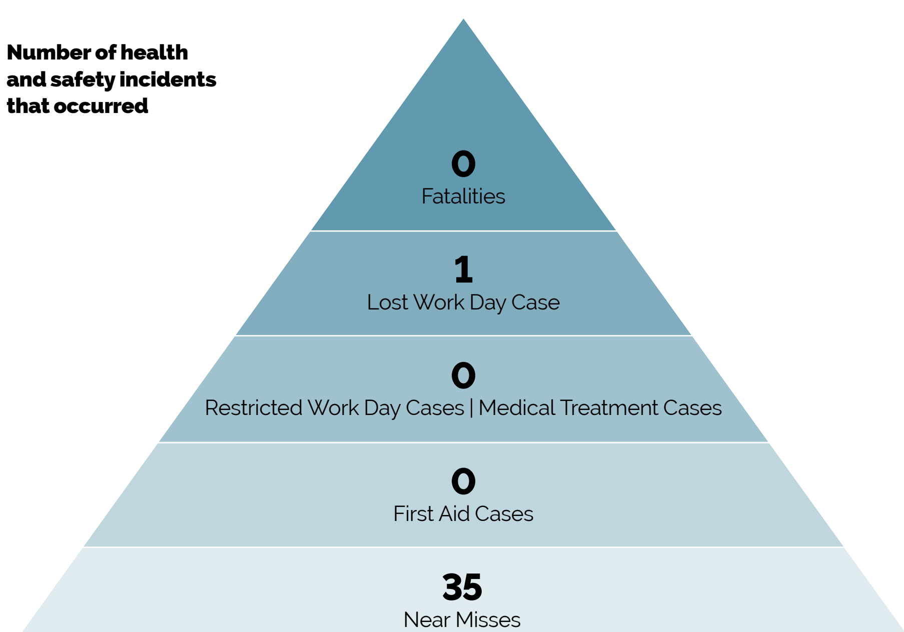
We continue to encourage our contractors where performance can be improved including proactive engagement and follow-up of incidents and issues. This included a comprehensive review of accident and emergency incidents during the construction of the Catcher and Kraken FPSO units. Findings from this review were shared with the Board, which allowed lessons to be learned and shared across the Group.

Health and safety triangles, Senegal operations October 2015 – June 2016

Number of preventative health and safety actions undertaken



Number of health and safety incidents that occurred



Business Relationships continued

Material issue 3 of 7: **Ethics, Anti-bribery and Corruption and Transparency**

Success in this area directly contributes to deliver against the following

Strategic Objectives

Shown in **bold**

- Deliver exploration and appraisal success
- Portfolio management
- Deliver operational excellence
- **Maintain licence to operate**
- Deliver a sustainable business

Read more: Business Model and Strategy on P4-5

These issues have the potential to impact our mitigation of these

Principal Risks

Shown below

- Stakeholder reaction to operations
- Fraud, bribery and corruption

Read more: Risk Management on P41-47

Our 2017 plans to manage this material issue are set out in these 2017

CR Objectives

- Continue to improve our Code of Business Ethics and Business Principles
- Enhance the gifts and hospitality register
- ABC training targeted at high risk areas

Our ability to do business relies on developing trust with our stakeholders including investors, governments, business partners, suppliers and broader society. This means we work in an ethical and transparent way and take a zero-tolerance approach to bribery and corruption. We are committed to ensure that those who work for us or on our behalf do not, in any way, offer to give or receive bribes. Moreover this commitment extends to being transparent in all our payments. We are also obliged under UK legislation to implement anti-bribery and corruption (ABC) mechanisms. This approach is defined in our values and business principles to which we hold ourselves accountable, and within the procedures we adopt and the people who work on our behalf as described on pages 10 and 11 (**Our Culture**).

Read more: Our Culture on P10-11

Code of Business Ethics

We have a Group Code of Business Ethics (the Code), which describes our standards of business ethics and conduct expected of everyone who carries out work for us on our behalf, including contractors. The Code is regularly updated along with our Business Principles, which identify the behaviours we expect from our personnel. These were both updated at the end of 2016 and reissued. Application of the Code throughout the business is ensured by the highest level of management, the Board. The Board's Audit Committee is responsible for appointing an internal auditor to regularly conduct internal audits of Cairn's compliance with the Code. All levels of management at Cairn, including executive and non-executive directors, regional directors, general managers and heads of departments, are responsible for ensuring consistent application of the Code. All personnel must abide by the Code and promote its use in all business activities. All employees are required to sign up to the Code as part of their employment conditions.

Simon Thomson, Chief Executive, and Ian Tyler, Chairman, on board Ocean Rig Athena drill ship used during Cairn's 2015/2016 Senegal drilling campaign.

Working Responsibly continued
Our Corporate Responsibility Priorities continued

Business Relationships continued
Material issue 3 of 7: **Ethics, Anti-bribery and Corruption and Transparency** continued

The Code includes our commitments to:
- Legal and regulatory compliance;
- A zero-tolerance approach to bribery and corruption;
- Respect human rights;
- Not make contributions to political parties, organisations or individuals engaged in politics or political lobbying, as a way of obtaining advantage in business;
- Provide a workplace free from discrimination and harassment; and
- Financial integrity and reporting.

Through our whistleblowing procedure, employees are encouraged to report any incident they believe may compromise our Code of Business Ethics.

Read more information at www.cairnenergy.com/responsibility

Measuring performance

0

Incidents of non-compliance with the Code

0

Employee dismissals for non-compliance with the Code

Anti-bribery and corruption

As part of our ongoing commitment to establishing a culture of zero tolerance to bribery and corruption, in 2016 we required all personnel, including contractors, to complete a bespoke e-learning module to ensure their continued understanding and application of our anti-bribery and corruption policies and procedures.

Read more information at www.cairnenergy.com/responsibility/ABC Management System

Measuring performance

90.6%

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

Monitoring and responding to ethical Issues

Throughout the year we tracked emerging ethical issues of importance to our business and the industry by monitoring: emerging legislation; guidance and agreements; press commentary; stakeholder enquiries; and through focused stakeholder engagement.

In 2016 we reviewed our potential contribution towards the UN Sustainable Development Goals (see **Sharing benefits in Senegal** p30), our readiness to report against The Modern Slavery Act 2015 (see **Human Rights** p64) and the implications of the COP21 Climate Change agreement (see **Climate Change, Emissions and Discharges** p69).

Western Sahara

In 2016 a key focus of stakeholder enquiries and activity was our involvement in Western Sahara, although in 2016 we had no active operations in the region. We hold a 20% non-operated interest in the Boujdour Maritime contract area offshore Western Sahara with a commitment for 3D seismic to be acquired by 2020 which will be conducted by the operating partner, Kosmos Energy.

In June 2016, the Norway Government Global Pension Fund announced its decision to exclude both Cairn and Kosmos Energy from their fund. The decision on exclusion was made on the basis of the recommendation of the Council on Ethics. In October 2016, BMO Global Asset Management (an investment fund management organisation) decided, on the basis of the same report, to exclude Cairn from the investible universe of BMO's Responsible Fund range.

Western Sahara has been classified since 1961 as a 'Non-Self-Governing Territory', by the United Nations. Both Morocco and the Saharawi Arab Democratic Republic claim Western Sahara as their sovereign territory. Cairn believes that hydrocarbon exploration offshore of the territory is consistent with international law. Resolution of the territorial status is not required for exploration as the UN 2002 Legal Opinion views Morocco as the territory's administering authority and as such it can issue permits for resource development. The UN continues to mediate a process to resolve the dispute between Morocco and the Saharawi Arab Democratic Republic. In 2013, Morocco's Economic, Social and Environmental Council, an independent constitutional body, launched

Ocean Rig Athena drill ship used during Cairn's 2015/2016 Senegal drilling campaign.

In 2016 we required all personnel, including contractors, to complete a bespoke e-learning module to ensure their continued understanding and application of our anti-bribery and corruption policies and procedures.

intensive consultations in the region on how to properly manage the development of the region. Initial oil and gas industry activities in the area are focused solely on exploration and do not involve the removal of resources. The region remains economically underdeveloped. Cairn believes that the exploration for hydrocarbon resources will enhance economic development prospects for all people of the territory, with the possibility of greater private sector investment and job creation.

Responsible resource development can proceed in parallel with the UN-led discussions on the region's future and the 2002 UN Legal Opinion provides for resource development to co-exist with the political process, as long as any such resource development is conducted for the benefit of the people of the territory.

The Joint Declaration of Principles signed by Kosmos Energy and the Government of Morocco states that local populations will benefit efficiently, effectively and transparently from production of hydrocarbons if commercially viable reserves are discovered.

Read more information at
www.cairnenergy.com/responsibility

Transparency

Cairn is committed to being open and transparent in all aspects of its business and this includes in its communications with stakeholders and in its reporting.

Communicating with shareholders

Shareholders are important stakeholders, and they are key to our funding position, consequently we invest significant resource in effective shareholder communications. We respond promptly to correspondence from shareholders and our website **www.cairnenergy.com** includes a dedicated investor relations section.

In order to ensure that the Board maintains an up-to-date understanding of the views of major shareholders, there is a focused and structured programme of regular shareholder dialogue. The Board is kept informed of any issues raised by shareholders through Board papers where shareholder concern is a standing agenda item, through feedback at pre-Board meetings and following significant announcements. In addition, we maintain an investor relations database, which details all meetings between Cairn and its investors.

Transparent reporting

We are committed to responsible and transparent reporting and have been recognised for the quality of our work in this area, being nominated in 2014 and 2015 by the Investor Relations Society in the Best Annual Report category among FTSE 250 companies and in 2015 shortlisted for Best Audit and Risk disclosure in the FTSE 250 at the Institute of Chartered Secretaries and Administrator (CSA) Excellence in Governance Awards. In 2016, our 2015 Annual Report was highly commended in the PwC Building Trust in Corporate Report Awards for 'excellence in reporting in the FTSE 250'. We apply global standards to ensure our reporting is of the highest quality. We use the Global Reporting Initiative[1] Sustainability Reporting Standards at a 'Core' level. We follow the content principles of materiality, stakeholder inclusiveness, sustainability context and completeness; and its quality principles of balance, comparability, accuracy, timeliness, clarity and reliability. See our **Responsibility** webpages.

We received a series of questions from FRC in response to the ClientEarth complaint in late 2016 alleging we had failed to adequately disclose climate change risks to our investors along with routine questions in other areas. We responded in full to all FRC questions in January 2017.

In terms of transparency on climate change risk in 2015 we judged the risk to Cairn business as 'medium' based on exposures across the portfolio. This included consideration of the absence of production, fully funded nature of non-operated developments and economic and social benefit to our countries of operation such as Senegal, in combination with the status of external developments on climate change.

We also acknowledged the rising importance of climate change to some of our stakeholders as 'significant' and rising given the outcome of COP21. Our position was ground-truthed with a cohort of stakeholders, as reported in 2015, and the overall assessment of climate change in terms of CR materiality was rated as 'medium' based on our assessment criteria. Consequently, we believe that at the close of 2015 the potential impact of climate change on the Company was fairly considered and appropriately represented in our 2015 Annual Report.

We normally report on climate change in the working responsibly section of our Annual Report and on our website www.cairnenergy.com/responsibility. This year is no exception and assessment of risk and CR materiality in 2016 is reported in the section on **Climate Change, Emissions and Discharges** on page 69.

Payments to governments

Cairn supports transparency around how revenues from the natural resources extractive industry are used and the transparency of tax contributions and other payments to governments by oil and gas companies. Cairn reports payments to governments annually, which are published in its Annual Reports, in compliance with EU legislation and as part of its voluntary commitment to the Extractive Industries Transparency Initiative (EITI). The EITI is a voluntary international initiative which governments commit to. It requires companies to publish what they pay to governments, and governments to publish what they receive from companies. We became a participating company of the EITI in September 2013.

As a listed company operating within the European Union, the EU Accounting Directive applies to Cairn and requires companies to disclose certain payments to governments on a country-by-country basis. Our initial report in this area was issued in July 2016.

1 GRI is an international independent organisation that helps businesses, governments and other organisations understand and communicate the impact of business on critical sustainability issues such as climate change, human rights, corruption and many others.

Working Responsibly continued
Our Corporate Responsibility Priorities continued

Society and Communities
Material issue 4 of 7: **Social & Economic Benefit**

Success in this area directly contributes to deliver against the following

Strategic Objectives

Shown in **bold**

- Delivering exploration and appraisal success
- Portfolio management
- Deliver operational excellence
- **Maintain licence to operate**
- Deliver a sustainable business

4 Read more: Business Model and Strategy on P4-5

These issues have the potential to impact our mitigation of these

Principal Risks

Shown below

- Stakeholder reaction to operations

41 Read more: Risk Management on P41-47

Our 2017 plans to manage this material issue are set out in these 2017

CR Objectives

- Continue to develop our impact benefit plan in Senegal
- Standardise our approach to impact benefit planning across the group and linkage to UN SDG's

Delivering social and economic benefit

Our strategy is to deliver value for our stakeholders through the oil and gas life cycle. This means generating social and economic benefit through our presence in any given area. Our stakeholders are a broad group and there are many ways in which we can deliver value for them, both economic and non-economic. Our key stakeholders associated with a project include host governments which grant our oil and gas licences and regulate our activities, communities affected by our operations and those who work on our behalf including personnel and contractors.

The economic contributions which can be associated with our activities include the following:

- Affordable energy and revenue for local populations through the discovery, appraisal and delivery of oil and gas to meet energy demands
- Distribution of operating expenditure through exploration and appraisal phases of a project and through payments to our contractors and suppliers including locally and internationally based companies
- De-risking state oil company investments by paying all exploration costs on behalf of state oil companies who are only required to invest if and when a commercial discovery is confirmed
- Payments to our workforce, including local employees
- Payments to government which may include licence fees, taxes, duties and training allowances
- Investment in local institutional and community development

In addition we make non-economic contributions which can lead to local benefits and include:

- Capacity building amongst our contractors and suppliers, in particular amongst local companies or individuals to help them meet the technical, HSE and CR standards required to work with us
- Training and development of our local workforce
- Sharing of knowledge (e.g. environmental, geological) with national and local bodies for the benefit of local communities and national authorities
- Capacity building within government institutions to develop understanding and knowledge of the oil and gas industry
- Upholding high standards of governance, ethics and anti-corruption through, for example, our commitment to the UN Global Compact and the Extractive Industries Transparency Initiative (EITI).

Read more information at www.cairnenergy.com/responsibility

In 2015, world leaders committed to the UN Sustainable Development Goals (SDGs) which set out 17 prioritised areas including ending poverty, ensuring access to energy, protection of ecosystems, addressing climate change and responsible working practices. We recognise a responsibility to look at our activities to identify both where our business adds value for society and where we may need to mitigate for potential negative impacts across environmental, social and governance related issues. In June 2016, we commissioned a review based on the SDGs to identify where our activities could impact on or support any of these goals. This helped to inform our approach to delivering benefits for our stakeholders in Senegal. See Sharing Benefits in Senegal on page 30.

Our stakeholders are a broad group and there are many ways in which we can deliver value for them.

During 2016, we continued to support social investment programmes, which are part of the Impact Benefit Plan for Senegal. Those programmes included:

- Promoting understanding and awareness of the oil and gas industry to Senegalese institutions through awareness seminars, English language training and support to national emergency planning
- Developing English language skills and awareness of the oil and gas industry among students of the University of Dakar
- Developing entrepreneurship in young people through sponsorship of the Great Entrepreneur Competition, an initiative of the British Council in Dakar
- Supporting a previous winner of the Great Entrepreneur Competition to establish a plastics recycling business through provision of equipment and mentoring
- Supporting a women-led microfinance project in rural communities by partnering with an international NGO called The Hunger Project.

More information about our Social Investment Programme is available at **www.cairnenergy.com/responsibility**

Contractors & Suppliers	Workforce	Communities	Government	Shareholders
Economic Contributions 2016				
Capital Spend US$428.4 million [1]	Staff Costs US$38.6 million [2]	Social Investment US$137,839	Payments to Government US$25.7 million [3]	Value Growth
Non-economic Contributions 2016				
Capacity Building 25 trained	Training and Development 36 average hours /employee	Knowledge Sharing	Capacity Building 162 trained EITI Support	

Notes:
1 Net share across the Group.
2 Excludes share-based payment charges which are non-cash.
3 Refunds from governments, in 2016, were US$40.4 million.

Working Responsibly continued
Our Corporate Responsibility Priorities continued

Society and Communities continued
Material issue 5 of 7: Human Rights

Success in this area directly contributes to deliver against the following
Strategic Objectives
Shown in **bold**

- Deliver exploration and appraisal success
- Portfolio management
- Deliver operational excellence
- **Maintain licence to operate**
- Deliver a sustainable business

4 Read more: Business Model and Strategy on P4-5

These issues have the potential to impact our mitigation of these
Principal Risks
Shown below

- Stakeholder reaction to operations

41 Read more: Risk Management on P41-47

Our 2017 plans to manage this material issue are set out in these 2017
CR Objectives

- Further develop MSA safeguards
- Deliver MSA training
- Develop MSA statement for 2017

Respecting human rights is part of our commitment to delivering value for all stakeholders. We are committed to respecting human rights in all our activities and this commitment is embedded in our Business Principles and includes our support for the United Nations' Universal Declaration of Human Rights. Human rights are particularly important to certain of our key stakeholders including our employees and communities in which we operate.

Our rights aware approach
In order to ensure respect for human rights in all our activities we have a human rights policy which is integrated within our Corporate Social Responsibility (CSR) Policy. It requires us to respect and support internationally recognised human rights standards; identify, assess and manage human rights risks, and; ensure that appropriate mechanisms are in place for those affected by our operations to raise and address grievances.

Our Corporate Responsibility Standard Operating Procedures and Human Rights Guidelines clarify what needs to be done, and the tools available to support implementation of our human rights policy across the business.

Over the years we have implemented a 'rights aware approach' which means identifying potential human rights issues in our activities, assessing if we have influence over the issues and defining appropriate action to be taken by the business.

Before entering a new country as an operator we apply human rights screening as part of our comprehensive due diligence process. Before operating activities we assess human rights impacts as part of an Environmental and Social Impact Assessment (ESIA) or where necessary, we undertake a Human Rights Impact Assessment (HRIA). If, following these assessments, any potential human rights issues are identified we consider the most effective way to manage them through engagement with potentially affected communities. When considering a non-operated joint venture, we identify and check any human rights issues and establish any risks requiring management by the operator before proceeding.

Respect for our employees
We believe that by promoting a work environment in which people are treated with dignity and respect, we can maintain a loyal, motivated and effective workforce. This includes ensuring fair and just rewards for employees' contributions and supporting opportunities for professional development (see **Human Resources** page 72).

We also have policies in place covering recruitment, grievance, harassment and equal opportunities, which seek to ensure that all current and potential employees are treated fairly. We expect our contractors to treat their employees in the same way.

We respect the rights of freedom of association and collective bargaining. Although we do not have any employees who are unionised or have any collective agreements in place, we do consult our workforce on organisational issues on a regular basis and through a variety of means. We respect those contract employees who work with us and their membership of unions which we consider during our contracting activities (see **Our culture** on page 10).

In 2016 we undertook a revision of our People Management Policies and Procedures and we aim to roll out the updated requirements in 2017. (See also **Human Resources** page 72).

Employees or contractors can raise any concerns they might have around human rights, and indeed any other issues, through a variety of means including the Company's whistle-blowing procedure.

Respect for communities
A fundamental respect for human rights is critical to maintaining good working relationships with the local communities with which we interact. Our CRMS sets out our approach to managing potential community impacts in accordance with the International Finance Corporation's (IFC) Performance Standard 5[1], requiring the development of action plans in cases where activities could lead to economic or physical displacement.

Our operated and non-operated assets are principally based offshore. As such, the potential for our activities to impact negatively on the human rights of local communities is limited. In 2016, our operated drilling operations were carried out offshore Senegal, with relatively limited onshore support operations in established ports. No physical displacement of individuals, or any identified economic displacement of individuals or communities resulted from our operations.

1 IFC Environmental and Social Performance Standard 5 – Land Acquisition and Involuntary Resettlement. January 1, 2012.

Team at Cairn supply base in Dakar port.

However, we recognised the potential for our activities to limit the ability of local fishermen to exploit the waters in which we work. We worked with local fishermen to minimise disruption through communication of our day-to-day and forward operations and implemented a mechanism whereby they were able to provide us with feedback. In addition, and as part of the development of our Impact Benefit Plan in Senegal (see **Social and Economic Benefit** page 62), we continue to work with an international NGO in Senegal to engage with and identify specific challenges facing fishermen along the coastal areas closest to our operations.

Grievances
Occasionally, during the lifetime of a project, unforeseeable human rights or other stakeholder issues can arise. We provide and promote a 'grievance procedure' by which individuals or representatives of communities affected by our operations can present their grievances and to which we aim to respond within 30 days.

Employees or contractors can also raise any concerns they might have around human rights, and indeed any other issues, through a variety of means including the Company's whistleblowing procedure.

In 2016, there were no reported grievances or breaches reported through the whistle-blowing procedure.

Modern Slavery Act 2015
In 2016 the Modern Slavery Act came into force in the UK. This Act requires companies with turnover greater than £36 million to produce a statement of their assessment and management of their supply chain in respect of forced, compulsory, bonded and child labour or any form of human trafficking. Although Cairn was not required, under the Act's turnover qualification level, to produce a statement in 2016, preparations commenced to better understand the objectives and implications of the Act. We analysed our current Corporate Social Responsibility policy and procedures against the requirements of the Act to identify any discrepancies. Although we do not foresee any major risks in this area it has been discussed by the board and our CSR policy adjusted **www.cairnenergy.com/responsibility**
We have also started work to better assess any vulnerable areas within our supply chain and will implement any required improvements in 2017.

Measuring performance

0

Total human rights grievances and incidents of discrimination

More information about our Approach to protecting Human Rights is available at **www.cairnenergy.com/responsibility**

Working Responsibly continued
Our Corporate Responsibility Priorities continued

People
Material issue 6 of 7: **Major Accident Prevention and Safety**

Success in this area directly contributes to deliver against the following
Strategic Objectives
Shown in **bold**

- Delivering exploration and appraisal success
- Portfolio management
- Deliver operational excellence
- **Maintain licence to operate**
- Deliver a sustainable business

4 Read more: Business Model and Strategy on P4-5

These issues have the potential to impact our mitigation of these
Principal Risks
Shown below

- Health, safety, environment and security

41 Read more: Risk Management on P41-47

Our 2017 plans to manage this material issue are set out in these 2017
CR Objectives

- Implement safety campaigns on Life-Saving Rules
- Further train our crisis and emergency personnel, improve plans and perform exercises

Prevention
Preventing major accidents and ensuring that our assets are fit to carry out their intended purpose, in this case preventing escape of fluids or other hazardous substances from wells and equipment, remains a material issue industry wide. We ensure effective engineering control barriers are in place and maintain our capability to respond in the event of a major accident or emergency. As in previous years our focus remains on major accident risk avoidance and prevention, a key part of which includes the assurance of well design and contractor competence. The assurance process is detailed in our Operating Standards and in the Project Delivery Process.

Project Delivery Process
Our Project Delivery Process (PDP) is the well-established method by which we can ensure we understand and can control risks at key stages in our projects. During the oil and gas life cycle the PDP helps us maintain focus on what is important to the Company and apply good practice through the application of local and international standards.

We use the Cairn PDP to manage CR issues and apply these standards for all operated projects under our control. Specific project types (e.g. seismic, drilling) must meet defined criteria at designated 'stage gates'.

Each stage gate has defined actions and deliverables, which must be available and signed off by a 'gatekeeper' who is independent of the project. In this way, project integrity and performance are reviewed throughout the process and, where they deviate from standards, corrective actions are identified and implemented.

Emergency and oil spill response preparedness
Cairn continues to maintain emergency and oil spill response preparedness over a wide range of scenarios which could occur. Oil spill in particular remains a high-profile stakeholder concern, and we remain committed to applying the IPIECA-IOGP Joint Industry Practice[1] which continued to issue good practice guides in 2016. These are described in our Annual Report and Accounts 2015 on page 56 and the Oil Spill Resources website **http://www.oilspillresponseproject.org/**. This initiative is recognised across the industry as the most effective and up-to-date response guidance on oil spill.

1 The IPIECA-IOGP Oil Spill Response JIP (OSR-JIP) was set up to implement learning opportunities in respect of oil spill preparedness and response following the April 2010 well control incident in the Gulf of Mexico. As part of this effort, the OSR-JIP has produced more than 20 good practice guides. IPIECA is the global oil and gas industry association for environmental and social issues.

Project Delivery Process

Why	How	Ready	Finished	Learn
Identify	**Assess**	**Define**	**Execute**	**Evaluate**
Why are we doing this project?	**How** could we do this project?	Are we **ready** to sanction the work?	Have we **finished** all we needed to do?	What do we **learn** and achieve?

Our focus remains on major accident risk avoidance and prevention.

Changes to response capability
In 2016 we completed the second phase of our exploration and appraisal drilling programme in Senegal and commenced planning for the third phase. With a change in contracting arrangements for rigs, vessels and aviation, we required revision of our emergency response arrangements. This included increasing local capability in our Dakar office by improving the management of our Senegal Incident Management Team (IMT) and also improving the management of our Edinburgh-based Crisis and Emergency Response Team (CERT). We revised our Senegal Emergency Response and Oil Spill Contingency Plans and also made revisions to a number of documents previously submitted to Senegal regulators including: Environmental and Social Impact Assessment; hazard study; hazardous installation document; and, emergency plan description. In the Dakar office we have an Emergency Co-ordination Centre from which the IMT operates; this centre was refitted to improve communications, including communication with our new supply base in Dakar and head office in Edinburgh, and improved communications technology.

Measuring performance

4 spills

totalling

167 litres

Oil/fuel spills in 2016

We continued to run CERT and IMT exercises for various emergency scenarios during the year increasing the range of potential situations to which our personnel may be exposed. Prior to commencing the third phase of our activities in Senegal the IMT personnel were given role specific training, including desk-top training and a scenario-based exercise involving the drilling rig and the CERT. Our supply base personnel and our vessel and helicopter crews were also given specialist training for oil spill management purposes.

Engaging with partners
We continued to work closely with our joint venture partners, in a non-operator capacity, on our Kraken and Catcher North Sea development projects and progressing them towards first oil and cash flow in 2017. This included working closely with the operators of both projects on the development of their Safety Cases. These document and demonstrate that safety and environmental critical risks of any installation (production platform or rig) have been reduced to As Low As Reasonably Practicable (ALARP). All fixed and mobile installations in the North Sea must hold a Safety Case, a requirement of the 2015 UK Offshore Installation (Offshore Safety Directive) (Safety Case) Regulations, which came into force following the implementation of the EU Offshore Safety Directive in 2015.

UK authorities required our partners in Kraken to submit a Safety Case. As a prudent partner we supported and reviewed the development of the Safety Case information and document to assure ourselves, of progress and completion, and also to identify lessons learned. Lessons learned from the process were shared with our partners for development of the Safety Case for the Catcher development. Such lessons learned will also prove helpful should an FPSO be the solution of choice, subject to Senegalese legislation, for a development scenario in Senegal.

We continued to progress development of the management systems for our other operated and non-operated activities in the UK and Norway with ongoing dialogue with Norwegian regulators who require that non-operators assure themselves of the adequacy of their partners' operating standards.

On board the Ocean Rig Athena drill ship used during Cairn's 2015/2016 Senegal drilling campaign.

Working Responsibly continued
Our Corporate Responsibility Priorities continued

People continued
Material issue 6 of 7: **Major Accident Prevention and Safety** continued

Occupational safety
Management of occupational safety, which refers to the management of day-to-day safety hazards, uses a number of mechanisms to promote the implementation and effectiveness of working procedures. This includes management visits, audits, permit to work, toolbox talks, safety drills and training which are monitored through our leading safety indicators.

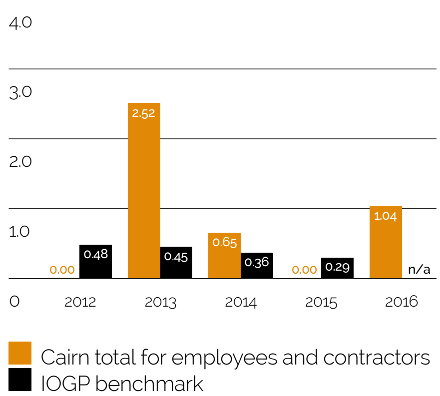
The lagging data below shows we experienced a Lost Time Injury[1] in which a member of our Senegal supply base contract crew suffered damage to three fingers as a result of entrapment during pipe handling in April. A thorough investigation was completed and findings were discussed by the Board in May alongside incidents suffered in non-operated assets and in the industry as a whole. Our new supply base operations have been designed to reduce occupational safety risks (e.g. lifting) based on industry good practice and lessons learnt from our operations at our previous supply base. (see **Establishing a permanent facility** on page 28). As part of this revision we placed emphasis on application of the IOGP Life-Saving Rules and in 2017 intend to hold focused sessions on application and auditing.

See also **Our culture** on pages 10 and 11.

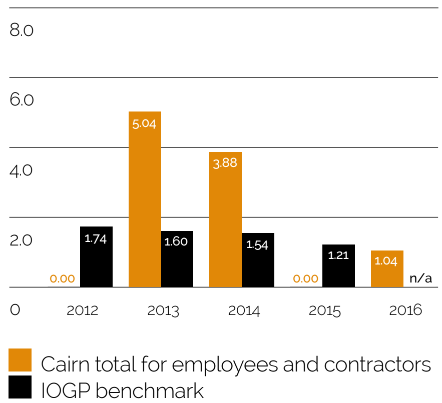
Our web pages discuss Health and Well-Being; Security; Equality & Diversity, and Employees
www.cairnenergy.com/responsibility

1 A fatal injury or any work related injury, which results in a person being unfit for work on any day after the day of occurrence of the occupational injury. 'Any day' includes rest days, weekend days, leave days, public holidays, or days after ceasing employment (IOGP).

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



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



Notes:
IOGP is the International Association of Oil and Gas Producers. We have included overall IOGP benchmark figures (average of onshore and offshore for employees and contractors). IOGP benchmark figures are not yet available for 2016.

Cairn TRIR and LTIF statistics can be higher than the IOGP 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 on-going production and other long term operations.

Environment

Material issue 7 of 7: **Climate Change, Emissions and Discharges**

Success in this area directly contributes to deliver against the following

Strategic Objectives

Shown in **bold**

- Delivering exploration and appraisal success
- Portfolio management
- Deliver operational excellence
- **Maintain licence to operate**
- Deliver a sustainable business

4 Read more: **Business Model and Strategy** on **P4-5**

These issues have the potential to impact our mitigation of these

Principal Risks

Shown below

- **Health, safety, environment and security**
- **Operational and project performance**

41 Read more: **Risk Management** on **P41-47**

Our 2017 plans to manage this material issue are set out in these 2017

CR Objectives

- **Provide baseline work and impact assessment for other blocks in our Senegal portfolio**
- **Support environmental work in other assets in support of applications and activities**
- **Continue to track risks arising from Climate Change treaties and legislation including COP21 and COP22**

Climate change review

Our industry as a whole recognises the potential risks as global energy transitions to a less carbon intense economy. This includes issues such as the potential for: future restriction of funding shareholder position and, stranded assets. We also recognise that balancing the need for energy and reducing GHG emissions will require efficient use of energy and the full utilisation of both conventional and innovative sources of energy into the foreseeable future, particularly if this is to remain affordable and accessible in developed and developing countries. Other global factors too remain important in relation to our industry including growing demand for energy and provision of energy security in individual countries.

The International Energy Agency (IEA) World Energy Outlook 2016 considers a number of transition scenarios to a low carbon economy, the most challenging of which (IEA 450) restricts global temperature rise to 1.5°C. In this instance nearly 60% of the power generated in 2040 is projected to come from renewables, almost half of this from wind and solar photovoltaics. Even in this scenario, IEA considers there to be 'no reason to assume widespread stranding of upstream oil assets, as long as governments give clear signals of their intent and pursue consistent policies to that end'. IEA goes on to indicate that 'Investment in developing new upstream projects is an important component of a least-cost transition, as the decline in output from existing fields is much larger than the anticipated fall in demand'.

One of our 2016 CR Objectives was to further examine the implications arising from the UN Intergovernmental Panel on Climate Change (IPCC) Conference of the Parties which took place in Paris at the end of 2015 as described in our 2015 Annual Report and Accounts. We have followed the progress of ratification during 2016 by major greenhouse gas emitting countries such as the USA and China, among others, and we recognise that climate change issues present potential risks to our future activities. In 2016 we conducted a review to better understand those potential risks.

This included a review of the Intended Nationally Determined Contribution (INDC)[1] reports for all locations in our portfolio. Potential strategic issues include emissions control restrictions (e.g. trading and permitting, levies), potential for stranded assets, securing access to finance, licence to operate and adaptation by countries and communities (e.g. due to rising sea levels, or change in environmental conditions affecting communities) to the impact from climate change. Our review was presented to the Board in September and actions for inclusion in our 2017 CR Objectives were identified. Climate change in the context of the oil and gas industry is further discussed in the **Industry Overview** section of this report (pages 12 and 13). Cairn continues to track risk in all locations in which we operate including climate change and believes that for the foreseeable future oil and gas will be important in the energy mix to meet demand and of particular benefit for wealth generation and delivery of affordable energy if managed in an ethical manner.

We acknowledge the rising importance of climate change to some of our stakeholders and, in 2016, we have assessed this as 'high' within our CR materiality assessment (see **Materiality matrix** page 53). This year, we have continued to judge the risk to the Cairn Business from climate change as 'medium' based on exposures across the portfolio, which cover mature basins and developing locations.

1 Countries across the globe adopted a historic international climate agreement at the UN Framework Convention on Climate Change (UNFCCC) Conference of the Parties (COP21) in Paris in December 2015. In anticipation of this moment, countries publicly outlined what post-2020 climate actions they intended to take under the new international agreement, known as their Intended Nationally Determined Contributions (INDCs). The climate actions communicated in these INDCs largely determine whether the world achieves the long-term goals of the Paris Agreement: to hold the increase in global average temperature to well below 2°C, to pursue efforts to limit the increase to 1.5°C, and to achieve net zero emissions in the second half of this century.

Working Responsibly continued
Our Corporate Responsibility Priorities continued

Environment continued
Material issue 7 of 7: **Climate Change, Emissions and Discharges** continued

Mature basins

In areas where the oil and gas industry is considered mature, such as the UK and Norway, there is clear legislation around climate change and the oil and gas industry including EU Emissions Trading Scheme Regulations[2] with ongoing emission reduction targets by individual countries and collectively by the EU. As such climate change risks pertaining to our assets in the UK and Norway, which include our non-operated development projects Kraken and Catcher, are well understood. Future exploration in the UK and Norway appears to be secure against the background of UK and Norwegian reduction commitments and cost of carbon (carbon allowances are allocated under trading schemes to restrict emissions, allowances can be traded at market rate). A short-term challenge is economic downturn and its impact on oil price with implications for the industry as a whole (see **Economics and Funding** pages 55 and 56). Ongoing monitoring of risk will be required as these mature locations seek to continue oil and gas activity and reduce emissions simultaneously while providing energy security in an affordable manner.

Access to funding is not seen as an issue in the short to medium term given government policies and known legislation and timescales for the sector, indeed our Kraken and Catcher non-operated developments remain fully funded. Short term the marginal cost of carbon is not seen as a significant issue, although it may play a part as assets age and production declines in the medium to long term, precipitating marginally earlier decisions to cease production. We do not foresee funding or carbon cost as impacting shareholder value overall in our mature area portfolio at the end of 2016.

The likelihood of stranded assets due to climate change in mature areas is not regarded as an issue in the short or medium term. There continues to be considerable promotion of exploration and production in mature areas due to the benefits, including economic and social, and recognition that the transition will take some decades. In the short to medium term, asset risks such as proximity to infrastructure and size of discovery outweigh most other risks to project viability and delivery of shareholder value. Longer-term climate change is also likely to drive innovation and improvement in equipment including during the design and selection stages of projects to remove and optimise emissions. For example, long-term innovation may take the form of low emissions technology and carbon capture. We do not use an internal cost of carbon on the basis that it is not material to our projects at this time but we continue to factor costs into our due diligence and investment proposal processes as necessary. It is an area we continue to monitor to ensure we understand trends and implications.

Given that much of the UK HSE related legislation is based on EU Regulations and Directives, including the area of climate change, the UK's exit from the EU following the 2016 referendum has also been identified as an event to monitor. This may impact not only climate change issues but other CR issues of interest, as the details of 'Brexit' become clearer.

Senegal and developing locations

Transition risks in developing locations are closely tied to the need for economic growth to provide local benefits such as employment and social and economic development. Such countries tend to have much lower aspirations in terms of carbon reduction and will be dependent on investment funds. Market based mechanisms also tend to play a less central role (e.g. projects under the Clean Development Mechanism of the Kyoto Protocol). Access to investment for companies is often linked to demonstrating a responsible position (in terms of both environmental and social performance e.g. under IFC guidance). Again in the short to medium term stranded assets are unlikely to be a significant issue in respect of climate change alone. There are likely to be more significant issues relating to cost of delivery of a project in remote or poor infrastructure areas affecting the overall value of the project.

At the end of 2016 our principal asset of this type is the Senegal appraisal and exploration project. The project is still relatively early in the value chain but has substantial potential both economically and socially for Senegal. Development and delivery will be less than 10 years and in the medium term the climate change risks relating to investment, stranded assets and carbon cost are considered low. This is due to the need for development and affordable reliable energy in Senegal linked to its status as a 'United Nations Least Developed Country'.

In 2016 we reviewed the potential risks, status under the Kyoto Protocol and the Intended National Determined Contributions (INDCs) submitted as part of COP21 in developing locations in which we have an interest such as Senegal. Senegal aims to generate income to improve infrastructure and deliver benefits to communities and society. The Senegal National Committee on Climate Change has identified priorities such as the energy sector describing mitigation and adaption aspects from a climate change perspective. Key actions identified are replacement of solid fuels, rural electrification, use of renewable energy sources and infrastructure improvement in particular. A successful oil and gas industry could assist in generating significant income, which could aid country development, provide affordable energy and inward investment in the medium term, and reduce reliance on solid fuels.

2 The EU Emissions Trading Scheme Regulations require regulated activities such as many offshore installations to restrict emissions of carbon (as carbon dioxide and methane emissions among others). This is achieved by allocation of allowances which must be maintained and surrendered in line with strict requirements of the regulations.

Physical risks

Physical risks include potential for extreme weather, sea level rise and water scarcity. The likelihood of impact on Cairn's business as with other companies is highly location and infrastructure specific. In terms of our infrastructure, as at the end of 2016 Cairn had no permanent installations; all our activities involved offshore mobile equipment.

Local people in our areas of activity may be adversely affected by sea-level rise or degradation in fishing quality/quantity, availability of water or farming. These are social issues which are essentially in the government domain; however, Cairn has a long history of both social responsibility and social investment. For example, water supply issues in India in the location of our land operations were the subject of a major aquifer management programme developed by Cairn.

Emissions, discharges and wastes

In March 2016 we completed the second phase of our exploration and appraisal programme in Senegal and commenced planning for the third phase which started in 2017. As such our operations in 2016 were relatively limited in terms of emissions, discharges and wastes. We expect emissions, discharges and wastes to be broadly similar to 2016 based on an anticipated programme of two firm wells in 2017. However, the third phase programme includes a number of optional wells, which, if executed, would increase our emissions, discharges and wastes. It remains difficult to set specific reduction targets when levels of activity vary from year to year, but we are committed to minimising our environmental impact from operations and to reporting fully and transparently on this matter.

GHGs form a part of our operational environmental footprint. We monitor and manage the GHGs emitted during our activities and disclose them in accordance with industry requirements and standards. In 2016, we conducted a review of the methods and factors used in the calculation of our GHG emissions, and adjustments were made in line with best practice. We disclose on an 'operational control' basis, which means we report emissions from those assets that are operated by us and not those controlled by our partners. With no operated production facilities in 2016, our direct GHG emissions occurred primarily from the combustion of fuel on the rig, vessels and aviation, and from flaring during well testing.

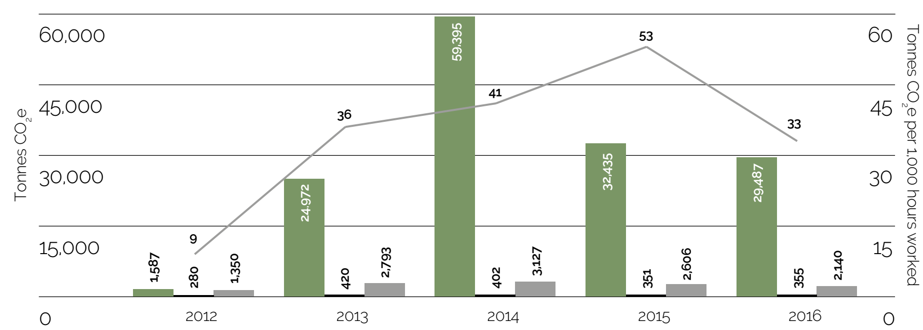
The graph Total and normalised GHG emissions (scopes 1, 2 and 3) indicates that our GHG emissions over the last five years are heavily dependent on the level of operational activity in any given year given the absence of any steady state production. This makes it difficult to identify baseline information and set meaningful targets for total GHG reduction over time. We have therefore chosen to adopt a methodology for calculating GHG emissions intensity with reference to the number of hours worked, as this provides a direct relationship with the levels of activity and provides a mechanism for engaging with our contractors on energy efficiency. The quantity of GHG emissions from our activities has reduced in 2016 from 2015 despite an increase in hours worked. Consequently, GHG intensity per thousand hours worked has improved substantially.

We experienced four minor spills of hydrocarbon in 2016, which arose for 'flare-out' incidents during well testing in the phase two drilling programme in Senegal. These arose as a consequence of ineffective rig orientation to the prevailing weather, seawater salting of the flare nozzle and setting the water deluge too high. These issues were addressed early in the campaign and no further problems occurred. A total of 167 litres we spilled to sea, however, the oil dispersed and evaporated rapidly and was considered to have a low environmental impact. All escapes were reported to the authorities.

At the end of the phase two exploration and appraisal campaign in Senegal, unanticipated residual wastes from the drill rig tanks required specific treatment as hazardous waste in accordance with EU classification. We achieved successful treatment by filter pressing and dry residues were packaged and sent ashore, prior to onward shipment to Spain under the Basel Convention due to the absence of suitable waste management sites in Senegal.

Biodiversity, product stewardship and resource use are discussed on our website **www.cairnenergy.com/responsibility**

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



Scope 1[1] tonnes CO_2e

Scope 2[2] (location-based) tonnes CO_2e

Scope 3[3] tonnes CO_2e

Scope 1, 2 (location-based) and 3 normalised tonnes CO_2e per 1,000 hours worked

We calculate our GHG emissions in accordance with the GHG Protocol Corporate Accounting and Reporting Standard.

1 For calculating Scope 1 (direct) GHG emissions we use emission factors from the API Compendium 2009 (fuel combustion), EEMS 2008 (flaring) and the GHG Protocol 2014 (waste incineration).
In 2016 we carried out a review of our Scope 1 GHG emissions calculations. As a result of this we updated to the latest published Global Warming Potentials (GWPs) for CO_2, CH_4 and N_2O from the Intergovernmental Panel on Climate Change (IPCC) Fifth Assessment Report (AR5). We also made minor changes to the emission factors we use from API 2009 by selecting ones that align more accurately to the fuel types we use, and introduced an additional two categories to our waste incineration data. We applied these changes across all of our Scope 1 GHG data, past and present, and so are restating all Scope 1 GHG figures in this report. In addition to this, we have updated our 2015 Scope 1 GHG emissions figure to incorporate flaring data that was not available when we produced our 2015 end of year reports. Our 2015 normalised GHG emissions have increased in line with this. N.B. 2015 flaring data was included in Cairn's 2016 'Half Year Corporate Responsibility Update' but has since been recalculated with amended gas densities and is restated in this report.

2 We report Scope 2 (purchased electricity) GHG emissions in line with GHG Protocol Scope 2 Guidance, i.e. in two ways: according to a location-based method and a market-based method. (Transmission and distribution losses are excluded.) For the location-based method we use emission factors from the IEA (International Energy Agency) Report 'CO_2 emissions from Fuel Combustion Highlights' (2013 Edition). These are grid average emission factors for each country. For district heating and cooling we use location-based emission factors from DEFRA 2015. For the market-based method we use emission factors, where available, in the following order of preference:
a. Supplier-specific emission factors – obtained from Cairn offices' electricity suppliers.
b. Residual mix emission factors – obtained from the RE-DISS II document 'European Residual Mixes 2014', last updated in June 2015.
c. Location-based emission factors. These are the same IEA and DEFRA emission factors that we use for calculating location-based emissions.
We have provided location-based Scope 2 figures in this report. Our market-based Scope 2 figures, and further details about our GHG emissions data and calculations, are available on our website.

3 For calculating Scope 3 (business travel) GHG emissions we use the DEFRA methodology, including its recommendation to include an uplift for the influence of radiative forcing in air travel emissions. We updated to DEFRA 2016 emission factors this year (see http://www.ukconversionfactorscarbonsmart.co.uk/).

4 Limited assurance of our 2016 GHG data (Scopes 1, 2 and 3 and normalised) has been provided independently by RPS which, within the scope of the limited assurance engagement, has found that the GHG emissions reported are materially correct and a fair representation of available information. A full assurance statement detailing the verification undertaken and its limitations is available on our website.

Human Resources

Helping people to deliver strategy

We remain committed to supporting and incentivising our people in their delivery of Group strategy, all the while ensuring that a culture of working responsibly is embedded in everything that they do in their pursuit of the Company's strategic objectives.

We do this by ensuring that we have the right people in place with the right competencies, that they have the right training and development opportunities and that the right systems and tools are at their disposal. We insist that our people exhibit the high performance behaviours which we have identified as part of our culture of working responsibly. In our pursuit of strategy we also need to make sure Cairn is an attractive place to work in order to retain talent and attract new talent, to ensure we are preforming to the best of our abilities.

Focused on leadership

We recognise that the actions and behaviours of senior leadership are key to our success. As such we focused on a number of initiatives during the year to strengthen the skills of people in senior leadership and management positions as well as continuing to work on succession planning.

Senior Leadership Team 360° feedback
At Cairn we have a Senior Leadership Team (SLT) which includes our Chief Executive, Chief Financial Officer, Chief Operating Officer, Director of Exploration and our Regional Directors ensuring that the key management get together at least six times a year to discuss delivery of strategy and provide leadership throughout the business. We understand that those on our SLT are role models for our company values (the 3Rs) and our High Performance Behaviours and that championing these, along with clear

The 3Rs

Building **Respect**

Nurturing **Relationships**

Acting **Responsibly**

10 Read more: **Our Culture** on **P10–11**

Diversity within the workforce

We are committed to equality and diversity and understand the importance of a diverse workforce in broadening our skill base, bringing different approaches, perspectives and ideas, challenging norms and encouraging creativity, all of which support the business in delivering its strategy.

and regular communication and clarity of strategy, remains fundamental in maintaining both a strong company culture and high level of employee engagement. The 3Rs stand for building respect, nurturing relationships and acting responsibly and our High Performance Behaviours are the behaviours we have identified as part of our commitment to working responsibly in a safe, secure, environmentally and socially responsible manner. As a means of achieving against their goal of being role models, specifically in listening and personal development, and showing commitment to acting upon feedback received from across the business, each member of the SLT participated in a 360° feedback exercise in 2016 which was facilitated by an external party.

The exercise aimed to identify strengths and development areas both for individual leaders and for the leadership team as a whole. Each member was required to solicit feedback from a range of internal stakeholders with whom they interact including their own line managers, their peers from across the Group, and those reporting to them. Feedback was then provided to each SLT member on a 1-1 basis, with individual action plans derived from this. The next step, which we are now focusing on, is to review the feedback holistically to understand both strengths and areas for development for the team as a whole and communicate the feedback to staff across the Group.

Management Bootcamp
Work continued on our Management Bootcamp throughout 2016 with the aim of further developing the management skills of all our managers in the business to best deliver results through people by providing practical 'how to' management tips and techniques. The Bootcamp is structured to be energising, inclusive, challenging and thought provoking. It considers the effect of behaviour on people and performance, the skills and tools needed to encourage the right behaviours and how these will impact positively on the performance of Cairn's teams and business deliverables. The programme consists of seven modules: recognition and feedback, coaching, building relationships, delegation and empowerment, developing teams, managing change and managing conflict. Delegates are also provided with a pre-course 1-1 coaching session to help set out their objectives for the course and to put the development into a personal context.

The feedback from those who have attended the course has been very positive.

"As the Management Bootcamp programme has been developed for Cairn based on feedback from managers within the business, the training sessions are targeted to cover areas relevant to our business right now and this is extremely beneficial following a period of significant change within the company. I like the short, modular in-house approach as this gives me an opportunity to take some time out of a busy schedule to focus on my professional development which will be of benefit to me, my team and the company."

Managing succession planning
As part of our annual succession planning review, the Board was presented with an updated Group Succession Plan in June. The review confirmed that we had made good progress in several of the development areas identified through the prior year's succession planning, with the Group talent pool enhanced during the year through a combination of external resourcing and internal promotions.

While we recognise that some succession risks exist, the review provided a crucial means of identifying where the key focus areas are and the resource, skills and capability gaps that need to be addressed to mitigate these risks.

Other positive outcomes of the review included:

- The new regional structure, as finalised in 2015, is working well.
- Staff retention remains strong, providing stability and consistency in the delivery of current and future projects.
- We have been able to benefit from quality, external talent available as a result of the challenges being faced by the industry as a whole, and this proved advantageous for us in building some in-house capacity where our internal resource pool had historically been low.
- Our Management Bootcamp programme will support the business in developing the future succession pipeline.

At year-end 2016:

48%
of Cairn staff were women

4%
of Cairn staff had a disability

10%
of Cairn staff worked part-time

43
average age at Cairn

100%
of employees that took parental leave returned to work

33%
of management roles were held by women

16
different nationalities were employed at Cairn

11%
1 member of the Board was a woman

Human Resources continued

Linking performance to strategy

We recognise the importance of linking the performance of our people to the delivery of strategy to ensure our people are aligned with our strategic objectives and incentivised to deliver them. Changes to our performance management process during the year included measuring High Performance Behaviours and linking them to remuneration, further strengthening our working responsibly culture.

Revisions to Discretionary Cash Bonus scheme
In April, the Company rolled out some enhancements to our Performance Management process and related Discretionary Cash Bonus scheme. The Company wanted to adopt a standardised approach, ensuring consistency in how performance is assessed and rewarded through the application of a common, open and transparent system for all staff, irrespective of location.

The proposed solution is a powerful combination of:

- Group KPIs, which set out the strategic objectives for the company as a whole
- Project performance objectives, recognising the importance of collaboration within a team, collective problem solving to meet an objective and project management skills to deliver these objectives in a timely manner
- Personal performance objectives, recognising individual achievement against objectives including the importance of demonstrating the right behaviours consistently and working to the Group's standards to achieve their objectives

We believe the revisions will:

- Develop more cohesive teams which are clear on their annual objectives, through the implementation of a team performance element
- Encourage, reward and emphasise the importance of project management, collaboration and teamwork
- Ensure that all staff have an element of their reward based on their own individual performance and merits, including their application of our High Performance Behaviours and People Management Accountabilities

Feedback so far from staff on the revisions has been positive.

Learning and development

Learning and development is a key, ongoing part of human resources activity and is clearly an important part of supporting our delivery of strategy. During the year we focused on two key learning and development initiatives. We held a technical conference focused on creating value for the business from exploration, a reflection of our Group strategy to deliver value for stakeholders by building and maintaining a balanced portfolio of exploration, development and production assets within the oil and gas lifecycle.

We also ran an e-learning training course on anti-bribery and corruption (ABC) which all of our staff were required to complete and pass. This ABC training course is part of ensuring our strategy to deliver value in a safe, secure, environmentally and socially responsible manner and was designed to further raise awareness and understanding of bribery and corruption. The training course covered all of the key issues relating to bribery and corruption, including the UK Bribery Act 2010.

Technical conference: "From Volumes to Value"
In addition to our suite of annual geological fieldtrips which included Utah, Ireland and one in the local Edinburgh area in 2016, the Company held a Technical Conference in September 2016, attended by our geoscience, engineering, commercial and new ventures functions from across our business. The conference was designed to ensure alignment in the way we work, with a particular focus on the methods of assessing value. Workshop sessions were organised utilising industry software aimed at identifying the 'value of information' – critical for optimising investment decisions in exploration, appraisal and development activities, such as seismic surveys, wells and appraisal programmes.

Mixed teams from across the business worked together to critically assess our areas of relative strength and weakness in each of five areas – New Ventures, Asset & Licence Management, E&A Decision Making, Value Creation and Data & Tools. The aim was to identify key actions in our drive to continually improve in all that we do and to explore ways to collaborate and share knowledge and techniques across

Cairn team at 2016 Geological Society Careers Day, Edinburgh.

the geoscience, engineering, commercial, exploration and new ventures functions. The results have been shared with the Management Team and Senior Leadership Team and are being incorporated in to our 2017 plans. The conference was hosted by Paul Mayland, Chief Operating Officer and Richard Heaton, Director of Exploration. It was attended by over 60 members of staff including our regional directors and staff based in our Stavanger and London offices.

Equipping our people with the right tools

As well as having the right people in place and ensuring they have access to the right training to perform to the best of their abilities, we need to have the right tools in place. In late 2015, management requested a review of the suitability of our current business systems with a view to moving to a single Group-wide business system. This was on the basis that multiple systems were in use across the Group which had the potential to create risks and process inefficiencies. By business system we mean the system used throughout the business to manage day-to-day functions.

At the end of 2015 a project commenced to formally define, document and review Cairn's Enterprise Resource Platform (ERP) requirements. Requirements were assessed against available platforms, future strategy and the risks and process inefficiencies we had already identified. At the end of that review, a decision was reached to move to a single, new ERP more suited to Cairn's current business. Work remains underway to design and build the new system with planned implementation during 2017.

Book Cliffs, Utah field trip.

External recognition of our people management

It is important to us to ensure we are managing people in the right way and in line with international standards. As such we are pleased to have external validation in the form of accreditation from the internationally recognised standard Investors in People (IIP).

Investors in People is a global standard for people management held by over 14,000 organisations in 75 countries. The standard defines what it takes to lead, support and manage people well for sustainable results. We are delighted to have been an accredited Investor in People since 2004, and in April, to have been reaccredited by an independent assessor from IIP Scotland. This accreditation identifies both what we are doing well and areas for improvement.

As part of the assessment our assessor met with a randomly selected 10% of employees from across the Group and we were delighted that following her review, our assessor found that she was "satisfied beyond any doubt that Cairn Energy PLC continues to meet the requirements of the Investors in People Standard".

The assessment found that there was a tremendous team spirit, a clear sense of company strategy and the Group KPIs with a focus on creating value, an understanding and appreciation of the new structure of the business into three defined geographical regions and a clear sense of staff willing to share knowledge and information with each other so that they can continuously improve.

Other key areas of best practice highlighted by the assessment included:

- Staff are very loyal to the Company and are committed to its future success. There is a sense of ownership and pride in working for the Company
- The Company is very clear on its future strategy and the business planning process is very sound
- The Company is very committed to the learning and development of its staff and the on-the-job training, including shadowing and informal coaching of staff, are of a high standard
- The Company's revised appraisal and informal feedback process is very solid
- Members of staff feel very valued and appreciated for the work they undertake in the Company. There is a strong culture of praise, thanks and encouragement
- Decision-making and team working are major strengths in the company
- Members of staff believe that the company is a great place to work.

The one key area for development highlighted by the assessment was a greater focus needed in the area of return on investment in learning and development, to be able to more fully appreciate the full impact of learning and development in the company. This will be considered through 2017.

This Strategic report has been approved by the Board and is signed on their behalf by.

SIMON THOMSON
Chief Executive
7 March 2017

Board of Directors

	Simon Thomson	**James Smith**	**Ian Tyler**	**Todd Hunt**	**Iain McLaren**
	Chief Executive (51)	Chief Financial Officer (40)	Non-Executive Chairman (56)	Non-Executive Director (64)	Senior Independent Non-Executive Director (66)
Committee membership	Senior Leadership Team – Chair Nomination committee Attends remuneration committee by invitation Attends part of each audit committee by invitation Group Risk Management Committee – Chair	Senior Leadership Team Governance committee Attends audit committee by invitation Group Risk Management Committee	Nomination committee – Chair Governance committee Remuneration committee Attends audit committee by invitation	Attends remuneration committee by invitation	Audit committee – Chair Nomination committee Remuneration committee
Term of office	Simon was appointed to the Board in November 2006 as Legal and Commercial Director and became Chief Executive in July 2011.	James was appointed to the Board in May 2014 as Chief Financial Officer.	Ian was appointed as an independent non-executive director in June 2013 and became non-executive Chairman in May 2014.	Todd was appointed as an independent non-executive director in May 2003. Given his length of tenure, he is no longer considered to be independent in terms of the UK Corporate Governance Code.	Iain was appointed as an independent non-executive director in July 2008.
Independent	Not applicable	Not applicable	Yes	No	Yes
Skills and experience	LLB (Hons), Aberdeen University Diploma in Legal Practice, Glasgow University	BA (Hons), University of Oxford	Bachelor of Commerce, Birmingham University	Batchelor of Business Administration, University of Texas	BA in Accountancy and Finance, Heriot Watt University
	Simon Thomson was appointed Chief Executive in July 2011 having been Legal and Commercial Director since 2006 and holding various posts across the organisation including head of assets. Simon originally joined Cairn in 1995.	James Smith joined Cairn in March 2014 from Rothschild where he was a director of the energy and power team with 15 years' experience advising E&P companies, oil majors and national oil companies on their M&A transactions and equity and debt market financing.	Ian Tyler qualified as a chartered accountant with Arthur Andersen in 1987, subsequently holding a number of senior finance and operational positions within listed companies before being appointed chief executive of Balfour Beatty plc from 2005 to 2013. During this time, he took the company from being primarily a UK construction business, to a global infrastructure services business.	Todd Hunt has more than 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.	Iain McLaren is a chartered accountant and was formerly senior partner of KPMG in Scotland. He is also a past president of the Institute of Chartered Accountants of Scotland.
Key external appointments	Non-executive director of Graham's The Family Dairy Limited Member of the advisory Board of the Winning Scotland Foundation until March 2017	No external appointments	Non-executive director of BAE Systems plc Non-executive chairman of Bovis Homes Group PLC Independent chairman of AWE Management Limited Senior independent non-executive director of Mediclinic International plc until February 2017	President and joint owner of Atropos Exploration Company and Atropos Production Company	Chairman of Investors Capital Trust plc Non-executive director of Baillie Gifford Shin Nippon plc Non-executive director of Edinburgh Dragon Trust plc Non-executive director of Ecofin Water & Power Opportunities plc Non-executive director of Jadestone Energy Inc

Executive Directors

Non-Executive Directors

Alexander Berger	**M. Jacqueline Sheppard QC**	**Keith Lough**	**Peter Kallos**	**Nicoletta Giadrossi**
Non-Executive Director (50)	Non-Executive Director (61)	Non-Executive Director (58)	Non-Executive Director (57)	Non-Executive Director (50)
Audit committee Governance committee	Remuneration committee – Chair Governance committee – Chair	Audit committee Nomination committee Governance committee	Remuneration committee Nomination committee	Remuneration committee
Alexander was appointed as an independent non-executive director in May 2010.	Jackie was appointed as an independent non-executive director in May 2010.	Keith was appointed as an independent non-executive director in May 2015.	Peter was appointed as an independent non-executive director in September 2015.	Nicoletta was appointed as an independent non-executive director in January 2017.
Yes	Yes	Yes	Yes	Yes
Masters in Petroleum Engineering, Delft University MBA Rotterdam School of Management	BA, Memorial University of Newfoundland BA and MA in Jurisprudence from University of Oxford LLB, McGill University	MA Economics, University of Edinburgh MSc in Finance, London Business School	Degree in Applied Physics, Strathclyde University Degree in Petroleum Engineering, Heriot Watt University	BA in Mathematics and Economics, Yale University MBA, Harvard Business School
Alexander Berger is chief executive officer of Oranje-Nassau Energie B.V., a private Dutch exploration and production company based in Amsterdam.	Jackie Sheppard was executive vice president, corporate and legal at Talisman Energy Inc from 1993 to 2008 and appointed Queen's Counsel for the Province of Alberta in 2008.	Keith Lough was Finance Director of British Energy PLC from 2001 to 2004 before becoming a founder shareholder and Chief Executive of Composite Energy Ltd, a privately owned coal-bed methane focused business. He held this post until 2011, when Composite was divested to Dart Energy.	Peter Kallos has held a number of posts at Enterprise Oil including Head of Business Development, CEO Enterprise Italy and General Manager of the UK business before his appointment in 2002 as Executive Vice President International and Offshore at Petro-Canada. In 2010, Peter became Chief Executive of Buried Hill Energy.	Nicoletta Giadrossi spent 10 years at GE where she became General Manager for GE's Oil and Gas, Refinery & Petrochemicals Division. Subsequently, she spent a number of years in private equity ahead of being appointed VP and General Manager, EMEA at Dresser-Rand. She later joined Aker for two years before taking up the role of President (Region A, Europe, Africa, Middle East, Russia & India) at Technip, a role she held from 2014 to 2016.
Chief executive officer of Oranje-Nassau Energie B.V., and a director of Oranje-Nassau Energie UK Limited and Oranje-Nassau Energy Petroleum Limited Non-executive director of Discover Exploration Limited	Non-executive chair of Emera Inc. Director of the general partner of Pacific NorthWest LNG LP Founder, lead director and chair of the audit committee of Black Swan Energy Inc. Director of Seven Generations Energy Corporation	Senior Independent non-executive director of Rockhopper Exploration PLC Non-executive director of the UK Gas and Electricity Markets Authority Non-executive director of Gulf Keystone Petroleum Ltd. Non-executive director of Papau Mining PLC until November 2016 Non-executive director of Rock Solid Images Inc. until November 2016	Chief Executive of Buried Hill Energy	Non-executive director of Fincantieri S.p.A. Non-executive director or Bureau Veritas Group Non-executive director of Faively Transport

Corporate Governance Statement
Chairman's Introduction

Operating with integrity at all levels, at all times.

Dear Shareholder,

At Cairn, we operate with integrity at all times, recognising that in doing so the Company will maintain the trust of its many stakeholders. We are committed to working responsibly as part of our strategy to deliver value for all stakeholders. This means working in a safe and secure, as well as environmentally and socially responsible manner.

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 in line with shareholders' and other stakeholders' long-term interests, whilst also generating confidence that the business is conducting itself in a responsible manner. Further information on our governance, culture, strategy and business model and commitment to working responsibly can be found in the Strategic Report section of this Annual Report and Accounts.

We are cognisant of the Financial Reporting Council's ongoing valuable work in relation to corporate culture and the important role of boards in influencing and shaping corporate culture. As a relatively small but long established company with fewer than 250 employees, we have a culture based on acting responsibly at all times. This means having the right values, principles and policies in place, that they are embedded throughout the organisation, and that the right people are in place to implement and uphold our values. At Cairn, our culture is underpinned by a core set of values which reflect how we do business and the behaviours expected of our people. We communicate these throughout the business as 'the three Rs', which stand for Building Respect, Nurturing Relationships and Acting Responsibly (see below).

During the year the Board has also placed much focus on operational delivery and risk management. An open and balanced review of our business performance has been covered in the Strategic Report on pages 2 to 75. During the year, the Board regularly discussed our strategic priorities, operational delivery and the associated key business risks and their ongoing management. We provide further information on these activities on pages 34 to 47 of this report.

Our core values

Building Respect

We build respect by communicating openly with each other and our stakeholders, listening effectively and providing feedback and recognition in a constructive way.

10 Read more: **Our Culture** on **P10-11**

Nurturing Relationships

We work closely with our stakeholders – colleagues, local communities, contractors, suppliers, governments, regulators, non-governmental organisations, industry partners and shareholders.

10 Read more: **Our Culture** on **P10-11**

There has also been a continuing focus by both the Board and nomination committee in relation to succession planning throughout 2015 and 2016 (and subsequently) with the aim of assessing the executive, non-executive and senior succession pipeline at Cairn, and identifying what skills are needed to support our strategy and business for the long term. This will continue to be a key area of focus for the Board in future years. I am delighted to report that we have further strengthened and diversified our Board through the appointment of Nicoletta Giadrossi as an independent non-executive director on 10 January 2017. We provide further information in relation to this appointment and our succession planning in the separate Nomination Committee Report on pages 96 and 97.

IAN TYLER
Chairman
7 March 2017

"At Cairn, our culture is underpinned by a core set of values which reflect how we do business and the behaviours expected of our people."

Acting Responsibly

We act with honesty and integrity to ensure all our operations are carried out safely and empower our people to achieve their goals and contribute to the wider performance of the business in a responsible manner.

10 Read more: **Our Culture** on **P10-11**

Corporate Governance Statement
continued

Compliance with the UK Corporate Governance Code
As a company incorporated in the UK with a Premium Listing on the London Stock Exchange, Cairn is 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). This statement reports compliance with the version of the Code published in April 2016.

Cairn is fully committed to achieving compliance with the principles and provisions set out in the Code and the Board is responsible for ensuring that an appropriate framework is in place to do so.

The information in this statement, together with the audit committee report, nomination committee report and Directors' Remuneration Report, describe the manner in which the Company has applied the main principles of governance set out in the Code and complied with the individual Code provisions. It is the Board's view that the Company has fully complied with the Code throughout 2016.

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 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 senior management appointments below Board level and to our succession planning.

Following the appointment of two non-executive directors in 2015 and one new non-executive director in January 2017, the Board currently comprises the Chairman, two executive directors and seven non-executive directors. The current directors of the Company as at the date of this report are set out in the table opposite. Further information about our directors is included in the Board of Directors section on pages 76 and 77.

Board diversity
The mix in our membership.

Board diversity, by age (years)

55
average

Board diversity, by nationality

6:4

Board diversity, by tenure (years)

5.5
average

Board diversity, by gender

8:2

Name	Role	Date of appointment (in current role)	Date of last re-election
Simon Thomson	Chief Executive	July 2011	12 May 2016
James Smith	Chief Financial Officer	May 2014	12 May 2016
Ian Tyler	Non-executive Chairman	May 2014	12 May 2016
Todd Hunt	Non-executive director	May 2003	12 May 2016
Iain McLaren	Non-executive director	July 2008	12 May 2016
Alexander Berger	Non-executive director	May 2010	12 May 2016
Jackie Sheppard	Non-executive director	May 2010	12 May 2016
Keith Lough	Non-executive director	May 2015	12 May 2016
Peter Kallos	Non-executive director	September 2015	12 May 2016
Nicoletta Giadrossi	Non-executive director	January 2017	N/A

The Company considers ongoing refreshment of the non-executive directors on the Board to be positive as it brings new thinking to the Company as well as ensuring there is a healthy level of independent challenge to management and that the Board's collective skills and experience equip it to direct the Company's strategy and meet its business needs as they evolve over time.

The Board is also mindful however 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. Further information on succession planning at Cairn is included in the Nomination Committee Report on pages 96 and 97.

Diversity is a key element of the Cairn Board, with emphasis placed not only on gender but also on culture, nationality and experience. The Board currently has two female non-executive directors and continues to demonstrate diversity in a wider sense, with directors from the Netherlands, the USA, Canada, and Italy as well as the UK, bringing a range of domestic and international experience to the Board. The Board's 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 Nomination Committee Report on pages 96 and 97 and in the Strategic Report section of this Annual Report and Accounts.

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.

Chairman: key responsibilities	Chief Executive: key responsibilities
Leading the Board in an ethical manner and promoting effective Board relationships. Ensuring that the Board plays a full and constructive part in the determination and development of the Company's strategy. Building a well balanced Board, considering Board composition and Board succession. Ensuring the effectiveness of the Board and individual directors. Overseeing the annual Board evaluation and acting on its results. Ensuring appropriate induction and development programmes for directors. Setting the Board agenda, chairing Board meetings and overseeing implementation of the Board's decisions. Engagement with shareholders and other stakeholders when appropriate.	Managing the business and proposing and developing the Company's strategy and overall objectives in consultation with the Board. Driving the successful and efficient achievement of the Company's KPIs and strategic objectives. Leading the Senior Leadership Team in ensuring the effective implementation of decisions of the Board and its committees. Providing strong and coherent leadership of the Company and effectively communicating the Company's culture, values and behaviours internally and externally. Engagement with shareholders and other stakeholders.

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 Chief Financial Officer 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.

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 2015, the Company conducted its second externally facilitated Board evaluation (the first was in 2012). The 2015 evaluation resulted in some important recommendations for improving the Board's effectiveness, which have subsequently been implemented, including enhancements to Board papers and to the Board risk management process.

This year, in view of the externally facilitated evaluation carried out in 2015, it was agreed that an internal Board performance evaluation would be most beneficial to the Company. The Chairman and Company Secretary subsequently discussed how best to facilitate this and it was decided that the Company Secretary should prepare a questionnaire for this purpose.

Corporate Governance Statement
continued

The questionnaire was approved by the Chairman and this was subsequently completed by all directors to evaluate the performance of the Board, each of its committees, and individual Board members. A separate questionnaire in respect of the Chairman's performance was prepared by the Company Secretary and approved by the senior independent non-executive director.

Following completion of the questionnaires, the Chairman held a series of one-to-one meetings with each of the directors in late November and early December 2016 in order to discuss the outcomes of the evaluation. In addition, the senior independent non-executive director met with the non-executive directors (excluding Ian Tyler) in order to discuss and appraise the performance of the Chairman.

The main action points arising from the 2016 performance evaluation include the following:

Key actions	Implementation
Potential amendments to running order of pre-Board and committee meetings	Consideration will be given to adjusting the running order of pre-Board and Board committee meetings in order to maximise the Board's time efficiency.
Consider ongoing requirement for Governance Committee	Consideration will be given to whether the Governance Committee continues to be required as the Board and other committees are ensuring compliance with all relevant governance requirements.
Enhancements to annual Board strategy session	The Chairman has proposed some amendments to the structure of this annual session to facilitate a more focused Board discussion of strategic goals and past performance.

As explained above, some improvements have been identified and have already been implemented or will be addressed during 2017.

Following the Board performance evaluation process conducted in 2016, the Board and the Board committees are satisfied that they are operating effectively and that each director has performed well in respect of that director's role on the Board and its committees. The Board believes that all of the directors' performance continues to be effective and that they each demonstrate commitment to their role.

The executive directors also have their performance reviewed by the remuneration committee against the Group KPIs which are set annually (further details of the KPIs can be found in the KPI section on pages 34 to 38). The 2016 bonuses payable to the executive directors under the Company's cash bonus scheme (described further in the Directors' Remuneration Report on pages 114 to 117) were linked directly to the Group's performance against these KPIs. As the KPIs set out our strategic objectives, this ensures that executive performance is directly linked to Group strategy.

Independence of non-executive directors
The Board considers the independence of each of the non-executive directors on an ongoing basis, 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 and other stakeholders;
- has a detailed and extensive knowledge of the Company's business and of the market as a whole which provides a solid background against 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 against these criteria, the Board concluded that all non-executive directors demonstrated each of the required competencies to a high level and are, therefore, each considered independent by the Board.

The Board recognises that, in view of the characteristics of independence set out in the UK Corporate Governance Code, length of service is an important factor when considering the independence of non-executive directors and that directors having served for longer than nine years may not be considered independent. The Board is however satisfied that Todd Hunt's judgement has remained independent and that he has consistently displayed all of the behaviours expected of our independent non-executive directors. Moreover, the Board is of the view that Mr Hunt brings an extremely valuable level of insight and challenge to Board discussions and that his extensive industry experience continues to be of significant benefit to the Company.

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 will seek re-election at the AGM to be held on 19 May 2017.

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, new directors are provided with a comprehensive induction pack which contains a wide range of materials including:

Board	Board papers and minutes of previous meetings; schedule of matters reserved to the Board; financial delegations of authority; list of Board and committee members and dates of appointment; and schedule of dates for Board and committee meetings.
Committees	Terms of reference for all Board committees.
Risk	Terms of reference for Risk Management Committee and minutes of last meeting; current Group Risk Matrix and Risk Appetite Statement; FRC Guidance on Risk Management, Internal Control and Related Financial and Business Reporting.
Key policies	Group Corporate Responsibility Business Principles; Group Code of Business Ethics; Anti-Bribery-and-Corruption (ABC) Management System; ABC Business Partner Due Diligence Procedure; Dealing Code; Procedures, Systems and Controls for Compliance with the Market Abuse Regulation, the Listing Rules and the Disclosure Guidance and Transparency Rules.
Organisation	Group Structure Chart; latest Annual Report and Accounts.

Governance	UK Corporate Governance Code; all supporting FRC Guidance; FRC Feedback Statement on UK Board Succession Planning and FRC Report Corporate Culture and the Role of Boards; GC100 Directors' Remuneration Reporting Guidance.
Legal/regulatory	Memorandum for directors on their responsibilities and obligations as directors.
Insurance	Full details of directors' and officers' liability cover.

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 for its directors. In 2016, 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 2016, the subjects covered by these seminars included:

- an expert-led session on general global economics and macro-economic trends;
- a corporate governance and legal regulatory update delivered by the Deputy Company Secretary;
- a pre-implementation seminar on the requirements of the new Market Abuse Regulation presented by Morgan Stanley;
- an anti-bribery-and-corruption update delivered by Pinsent Masons; and
- various asset presentations by senior management at pre-Board meetings (further information on pre-Board meetings is included on page 84).

These seminars are held prior to Board meetings and are attended by all directors present at such meetings as well as the Chief Operating Officer and Director of Exploration (the Company keeps a record of attendance). Any director may request that a particular subject is covered in a seminar. In addition, all media articles relating to the Company and all analyst reports relating to the Company are distributed to all directors.

The Company also provided additional training and information for all of its PDMRs (Persons Discharging Managerial Responsibility) regarding their revised obligations and responsibilities as a result of the implementation in July 2016 of the Market Abuse Regulation.

Information and support
The Board has full and timely access to all relevant information to enable it to discharge its duties. Under the direction of the Chairman, the Company Secretary is responsible for ensuring good information flows within the Board and its committees and between management and non-executive directors, as well as facilitating induction and assisting with professional development as required. 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. The governance committee also supports the Board in relation to corporate governance matters and further information on the role of this committee is provided on page 87.

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. 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. The Board conducted an in-depth review of this in 2015 and adopted an updated schedule of matters reserved which is divided into categories covering different types of decisions, including: corporate; Board/directors; financial/operational; and legal/regulatory.

By way of example, some of the matters which the Board considered and/or approved during 2016 and Q1 2017 were:

Corporate	Board/Directors
The Company's 2015 Annual Report and Accounts and 2016 Half-Yearly Report	The appointment of a new non-executive director
The Company's 2016 AGM circular	Appointments to Board committees
The Company's Risk Appetite Statement	Detailed review of succession planning
Financial/Operational	**Legal/Regulatory**
The appropriateness of the Group going concern sign-off for the 2015 full year accounts and 2016 interim accounts	Oversight of the arbitration process seeking resolution of the Indian tax issue
The Company's viability statement	Implementation of new policies and procedures to comply with the Market Abuse Regulation
The Company's annual work programme and budget	
Group Reserves and Resources	
The Company's HSE Policy	
Selection of a mobile offshore drilling unit and well management services for the 2016/2017 Senegal drilling programme	
Approval of Group funding strategy and related financing arrangements	

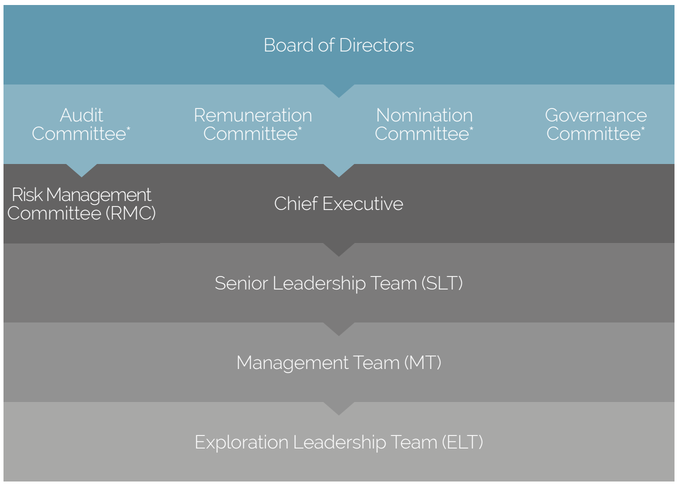
In addition to the above, the Board conducts an annual review of the effectiveness of the Company's internal controls (with ongoing monitoring of this throughout the year); an annual detailed strategy meeting; and an annual 'deep-dive' session on risk management.

The Board also has an approved set of 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 senior executive management structure at Board level and beneath remains unchanged from that disclosed in last year's corporate governance statement, with the Senior Leadership Team (SLT) and Management Team (MT) continuing to play a key role in supporting the Board.

Corporate Governance Statement
continued

Board and management committee structure



* Further information on our Board committees is contained later in this statement and in the separate audit committee report, nomination committee report and directors' remuneration report.

The SLT comprises the Chief Executive, the Chief Financial Officer, the Chief Operating Officer (COO), the Director of Exploration, the Company's two Regional Directors and the General Manager, Senegal. The SLT is chaired by the Chief Executive and meets six times per year with those meetings scheduled in advance of Board meetings.

Key elements of the SLT's role include the following:

- devise and generate the Company's strategy to be proposed to the Board for approval and implement and communicate this strategy across the business;
- implement the business plan, the key performance indicators and annual work programme and budget following their approval by the Board;
- consider business development and new venture projects prior to submitting these to the Board; and
- provide leadership and guidance to the Company on vision, strategy, culture, corporate governance, corporate responsibility and HSE matters.

The members of the SLT are also members of the RMC, which identifies and reviews key business risks – further information on the role of the RMC is contained in the internal control section of this statement on page 89.

The MT comprises the COO (chair), the Director of Exploration, the Deputy Finance Director, two Regional Directors, the General Manager, Senegal, and four functional managers (Human Resources Manager, Legal Manager, HSE Manager and Business Development and New Ventures Manager).

The MT meets formally six to nine times per year with four of those meetings focusing on a quarterly performance review of the business.

The key elements of the MT's role include the following:

- develop and implement a Business Plan, which will deliver the Company's strategic objectives (these will be reflected in annual KPIs, including HSE);
- critically assess and determine the mitigation plans for key business risks and ensure that all risks are captured and reviewed regularly in the Company's risk register;
- coordinate operations and licence management along with resource allocation and organisational alignment to ensure timely and cost-effective delivery against approved budgets;
- oversee the Company's commitment to working responsibly; and
- review and approve the Company's Standard Operating Procedures.

The Exploration Leadership Team (ELT), which is chaired by the Director of Exploration, comprises the Group Geoscience Manager, the Chief Geologist, the Chief Geophysicist, three regional Exploration Managers and a representative from new ventures/new business.

The ELT meets on a monthly basis to facilitate alignment, consistency, best practice and teamwork in the following areas:

- ensuring exploration, appraisal and new venture opportunities align with the Company's Business Plan;
- ensuring consistent screening and ranking of exploration opportunities prior to detailed assessment, thereby utilising the significant knowledge and experience of the ELT;
- developing and implementing new geosciences technology and techniques where appropriate for application within the Company to reduce subsurface uncertainty and/or risks; and
- ensuring appropriate representation at resource assessment reviews and other internal subsurface peer reviews.

Board meetings
During 2016, six scheduled meetings of the Board were held, with all of these meetings taking place over two consecutive days. The first day includes a Chief Executive's lunch with the non-executive directors and a Board education session followed by a pre-Board meeting and a Board dinner in the evening. The pre-Board meeting includes a detailed presentation from senior management on key projects, assets or matters to be considered at the Board meeting and thereby provides an excellent opportunity for a technically rigorous discussion. It also allows the Board to more fully understand any risks or challenges to the business plan and strategy and allows exposure to talent within the Company.

The Company's Board meetings are then held on the second day and followed by a Board lunch. Board committee meetings are held on either the first or second day or, depending on the number of committee meetings required, on both days. All Board committee meetings take place prior to the main Board meeting so that the chair of each committee can provide a report to the Board.

Three of the Board meetings during 2016 were held at the Company's registered office in Edinburgh, two were held at the Company's office in London and one was held at the Company's office in Stavanger. Details of attendance at each of those Board meetings, and at meetings of each of the Board committees, are set out on page 86. 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 in the unlikely event that directors are not able to attend meetings in person.

The annual timetable for Board and committee meetings is discussed at least 18 months prior to its commencement allowing the directors to plan their time accordingly. The Board and committees have agreed dates for all scheduled meetings in 2017 and 2018. This process ensures that the Chairman can be comfortable that each director is able to devote sufficient time and resources to their role on the Board and, where relevant, its committees.

The formal agenda for each scheduled Board meeting, which regularly includes presentations from senior management, is set by the Chairman in consultation with the Chief Executive and the Company Secretary. The system for establishing agenda items means that the Chairman, the Board and each of the board committees have the confidence that all required items are included on their agenda at the most appropriate time of the year and that there is sufficient time allocated for discussion, allowing the directors to discharge their duties effectively.

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. There is also a procedure in place to allow Board meetings to be convened at short notice where required to deal with specific matters which need to be considered between scheduled Board meetings.

The non-executives have a practice of meeting informally before and after each Board meeting without executive directors being present. At these non-executive forums, the non-executive directors are invited by the Chairman to bring forward any matter pertaining to the business of the Board that they believe would benefit from discussion in such forum. This practice also applies after Board committee meetings (in particular the audit, remuneration and nomination committees) to ensure that non-executive directors can discuss any relevant issues arising from those meetings without executive management being present.

Overseas Board Meetings

A valuable opportunity for the Board to enhance its knowledge and understanding of the business by combining one meeting in the annual Board cycle with visits to overseas offices and site visits to key assets.

Senegal: December 2015
The Board spent three days in Senegal in early December 2015 including an offshore visit to the drilling rig operating at that time. The Board and committee meetings were held in the Dakar office and the Board also met with a number of Senegalese government ministers at a reception hosted by the British Ambassador to Senegal.

Stavanger: June 2016
The Board spent two days in Stavanger in June 2016 – in addition to the Board and committee meetings held in the Stavanger office, the Board held a half-day strategy session and had a detailed presentation on the Group's North Sea assets from the Stavanger management team.

Board visit to Ocean Rig Athena drill ship used during Cairn's 2015/2016 Senegal drilling campaign.

Corporate Governance Statement
continued

Directors' attendance at Board and committee meetings
The table below sets out the attendance record of each director at scheduled Board and Board committee meetings during 2016.

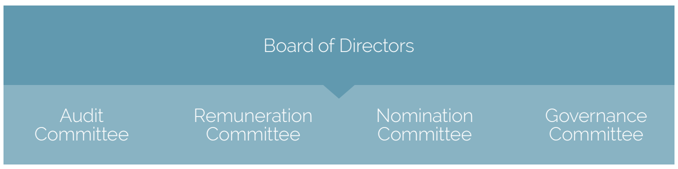
Board meeting attendance

	Board	Audit Committee	Remuneration Committee	Nomination Committee	Governance Committee
Meetings held during 2016[1]	6	4	6	3	2
	Meetings attended	Meetings attended	Meetings attended	Meetings attended	Meetings attended
Executive Directors					
Simon Thomson (Chief Executive)	6	n/a[2]	n/a[2]	2	n/a
James Smith (CFO)	6	n/a[3]	n/a	n/a	2
Non-Executive Directors					
Ian Tyler (Chairman)	6	n/a[4]	5[5]	3	2
Iain McLaren (Senior Independent Director)	6	4	6	3	n/a
Todd Hunt	6	n/a	n/a[6]	n/a	n/a
Alexander Berger	6	4	n/a	n/a	2
Jackie Sheppard	6	n/a	6	n/a	2
Keith Lough	6	4	n/a	3	2
Peter Kallos	6	n/a	6	3	n/a

Notes:
n/a not applicable (where a director is not a member of the committee).
1 During 2016, 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 Simon Thomson is not a member of the remuneration committee but attends its meetings by invitation (other than parts of meetings where he would be conflicted). Mr Thomson also attends part of each audit committee meeting by invitation (to participate in discussions on risk and internal control only).
3 James Smith is not a member of the audit committee but attends its meetings by invitation.
4 Ian Tyler is not a member of the audit committee but attends its meetings by invitation.
5 Whilst Ian Tyler was unable to attend the first remuneration committee meeting held in 2016, he submitted detailed comments prior to the meeting to both the chair of the committee and the Chief Executive (the meeting had been convened to consider one agenda item, namely performance against the Group's 2015 KPIs).
6 Todd Hunt is not a member of the remuneration committee but attends its meeting by invitation.
7 Nicoletta Giadrossi was appointed as a non-executive director of the Company on 10 January 2017 and did not attend any meetings during 2016.

Board committees

Board committee structure



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. Copies of the terms of reference, which satisfy the requirements of the UK Corporate Governance Code, are available on the Company's website.

Each of the Board committees is 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.

In line with best practice, more detailed reports from the audit and nomination committees are presented as separate reports (on pages 91 to 97) rather than including these in the Corporate Governance Statement. In addition, full details of the Company's remuneration policy are given in the separate Directors' Remuneration Report on pages 98 to 124.

Audit committee

The members of the audit committee during the year were as follows:

- Iain McLaren (Chair);
- Alexander Berger; and
- Keith Lough

The audit committee met four times during 2016 and currently comprises three independent non-executive directors. The Chairman is not a member of the committee but attends its meetings by invitation. Further information on the role, responsibilities and work of the audit committee is included in the Audit Committee Report on pages 91 to 95.

Remuneration committee

The members of the remuneration committee during the year were as follows:

- Jackie Sheppard (Chair);
- Iain McLaren;
- Ian Tyler; and
- Peter Kallos

The remuneration committee met six times during 2016 and currently comprises four independent non-executive directors. The Chief Executive is not a member of the committee but attends its meetings by invitation. The committee'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 committee has established a practice of meeting informally without any executive directors or advisers present after each committee meeting to allow the non-executives to discuss any matter which has arisen in the meeting (or relating to the duties of the committee) which they believe would benefit from discussion in such a forum.

Further information on the role, responsibilities and work of the remuneration committee is included in the Directors' Remuneration Report on pages 98 to 124.

Nomination committee

The members of the nomination committee during the year were as follows:

- Ian Tyler (Chair);
- Iain McLaren;
- Simon Thomson;
- Keith Lough; and
- Peter Kallos

The nomination committee met three times in 2016. 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, the Chief Executive is also a member of the committee.

Further information on the role, responsibilities and work of the nomination committee is included in the separate Nomination Committee Report on pages 96 and 97.

Governance committee

The members of the governance committee during the year were as follows:

- Jackie Sheppard (Chair);
- Alexander Berger;
- Ian Tyler;
- Keith Lough; and
- James Smith

The governance committee met twice in 2016 and is comprised of a majority of non-executive directors. In addition, to ensure continuing executive input on governance matters, the CFO is also a member of the committee.

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. 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.

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 with executive management after the announcement of the year-end and half-yearly results. The Chairman is available to attend a number of these meetings. The Board is kept informed of any issues raised by shareholders both as a standing agenda item in Board papers and through feedback at pre-Board meetings and following results or other significant announcements.

Corporate Governance Statement
continued

AGM Details (2016 and 2017)	Overview
2016 AGM: held on Thursday 12 May 2016 The Caledonian Waldorf Astoria Hotel, Edinburgh	• Full director attendance • At least 96.79% of votes received for the re-election of all directors • Highest votes in favour 99.99% for four resolutions • Lowest votes in favour: 96.55% to approve 14 days' notice of general meetings
2017 AGM: to be held on Friday 19 May 2017 The Caledonian Waldorf Astoria Hotel, Edinburgh (full details in Notice of AGM)	• Full director attendance expected • New remuneration policy to be tabled for approval • 18 Ordinary Resolutions and 4 Special Resolutions being proposed to shareholders

In addition, the Company maintains an investor relations database which details all meetings between the Company and its investors or other related stakeholders. All analyst reports relating to the Company are also distributed to the Board.

A list of the Company's major shareholders can be found in the Directors' Report on page 127. 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.

During 2016, the Company undertook a comprehensive programme of engagement with a selection of Cairn's larger institutional investors and their representative bodies in order to understand their views on a number of proposed changes to the Company's remuneration arrangements. Shareholders were given an early opportunity to raise any questions, and certain suggestions made by shareholders were included in the final remuneration structure set out in the Directors' Remuneration Report.

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 directors to attend the AGM. 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.

As part of our commitment to transparency we look to involve shareholders, as one of our key stakeholder groups, fully in the affairs of the Company and to give shareholders the opportunity at the AGM to ask questions about the Company's performance and activities. Details of resolutions to be proposed at the AGM on 19 May 2017 can be found in the Notice of Annual General Meeting which is contained in the shareholder circular posted with this Annual Report and Accounts. Further explanation of each of the resolutions can also be found in the circular.

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 following 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.

Information pursuant to the Takeover Directive
The Company has provided the additional information required by the Disclosure and Transparency Rules of the UK Listing rules (and specifically the requirements of DTR 7.2.6 in respect of 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.

Internal control
The Board has overall responsibility for the Group's system of internal control, which includes all material controls, including financial, operational and compliance controls and related risk management, and for regularly reviewing its effectiveness. The system of internal control is designed to identify, evaluate and manage significant risks associated with the achievement of the Group's objectives. Because of the limitations inherent in any system of internal control, Cairn's system is designed to meet its particular needs and the risks to which it is exposed, with a focus on managing risk rather than eliminating risk altogether. Consequently it can only provide reasonable and not absolute assurance against material misstatement or loss.

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 a commonly used and recognised framework for considering internal control systems. The COSO framework, which was first released in 1992 and updated in 2013, seeks to help organisations develop systems of internal control which help facilitate the achievement of business objectives and improvements in Company performance. The framework also supports organisations in adapting to increasingly complex business environments and managing risks to acceptable levels with the aim of safeguarding shareholders' interests and Company assets.

The framework has been in place for the 2016 financial year and up to the date of approval of the Annual Report and Accounts. The Board, supported by the audit committee, has carried out a review of the effectiveness of the system of internal controls during 2016 and will ensure that a similar review is performed in 2017. In so doing, the Board and audit committee took into account the assurance provided by the Chief Executive in respect of the effectiveness of the Group's system of internal control. The Board is accordingly satisfied that effective controls are in place and that risks have been mitigated to a tolerable level across the Group in 2016.

Cairn seeks to create value through oil and gas exploration and production while at the same time safeguarding the environment and respecting and contributing to the communities it is a part of. In order to achieve this, Cairn's core values of building respect, nurturing relationships and acting responsibly are at the core of the business, informing how the Company operates. These values are promoted to Cairn's employees, partners and contractors. Cairn's licence to operate depends on transparent relationships and active stakeholder engagement programmes with our many stakeholders including governments, communities, partners, shareholders and suppliers globally. The directors believe that this commitment to strong governance generates trust and ensures consistent global standards and is critical to the Company's success.

Particular attention has been placed by the Company's management during 2016 on ensuring that an effective system of internal control has been maintained during the year in relation to the key risks in the Company's business activities. Enhancements have been made during 2016 to the following key controls, business processes and procedures:

- the Group developed a Cairn Operating Standards Manual of core business processes which outlines 'the Cairn way' for executing key processes. The Manual was rolled out across the Group in 2015 and a further three chapters were added to it in 2016. Compliance with the business standards became mandatory from Q1 2016;
- the suite of policies and procedures which form the Group's Corporate Responsibility Management System (CRMS) were enhanced to achieve continued alignment with the Cairn Operating Standards and the latest International Association of Oil and Gas Producers (IOGP) guidance. This included the Group Code of Business Ethics and the Group's CR policies;
- the Group Risk Management Procedure was updated to incorporate a number of recommendations from a recent risk management audit and to include some emerging practices in risk management. The procedure was rolled out across the Group in Q1 2016;
- the Group Business Continuity Plan was revised in 2016 to determine if the existing business continuity recovery strategy remained appropriate. A test of the Business Continuity Plan is planned for Q4 2017; and
- the Group plans to implement a new Enterprise Resource Planning (ERP) solution to replace the existing Oracle e-business suite. The aim of this project is to enhance levels of engagement and compliance through the implementation of an intuitive system interface. This would provide a single global ERP platform for Cairn, facilitating consistent, transparent processes in Edinburgh, Stavanger, Dakar and London.

The following describes the key elements of the framework and the processes used by the Board during 2016 to review the effectiveness of the system and the approach to be taken in 2017.

1. Strategic Direction
The Company's strategy and business plan are proposed by the SLT and approved by the Board. The Chief Executive is responsible for managing the Company's business and implementing the Company's strategy and overall commercial objectives in consultation with the Board and SLT. The Chief Executive is also responsible for implementing the decisions of the Board and its committees and driving performance against the Company's KPIs.

2. Operating Management
The Company operates three regional units covering different countries and assets and with various partners on both an operated and non-operated basis. The assets within each region are the principal focus for our regional managers, who are tasked with delivering the strategic objectives for their particular region, with a combination of operational and technical teams as well as functional departments providing support to each of the assets. The implementation of the Cairn Operating Standards supports this process, providing assurance, standards and consistency in the delivery of our strategic objectives.

The executive directors continue to be supported by the SLT as well as by the MT and ELT. Further information on the composition of these teams and their remit can be found earlier in this statement on page 84. There are also a number of functional department heads whose roles include providing expert input and challenge to the Company's work programmes, budgets and business plans; and supplying the directors with full and accurate information with which to make statements on the adequacy of internal control.

The Company refreshes its Business Plan, work programme and budget on an annual basis in line with its overall strategy. These documents start at asset level before being consolidated at regional and Company levels. The Business Plan sets out detailed objectives and KPIs for each asset and supporting functional departments, and is consolidated into the Company's strategic planning. After an iterative process, the annual Business Plan, work programme and associated budget are presented to 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 Board is responsible for maintaining sound risk management and internal control systems across the Cairn Group. The Board must satisfy itself that the significant risks faced by the Group are being managed appropriately and that the system of risk management and internal control is sufficiently robust to respond to internal or external changes in the Group's business environment.

The RMC 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 Statement agreed by the Board.

To supplement the role of the RMC, the Group Risk Management Procedure defines the processes through which Cairn seeks to systematically identify, analyse, assess, treat and monitor the business risks faced by the Group. The Group Risk Management Procedure also identifies the risk management organisational structure through which business risks are managed and regularly reviewed at operating, asset, country and Company levels. Asset, project, country and functional level risk registers are used to capture, assess, monitor and review risks before the principal risks are consolidated into the Group Risk Register.

In 2016, risk management updates were presented at each Board meeting and as part of an annual process, the Board undertook a strategic risk workshop which analysed the key threats and opportunities which could impact on achievement of the Group's strategic objectives. This was completed in December 2016.

The RMC, which meets on a quarterly basis, was chaired by the CEO in 2016 and comprises the 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 MT risk meetings were also held during 2016 to manage and facilitate the assessment and treatment of business risks that may affect the Company's ability to deliver its strategy.

Corporate Governance Statement
continued

Enhancements to our approach to risk management during 2016 included the following:

- the Group Risk Appetite statement was reviewed and approved by the Board. The Board is satisfied that the current level of risk the Group is willing to take in pursuit of its strategic objectives is appropriate;
- the Group Risk Management Procedure was revised and rolled out across the Group in Q1 2016; and
- a project was undertaken to review the merit of implementing a risk solution to enhance the risk management system. A number of systems were evaluated and work continues on determining the value of implementing a risk solution. A final decision is expected in Q1 2017.

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 2016 is that the internal controls in respect of key risks are effective.

4. Assurance

The 'three lines of defence' framework adopted by the Board provides 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 the relevant roles and responsibilities. The framework defines the key policies and procedures which govern the way in which Cairn conducts its business and is therefore a core part of its system of internal control.

During 2016, 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 through the completion of internal control self-assessment questionnaires. These questionnaires, which are tailored to each region or function, are designed to provide an internal assessment of the effectiveness of key controls for the Group's principal risks.

Additionally, assurance maps for the principal risks are being developed, which outline the key sources of assurance across the three lines of defence. The three lines of defence model is a method of assessing different sources of assurance the Group can rely on when analysing key risks and controls. Assurance is gained through the application of the business management system which directs the day-to-day running of the business (first line), the oversight functions within Cairn which provide challenge to the risk and control environment (second line) and any third party reviews the Group instructs to assess the status of a risk/control (third line). The assurance maps help identify potential areas of control weakness and/or ineffective use of assurance resources across the Group, which has influenced the topics included in the 2017 Internal Audit Plan.

The Directors derived assurance from the following internal and external controls during 2016:

- 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 and actions taken in respect of weaknesses identified in the prior 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 and actions taken in respect of weaknesses identified in the prior 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.

IAN TYLER
Chairman
7 March 2017

Audit Committee Report

The Audit Committee

The audit committee continued to support the Board in its responsibilities which include setting the Company's strategic aims, providing the leadership to put them into effect, supervising the management of the business and reporting to shareholders on their stewardship. As part of this, the committee's responsibilities include the integrity of the Group's financial statements, the effectiveness of the Group's risk management and internal assurance processes and related governance and compliance matters, including assessment of going concern and longer-term viability.

Members and meetings in 2016	Member since	Meetings attended
Iain McLaren (Chairman)	07/08	
Alexander Berger	03/12	
Keith Lough	05/15	

Dear Shareholder,

Composition and summary of audit committee meetings during the year

During the year under review, I served as Chair of the audit committee alongside two of my fellow non-executive directors; Alexander Berger and Keith Lough. Both Alexander and Keith are considered by the Board to be independent. Ian Tyler also attended meetings in his capacity of Chairman of the Cairn Energy PLC Board.

The members of the committee have been chosen to provide the wide range of financial and commercial experience needed to fulfil these duties. Keith and I are Chartered Accountants with recent and relevant financial experience. Alexander brings comprehensive industry knowledge to the committee.

At our request, the CFO, the Chief Executive (in his capacity of Chair of the Group's Risk Management Committee) and senior members of the Finance and Risk and Compliance departments attended each of these meetings. Additionally, both internal and external auditors also attended each meeting. I also regularly met privately with the external audit partner to discuss matters relevant to the Group throughout the year.

The audit committee met four times in 2016, with meetings arranged around the key external reporting dates. The first meeting in March 2016 focused on the 2015 year-end external audit process (reported in the 2015 Annual Report and Accounts). Meetings in June and August both centred on the Group's half-year reporting and a December meeting on planning for the 2016 year-end cycle and external audit process and internal work programme for 2017. Subsequent to the year-end, a further meeting was held in March 2017 to conclude on the 2016 audit and significant issues.

At each meeting the committee receives an updated report from the external auditors which either explains their plans and scope for a forthcoming audit or review, or contains the conclusions from that audit or review. The audit committee also monitors the internal audit process, tracking the progress of internal audits and reviewing their output and recommendations.

The audit committee also closely monitor Cairn's Risk Management system, reviewing the activities of the Group's Risk Management Committee and the Group's risk management project plan with further review and challenge of the Group's risk registers and opportunity matrix at each committee meeting.

Other business covered by the committee includes the annual approval of corporate assumptions, the Group's policy on non-audit services and the Group's Whistleblowing Policy.

FRC Corporate Reporting Review

During the year the FRC's Conduct Committee raised a number of points on the Company's 2015 Annual Report. The Committee has reviewed the correspondence between the Company and the FRC, noting that the Company has responded to all of the initial points raised. The Committee are supportive of the Company's response to date. As a result of the initial correspondence, additional disclosures are included in the 2016 financial statements in respect of the Group's oil and gas assets and segmental reporting. The Committee also noted the Company's commitment to consider the need for further disclosures on the impact of climate change as appropriate. The Committee is aware of continuing communication, with the FRC seeking additional detail on the Company's assessment on the impact of climate change and further clarification regarding the Group's tax disclosures.

Audit Committee Report
continued

Responsibilities and activities during the year

The Terms of Reference of the committee take into account the requirements of the Corporate Governance Code and are available for inspection on the Group's website. A summary of the committee's principal responsibilities and activities during the year is set out below.

	Principal responsibilities of the committee:	Key areas formally discussed:
Financial statements	• Monitoring the integrity of the financial statements of the Group and formal announcements relating to the Group's financial performance; • reviewing any significant financial reporting judgements; and • reviewing the appropriateness of accounting policies, their consistent application and disclosures in financial statements.	• Going concern conclusions and linkage to the viability statement; • significant accounting issues at the interim and year-end (see below); and • approval of the Group's corporate assumptions (those impacting impairment testing are summarised in section 2 of the financial statements).
External audit	• 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.	• Reviewing the external auditor's scope and audit plan for the 2016 year-end; • discussing the materiality levels set by the auditors; • approval of the auditor's remuneration; • consideration of the results of the external audit with the auditors and management; and • assessment of the effectiveness of the external audit (see below).
Internal risk management and assurance	• Reviewing the Group's internal financial controls and internal control and risk management systems and oversight of the Group's Risk Management Committee; and • monitoring and reviewing the effectiveness of the Group's internal audit function.	• Reviewing the Group's corporate and operational risk register; • reviewing reports on the activities of the Risk Management Committee; • selection of internal audit work planned for 2017 and consideration for future years; and • assessment of key findings raised from internal audits conducted in the year.
Whistleblowing procedures	• 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.	• Reviewing and approving of the Group's whistleblowing procedures.
Other matters	• Reviewing the Group's policy for approval of non-audit work to the Company's auditors; and • reviewing booking of Group reserves and resources.	• Classification of reserves and resources for disclosure in the Annual Report.

The review of the Annual Report and Accounts for fair, balanced and understandable presentation and disclosure, while considered by the Audit Committee, is formally performed and approved by the full Cairn Energy PLC Board.

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. Cairn not only adopted this policy but complied with this provision early and completed an external audit re-tendering process in 2013. PricewaterhouseCoopers LLP (PwC) were subsequently appointed as external auditor of the Group, on our recommendation. The 2016 year-end audit therefore represents the fourth year of PwC's tenure as Group auditor.

2016 year-end significant accounting issues

The Group's ongoing focus on growing its significant Senegal resource base and on progressing its North Sea developments to first oil and cash flow in 2017 within a continuing low oil price environment provide the backdrop for the significant accounting issues that were reviewed by the committee during the year.

Carrying value of exploration assets

Audit committee action	Audit committee conclusions
The committee reviewed the carrying value of the Group's exploration and appraisal assets, challenging management where costs remain capitalised for assets where no exploration drilling has taken place.	After challenging management, the committee are satisfied that exploration costs remaining in the Group's exploration and appraisal assets are appropriately capitalised.
The committee also reviewed the exploration assets impairment tests performed by management on the Group's key exploration assets in the Senegal and UK & Norway regions, noting and challenging the key assumptions included within fair value models.	The committee were satisfied that impairment tests performed by management were conducted in accordance with Cairn's accounting policy, agreeing with the impairment charge recognised. The committee were satisfied that the Group's key corporate assumptions on which the impairment tests were based are appropriate.

Impairment testing on oil and gas assets and goodwill

Audit committee action	Audit committee conclusions
The committee review and approve the Group's corporate assumptions set by management, which include short and long term oil price. In challenging those assumptions, the committee benchmark against market trends, observed independently by the Group's auditors, seeking assurance that the assumptions used by management are comparable with those applied in the sector. These assumptions are key inputs into the impairment testing of the Group's oil and gas related assets, which is the most significant accounting issue in the current year. Further the committee consider asset specific assumptions applied by management in impairment models, including reserve volumes and production commencement dates.	The audit committee were satisfied that appropriate corporate assumptions were adopted by management, as key inputs into financial models used in the impairment calculations. The committee continue to monitor these assumptions at each meeting. The committee also were satisfied with the reserve volumes booked by management, taking assurance from independent reserve reports which support management's approach. As production nears on the Group's development assets, the committee were satisfied that commencement dates for production applied in the impairment models were consistent with current expectations.
The committee reviewed managements conclusion on the impairment test and the impairment subsequently recorded in the income statement, seeking assurance from the auditors that impairment has been disclosed correctly between exploration and development assets and related goodwill.	The committee were satisfied that the correct impairment charge was recorded in the financial statements and that this was appropriately disclosed by category of asset.

Other recurring accounting issues

There were two further material accounting issues where the audit committee challenged the judgement of management.

Indian taxation arbitration

The audit committee continue to monitor progress in the ongoing arbitration with the Government of India. In line with prior years, the committee were satisfied that no provision is required in the financial statements in relation to the Indian tax proceedings. The committee support management's disclosure of this issue as a contingent liability.

Recognition of deferred tax assets on UK tax losses

The audit committee examined management's conclusion that it remained inappropriate to recognise deferred tax assets at the balance sheet date. The committee were satisfied that the approach management had taken to assess the likelihood of future profit available to offset tax losses was appropriate and that suitable sensitivity analysis had been performed to support management's conclusion.

Going concern and viability

At each reporting date, management consider the factors relevant to support a statement of going concern (see page 140). 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, challenged and is appropriate.

Given the continuing low price environment facing the oil and gas industry, the audit committee carefully reviewed management's going concern conclusion based on the Group's latest net cash position and the forecast exploration and appraisal spend in the period ending 31 March 2018. This confirmed that the Group is fully funded to meet its work programme and firm commitments over this period. The audit committee subsequently recommended to the Board that the Group continues to use the going concern basis in preparing its financial statements.

With the viability statement now in its second year (included on page 40), the audit committee took advice on how the Company's implementation of this new reporting requirement compared with other reporters and what improvements the Company could make in preparing the viability statement for the current Annual Report.

At the March 2017 meeting the committed reviewed and queried management on the sensitivity analysis prepared to support their conclusions reached. Following this review, the committee recommended approval of the viability statement to the Board.

Audit Committee Report
continued

Assessment of external audit process

The committee has an established framework to assess the effectiveness of the external audit process. This comprises:

Audit committee action	Audit committee conclusion
A review of the audit plan including the materiality level set by the auditors and the process they have adopted to identify financial statement risks and key areas of audit focus (summarised in the Independent Auditor's Report on pages 129 to 133).	The Committee agreed with the level of materiality set by the auditors.
A review of the Audit Quality Inspection (AQI) Report on our auditors published by the Financial Reporting Council with particular emphasis on those key messages applicable to Cairn.	There were no matters raised in the AQI report that caused concern for the audit committee.
A review of the final audit report, noting key areas of auditor judgement and the reasoning behind the conclusions reached.	The audit committee reviewed findings on the key audit issues identified. The committee were satisfied that appropriate challenge had been made of management and that the audit process was robust.
Regular communications through formal papers submitted and presentations to the committee and meetings between myself as Chair of the audit committee and the lead audit engagement partner.	The audit plan for the year ending 31 December 2016 was presented to the audit committee in June 2016 and is summarised in the Independent Auditor's Report on pages 129 to 133.
A formal questionnaire issued to all audit committee members and senior Cairn management who are involved in the audit covering the robustness of the audit process, the quality of delivery, the quality of reporting and the quality of the auditor's people and service.	No matters of significance were reported.

Of particular focus for the Committee is the assessment of the judgement applied by PwC during each stage of the audit process including setting audit materiality, identifying the risks to the financial statements, evaluating audit findings and communicating those areas of judgement to the committee.

The audit committee noted the level of planned materiality and agreed on the levels of misstatements to be reported to the committee. The final audit report was presented to the audit committee in March 2017. After thorough discussion, the committee agreed with the conclusions that the auditors had reached noting the degree of judgement around the areas of significant audit risk.

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 at a reasonable cost. These advisers may include the Group's external auditors, under a restricted set of circumstances, 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 December 2016. Full details of the Group's policy can be found on the Company's website.

During the year, PwC provided other services including certification of the Group's EITI submission in Senegal and providing the accountant's report on the circular requesting approval for the sell-down of the Group's holding in Cairn India Limited should the current restriction be lifted.

A full analysis of remuneration paid to the Group's external auditor in respect of both audit and non-audit work is provided in note 6.4 to the financial statements.

Internal audit

Following a competitive tender process, Ernst & Young LLP (EY) were appointed as the Group's internal auditor with effect from July 2013. 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 88), the results of historical audits of fundamental business processes and the significant risks in the Group Risk Matrix and identified mitigation measures. The plan is then presented to the audit committee for review and approval. 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 Group Risk Management 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 and meet separately with the internal auditors to discuss areas of common focus in developing their audit plan.

Working responsibly – whistleblowing and related policies
The Group is committed to working responsibly as part of its strategy to deliver value for all stakeholders. This means delivering value in a safe, secure, environmentally and socially responsible manner.

As part of this the audit committee is responsible for ensuring the Group has a robust Whistleblowing Policy in place. This policy is reviewed regularly by the audit committee, with the last review in December 2016. An independent review of the Group's Whistleblowing Policy and procedures was also undertaken earlier in 2016.

The committee is also responsible for and 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. During 2016 a Group wide initiative was undertaken to provide a training update to all employees and long-term contractors in addition to the training that is provided to all new staff joining the company. Bespoke training was also provided to the Board during 2016. As Cairn enters new countries, further monitoring is undertaken and training is continued. Further information regarding these policies can be found on the Group's website.

IAIN MCLAREN
Chair of the audit committee
7 March 2017

Nomination Committee Report

The Nomination Committee

Members and meetings in 2016

Cairn recognises that the role of its nomination committee, working together with the Board as a whole, is key to promoting effective board succession and the alignment of board composition with the Company's culture, values and strategy. The Company reviewed the results of the work undertaken by the Financial Reporting Council in 2015 and 2016 in relation to UK Board succession planning and revisited the role of the Board and nomination committee in this context to ensure it remains appropriate.

	Member since	Meetings attended
Ian Tyler (Chairman)	05/14	
Simon Thomson	03/13	
Iain McLaren	03/13	
Keith Lough	05/15	
Peter Kallos	09/15	

The membership of the committee is set out in the corporate governance statement and comprises a majority of non-executive directors; the Chief Executive is also a member of the committee.

The role of the nomination committee includes:

- evaluating the balance of skills, knowledge, experience, diversity and independence on the Board;
- supporting the process for Board appointments and making recommendations to the Board in respect of new appointments;
- working with the Board to address any performance evaluation outcomes linked to Board succession planning; and
- oversight of the executive pipeline of talent beneath Board level.

Board changes

The Company appointed two new non-executive directors during 2015 and fully described the process for these appointments in last year's Corporate Governance Statement.

During 2016, the Company commenced a search for one additional new non-executive director resulting in the appointment of Nicoletta Giadrossi in January 2017. The Company instructed recruitment consultants Spencer Stuart in connection with this appointment. Spencer Stuart provided independent advice and services to the Company throughout the search, including the preparation of both a long and short list of candidates for consideration by the nomination committee.

All candidates on the short list were initially interviewed by the Chairman and Chief Executive following which Nicoletta Giadrossi was selected as the preferred candidate. Following selection and prior to her appointment, Nicoletta met individually with all other members of the Board and the Company Secretary in December 2016. The feedback from these meetings was very positive, as a result of which the nomination committee recommended to the Board that Nicoletta be appointed as a non-executive director of the Company and the proposed appointment was unanimously approved by the Board.

Prior to her appointment, Nicoletta was given the opportunity to, and subsequently did, carry out due diligence on the Company. She was also provided with the Company's induction pack for new directors (further details of the Company's induction process are included in the Corporate Governance Statement on pages 82 and 83). Nicoletta was appointed on 10 January 2017 and also became a member of the remuneration committee with effect from that date. She will seek re-election by shareholders at the AGM to be held on 19 May 2017.

Succession planning and development of executive pipeline
The nomination committee regularly evaluates the balance of skills, experience, independence and knowledge of the Company on the Board and makes recommendations to the Board as appropriate. In so doing, the committee fully supports the principle that any new appointments to the Board should be made on merit, against objective criteria, and with due regard for the benefits of diversity on the Board, including gender.

The Board and nomination committee work together with the aim of maintaining a comprehensive succession plan for appointments to the Board and to senior management, so as to maintain an appropriate balance of skills and experience within the Company and on the Board and to ensure progressive refreshing of the Board. The Company's succession planning also includes contingency plans for the sudden or unexpected departure of executive directors and other senior managers.

The Board has also carefully considered the significance of succession planning and human resource management to the Company's strategy and will be annually reviewing this at Board level.

The key positions covered in our succession plan include the executive directors, regional directors and a number of other senior functional and technical managers. The Board considered succession planning for each of the key positions, analysed any succession gaps or risks identified and considered how best to continue to develop the succession pipeline of executive talent. As a result, the Board has a deep understanding of succession planning across the Company and the range of measures being used to continue to develop and recruit talented senior employees.

During 2016, the Board's review of succession planning covered an executive summary, a review of the process used by the Company for succession planning, key achievements since the previous review, analysis of the succession plan for each key position over various time horizons, an organisational capability assessment and 'health-check', and actions being undertaken to address any succession risks or challenges identified.

Diversity
The nomination committee very much takes into account the benefits of diversity on the Board, including gender. Following the recent appointment of Nicoletta Giadrossi, the Company currently has two female non-executive directors (representing 20% of total membership) and the Board is very diverse in terms of the range of culture, nationality and international experience of its members. The directors' 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. The committee will further monitor and consider diversity for future Board appointments, whilst continuing to recruit on merit.

Beneath Board level, the Company also aims to develop and increase the number of women in senior management roles across the Group. There is currently one woman on the Senior Leadership Team (representing 14% of total membership) and there are two women on the Management Team (representing 20% of total membership).

The Company operates a range of measures which support diversity at Cairn, including succession planning, training and development, and flexible working policies. The pipeline of younger talent within the Group is also diverse and bodes well for the future.

Board and committee performance evaluation
The Board retains overall responsibility for implementation of its annual performance evaluation and the process and outcomes of the 2016 evaluation are described in the Corporate Governance Statement on pages 81 and 82. The process included a review of all Board committees and it was concluded that the relationship between the Board and its committees was functioning well, with all committees fully meeting their remit. The nomination committee works together with the Board in seeking to address any performance evaluation outcomes relating to Board composition and succession planning.

IAN TYLER
Chair of the nomination committee
7 March 2017

Directors' Remuneration Report

The Remuneration Committee
Members and meetings in 2016

	Member since	Meetings attended
Jackie Sheppard (Chair)	10/11	
Ian Tyler	06/13	
Iain McLaren	05/10	
Peter Kallos	09/15	

Part 1 – Annual statement from the Chair of the committee

Dear shareholder,

As the Chair of Cairn's remuneration committee, I am pleased to present our Directors' Remuneration Report for 2016. During the year, we continued to apply the executive remuneration policy that was originally put in place in 2014. However, as this policy will expire shortly, shareholders will be asked to approve a new framework for directors' pay at the forthcoming Annual General Meeting.

An overview of the new policy is set out below, with full details being provided in the Directors' Remuneration Policy that forms Part 2 of this report. Part 3 contains our Annual Report on Remuneration which identifies the various elements of pay that were actually delivered to the Company's directors during the year ended 31 December 2016; an overview of these items is also set out in this introductory statement.

At this year's AGM on 19 May 2017 shareholders will be asked to vote on the contents of the new Directors' Remuneration Policy – if approval is received, the policy will immediately become binding and it is anticipated that it will be operated during the remainder of 2017 and onwards until the 2020 AGM. Shareholders will also be invited to pass an advisory vote in relation to the Annual Report on Remuneration. The committee hopes that our shareholders will be supportive of both these resolutions.

Our new remuneration policy for 2017 and beyond
As highlighted in my introductory letter to last year's directors' remuneration report, the committee commenced its review of pay arrangements across the organisation during the course of 2015. This process has involved a critical examination of each element of executive compensation in the context of the following principles:

- **Alignment with strategy** – our remuneration policy should actively support an alignment with the Company's strategy and business model and should incentivise executives to deliver our long-term strategic objectives for the benefit of shareholders;
- **Simplicity** – our pay structures should be simple and transparent, thereby improving line of sight for participants and increasing clarity for investors; and
- **Best practice** – it is important that our remuneration arrangements appropriately reflect shareholders' expectations and include best practice themes as they develop.

Against this background, the committee has formulated a new remuneration framework which is intended to provide a better balance between driving short-term performance and rewarding long-term success. The restated policy does, however, maintain an emphasis on longer-term shareholder alignment and introduces a number of additional features that reflect changes to best practice since 2014.

Full details of the new policy are set out in Part 2 of this report; pages 123 and 124 also contains a summary of how it will actually be implemented in its first year of operation. However, the main differences between the revised approach and the Company's 2014 policy can be highlighted as follows:

Pay element	Current (2014) policy	New (2017) policy
Annual bonus	Bonus opportunity of up to 100% of salary with any amounts awarded to an individual being paid out immediately in full.	Maximum opportunity increased to 125% of salary. However, any bonus earned in excess of the previous 100% of salary limit will be deferred into Cairn shares for three years.
Long Term Incentive Plan – normal award limits	Awards based on relative Total Shareholder Return (TSR) normally limited to 300% of salary, plus a multiplier (see below) that can increase awards up to 400% of salary for outstanding absolute TSR performance.	Awards based on relative TSR limited to 200% of salary, plus a 'kicker' of 50% of salary for outstanding absolute performance (see below).
Long Term Incentive Plan – exceptional award limits	LTIP awards may be made up to 400% of salary (532% including multiplier) in exceptional circumstances (e.g. recruitment). No awards have been granted using this exceptional circumstances limit under the 2014 policy.	No ability to grant awards in excess of normal annual limits.
Long Term Incentive Plan – performance conditions	Vesting of awards based on relative TSR performance against a sector peer group, with 20% vesting for achieving a median ranking, rising on a straight-line basis to 100% vesting for upper decile performance. If an upper decile relative TSR is achieved, a multiplier of up to 1.33 applies to the award based on Cairn's absolute TSR performance.	For 2017, it is anticipated that two forms of LTIP award will be granted to each executive director, namely: • a 'core' award (200% of salary) – dependent on relative TSR performance against a comparator group, with 25% vesting for median ranking, rising on a straight-line basis to 100% vesting for achievement of upper quartile level; and • a 'kicker' award (50% of salary) – conditional on Cairn's TSR performance delivering at least 100% growth and an upper quartile comparator group ranking.
Long Term Incentive Plan – holding periods	A one year holding period applies to 50% of the shares over which an LTIP award vests.	A two year holding period will apply to all the shares in respect of which a 'core' or 'kicker' award vests.

Taken together, and as illustrated in the following table, the proposed changes will deliver a reduction in the overall maximum incentive opportunity available to executive directors:

	Maximum normal opportunity (as a % of base salary) under...	
Incentive arrangement	Current (2014) policy	New (2017) policy
Annual bonus	100%	125%
Long Term Incentive Plan – 'core' award	300%	200%
Long Term Incentive Plan – multiplier/'kicker' award	100%	50%
Total	**500%**	**375%**

The committee is aware that the combined effect of the above variations will be to increase the proportion of the overall remuneration policy that is directly linked to short term performance. Although we believe that this re-balancing is appropriate given the maturing nature of the business, we remain confident that there will continue to be a high level of alignment with long-term share price performance, particularly through the introduction of the new bonus deferral feature and the extended LTIP holding periods. In addition, and subject to the new policy being approved, the committee has decided that it will increase the shareholding guidelines which apply to executive directors from 100% of salary to 200%.

In order to give effect to certain elements of this revised approach to executive pay, it will also be necessary for the Company to establish a new Long Term Incentive Plan that will replace the corresponding arrangement that was adopted by shareholders in 2009. Full details of this plan (which requires the approval of shareholders prior to its introduction) are contained in the circular accompanying this year's notice of AGM.

As part of the process surrounding the design of our new policy, we consulted extensively with the Company's major investors and their representative bodies in order to understand their views on our proposed changes. Those we consulted with were generally supportive of the proposed changes, and certain suggestions made by these shareholders were included in the final structure set out in this report.

We firmly believe that the new policy described above represents a responsible and cohesive approach to executive remuneration that will support our strategy and appropriately reward our senior executives for delivering value to our shareholders.

Directors' Remuneration Report
continued

Remuneration in 2016
The work of the committee in 2016 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 balance sheet strength and financial flexibility.

Its key decisions relating to remuneration in 2016 are described in more detail in the Annual Report on Remuneration contained on pages 110 to 124 and can be summarised as follows:

Base salary increases
At its meeting in November 2016, the committee agreed that, with effect from 1 January 2017, a base salary increase of 1% would be applied to both the Company's executive directors (being Simon Thomson and James Smith).

The above increase was consistent with the level of standard annual salary increase awarded to other employees at that time.

Annual bonus
Based on an assessment of the extent to which the relevant targets were achieved during 2016, payments made under the annual bonus scheme to the executive directors during the year (as a percentage of annual salary) were 80.16% for Simon Thomson and 78.50% for James Smith. Further details of the way in which these awards were determined are set out on pages 114 to 117 of the Annual Report on Remuneration.

Long Term Incentive Plan (LTIP)
The performance period applicable to the LTIP awards granted in 2013 came to an end during 2016. Over this period, the Company's TSR was sufficient to place it above the median level in the applicable comparator group with the result that these awards vested in respect of 81.68% of the shares over which they were granted.

As part of the above vesting process, the LTIP's rules required the committee to review the Company's overall performance over the three years from the grant of the awards. After due and careful consideration, the committee concluded that there had been a sustained improvement in such overall performance during that time.

Non-executive directors' fees and Chairman's fee
During 2016 the committee reviewed the Chairman's annual fee in the context of market data and the time commitment for the role. Following this review the fee was increased from £160,000, as set on his appointment in May 2014, to £175,000 effective 1 January 2017.

The fees paid to non-executive directors were also reviewed during the year by the Board (excluding non-executive directors). Following this review it was determined that the basic annual fee would be maintained at £74,900. Similarly, no change was made to the additional fee payable for chairing the audit and/or remuneration committees.

Feedback on Directors' Remuneration Report
We welcome questions and feedback from all those interested on both the content and style of this report.

M. JACQUELINE SHEPPARD QC
Remuneration committee chair
7 March 2017

Part 2 – Directors' Remuneration Policy

Introduction
This Directors' Remuneration Policy provides an overview of the Company's policy on directors' pay that it is anticipated will be applied in 2017 and will continue to apply until the 2020 AGM. 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.

In accordance with the requirements of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (as amended) (the 'Regulations'), the policy contained in this part will be subject to a binding vote at the AGM to be held on 19 May 2017 and will take effect immediately upon receipt of such approval from shareholders.

As discussed in the Chair's introduction, the proposed policy includes a number of changes from the previous policy approved by shareholders at the 15 May 2014 AGM:

- Increased maximum annual bonus opportunity from 100% to 125% of salary.
- Introduction of annual bonus deferral for any bonus earned over 100% of salary. Deferral would be into Cairn shares for a three year period.
- Introduction of a replacement long-term incentive plan (the 2017 LTIP). Under this plan the total normal annual opportunity would be reduced from 300% of salary (400% including the absolute TSR multiplier) to 200% of salary (250% including the 'kicker'). For 2017 awards this would include up to 200% of salary for relative TSR performance and up to 50% of salary for a mix of absolute and relative TSR performance.
- Under the relative TSR element, the vesting schedule has changed from 20% vesting for median TSR performance and 100% for upper decile TSR performance to 25% vesting for median TSR performance and 100% for upper quartile TSR performance.
- The absolute TSR element will be made more challenging and will only vest if the Company's relative TSR is at least upper quartile and three year absolute TSR performance is at least 100%. Under the 2014 policy, the multiplier started to apply if the relative TSR hurdle had been achieved and if absolute three year TSR performance was at least 50%.
- The holding period has been strengthened so that all vested shares (whether arising from the relative or absolute TSR elements) are subject to a two year holding period.

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 the PDMRs;
- determining the level of awards made under the Company's LTIPs and employee share award schemes and the performance conditions which are to apply;
- determining the KPIs used to measure performance for the annual bonus scheme;
- determining the bonuses payable under the Company's annual bonus scheme;
- determining the vesting levels of awards under the Company's LTIPs and employee share award schemes; 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.

The 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 and regulatory 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 mandate, it takes into account the views and opinions of all the relevant stakeholders in the business.

During 2016, 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 their views on a number of proposed changes to the executive directors' remuneration arrangements. Shareholders were given an early opportunity to raise any questions. In developing these proposed changes the committee was minded to include a number of features, such as bonus deferral, extended holding periods for LTIP awards and increased shareholding guidelines, which are aligned with shareholders' interests.

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 regularly given the opportunity to raise issues on a variety of matters, including executive pay, via a number of mechanisms.

Directors' Remuneration Report
continued

Overview of proposed remuneration policy
Cairn's policy on executive directors' remuneration for 2017 and subsequent financial years is to ensure that it appropriately incentivises individuals to achieve the Group's strategy to deliver value for stakeholders by building and maintaining a balanced portfolio of exploration, development and production assets, whilst offering a competitive package against the market.

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

Policy Table – elements of directors' remuneration package

Remuneration element	Purpose and link to strategy	Operation	Opportunity	Framework for assessing performance
Base salary	Helps recruit and retain employees. Reflects individual experience and role.	Normally reviewed annually (with changes taking effect on 1 January) and/or when otherwise appropriate, including when an individual changes position or responsibility. 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). Decision influenced by: • role and experience; • average change in broader workforce salaries; • individual performance; and • remuneration practices in companies of a broadly similar size and value and relevant oil and gas exploration and production companies.	Whilst the committee has not set a monetary maximum, 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: • an increase in the scope and responsibility of the individual's role; or • the individual's development and performance in the role following appointment; or • a re-alignment with market rates.	None
Benefits	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. The committee reserves the right to provide further benefits where this is appropriate in the individual's particular circumstances (for example costs associated with relocation as a result of the director's role with the Company). Executive directors are also eligible for other benefits which are introduced for the wider workforce on broadly similar terms.	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. Whilst the committee has not set a monetary maximum for other benefits, they will be in line with the market as determined by the committee.	None

Remuneration element	Purpose and link to strategy	Operation	Opportunity	Framework for assessing performance
Annual bonus	Rewards the achievement of annual KPIs and/or other objectives linked to the Company's strategic goals.	Bonuses are awarded by reference to performance against specific targets measured over a single financial year. Any amounts awarded to an individual under this arrangement up to 100% of salary are paid out in full shortly after the assessment of the performance targets has been completed. The remainder of the bonus will be deferred into an award of shares for a three year period, or such other period as determined by the committee. Annual bonuses may be subject to clawback, and the extent to which deferred share awards vest may be reduced, 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 which, had it been known at the relevant time, would have reasonably been expected to have resulted in a lower award being made.	Maximum % of salary: 125%.	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. All, or a significant majority, of the bonus opportunity will normally be determined by reference to performance against demanding Group KPIs such as: • exploration and new venture objectives; • development and production targets; and • HSE. 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. A payment scale (ranging from 0% to 100% of the opportunity) for different levels of achievement against each KPI and/or other objective is specified by the committee at the outset of each year. 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. 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.

Directors' Remuneration Report
continued

Remuneration element	Purpose and link to strategy	Operation	Opportunity	Framework for assessing performance
2017 Long Term Incentive Plan (or 2017 LTIP)	Incentivises executive directors to deliver long-term performance for the benefit of shareholders, thereby aligning the interests of the directors with those of the Company's investors.	Cairn is seeking shareholder approval for a new LTIP at the 2017 AGM. Awards will normally be made annually with vesting dependent on achievement of performance conditions chosen by the committee that are measured over a period of at least three years. All awards which vest will normally be subject to a holding period in terms of which the relevant shares will only be released/become exercisable after a further period of at least two years has expired from the vesting date. The committee reviews the quantum of awards annually, taking into account factors such as market rates and overall remuneration. 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 which, had it been known at the relevant time, would have reasonably been expected to have resulted in a lower vesting being determined.	Normal total maximum % of salary: 250%.	Vesting of awards granted under the 2017 LTIP will be determined by the growth in Total Shareholder Return (TSR) of Cairn over a performance period of at least three years. Awards up to 200% of salary (the 'core award') will be subject to TSR performance measured relative to a comparator group selected by the committee, with no more than 25% vesting at median and 100% for at least upper quartile performance. In order to focus on exploration success which leads to a material increase in the share price, once performance for the 'core award' has been fully achieved, an additional element of up to 50% of salary can be earned if absolute TSR growth over the same performance period equals or exceeds 100% (the 'kicker award'). No part of any award will vest unless the 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. Although the committee's intention is that the above conditions will be applied to LTIP awards granted in 2017, 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.

Remuneration element	Purpose and link to strategy	Operation	Opportunity	Framework for assessing performance
2009 Long Term Incentive Plan (or 2009 LTIP)	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.	It is not proposed that further awards will be granted to executive directors under this plan. Awards vest dependent on achievement of performance conditions measured over a three-year period. On vesting of an award, 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. 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.	Normal maximum % of salary: 300% (400% including multiplier). Exceptional circumstances maximum % of salary: 400% (532% including multiplier).	Vesting 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. 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). It also states that no part of any award will vest unless the 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.
Share Incentive Plan (or SIP)	Encourages a broad range of employees to become long-term shareholders.	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: • partnership shares acquired using deductions from salary; • matching shares awarded to those employees who purchase partnership shares on the basis of a ratio specified by the Company; and • free shares. Matching and free shares awarded under the SIP must normally be held in the plan for a specified period.	Participation limits are those set by the UK tax authorities from time to time. These limits are currently as follows: • Partnership shares: up to £1,800 per tax year can be deducted from salary. • Matching shares: up to two matching shares for every one partnership share purchased. • Free shares: up to £3,600 worth in each tax year.	None

Directors' Remuneration Report
continued

Remuneration element	Purpose and link to strategy	Operation	Opportunity	Framework for assessing performance
Pension	Rewards sustained contribution.	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. The Company contributes a specified percentage of basic annual salary for senior employees, including executive directors. Where an executive director has an individual personal pension plan (or overseas equivalent), the Company pays its contribution to that arrangement. 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.	Company contributes 15% of basic salary on behalf of executive directors or pays them a cash equivalent.	None
Non-executive directors' fees	Helps recruit and retain high-quality, experienced individuals. Reflects time commitment and role.	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: • market practice; • time commitment; and • responsibilities associated with the roles. Additional fees are payable to the Chairs of the audit and remuneration committees. Expenses incurred in the performance of non-executive duties for the Company may be reimbursed or paid for directly by the Company, including any tax due on the expenses.	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

Remuneration element	Purpose and link to strategy	Operation	Opportunity	Framework for assessing performance
Chairman's fees	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. Expenses incurred in the performance of the Chairman's duties for the Company may be reimbursed or paid for directly by the Company, including any tax due on the expenses.	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 2017 is provided on pages 123 and 124.

2 The following differences exist between the Company's above policy for the remuneration of directors and its approach to the payment of employees generally:
- Participation in the LTIPs is typically aimed at the executive directors and certain selected senior managers. Other employees are eligible to participate in the Employee Share Award Scheme (details of which are provided on pages 158 and 159.
- 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 2017 LTIP and 2009 LTIP (further details of which, in the latter case, are provided on page 118) were selected by the 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 2009 LTIP or 2017 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 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 currently not appropriate to apply performance conditions to free shares awarded under it, although the committee retains the discretion to apply performance conditions to future awards.

Common terms of share awards

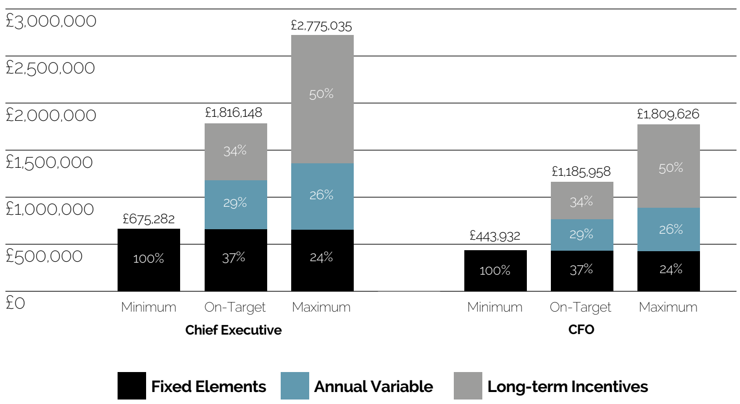
Awards under any of the Company's discretionary share plans referred to in this report may:
- be granted as conditional share awards or nil-cost options or in other such form that the committee determines has the same economic effect;
- have any performance conditions applicable to them amended or substituted by the committee if an event occurs which causes the committee to determine an amended or substituted performance condition would be more appropriate and not materially less difficult to satisfy;
- incorporate the right to receive an amount (in cash or additional shares) equal to the value of dividends which would have been paid on the shares under the award that vest up to the time of vesting (or, where the award is subject to a holding period, release). This amount may be calculated assuming that the dividends have been reinvested in the Company's shares on a cumulative basis;
- be settled in cash at the committee's discretion; and
- be adjusted in the event of any variation of the Company's share capital or any demerger, delisting, special dividend or other event that may affect the Company's share price.

Legacy awards

The committee reserves the right to make any remuneration payments and/or payments for loss of office (including exercising any discretions available to it in connection with such payments) notwithstanding that they are not in line with the policy set out above where the terms of the payment were agreed (i) before 15 May 2014 (the date the Company's first shareholder-approved directors' remuneration policy came into effect); (ii) before the policy set out above came into effect, provided that the terms of the payment were consistent with the shareholder-approved directors' remuneration policy in force at the time they were agreed; or (iii) at a time when the relevant individual was not a director of the Company and, in the opinion of the committee, the payment was not in consideration for the individual becoming a director of the Company. For these purposes 'payments' includes the committee satisfying awards of variable remuneration and, in relation to an award over shares, the terms of the payment are 'agreed' at the time the award is granted.

Directors' Remuneration Report
continued

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 current executive directors in 2017 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 the executive directors are entitled in 2017 irrespective of performance levels, namely base salary (at current rates), benefits (using the details set out in the 2016 single-figure table provided on page 112) 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 2017 LTIP. Given that neither of these incentive arrangements explicitly stipulate an 'on-target' amount, the assumed levels for this scenario are:
  - in the case of the LTIP, for on-target performance the 'kicker' award would not vest. Therefore the illustration is based on 55% vesting of the 'core award' of 200% of salary. This vesting level is broadly equal to the percentage applied in determining the grant date 'fair value' of an LTIP award for the purposes of the Company's share-based payment charge; and
  - in the case of the annual bonus, a payout of 75% of maximum opportunity (being the approximate average of such payouts for all executive directors over the five years up to and including 2016).
- The 'maximum' columns demonstrate total remuneration levels in circumstances where the variable elements pay out in full, namely an annual bonus payment of 125% of salary (with 100% of salary paid in cash and the balance delivered in the form of a deferred share award) and 100% vesting of LTIP awards to be granted in 2017 over shares worth 250% of salary.
- For the purposes of valuing the LTIP and deferred bonus 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.

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 reasonable 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.

Chairman and non-executive directors

On the appointment of a new Chairman or non-executive director, the fees will be set taking into account a range of relevant factors including market practice, time commitment and the responsibilities associated with the role. 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	• Salary, pension and benefits. • Company car or cash allowance. • Permanent health insurance. • Private health insurance for director and dependants. • Death-in-service benefits. • 30 days' paid annual leave. • Participation in annual bonus plan, subject to plan rules. • Participation in deferred bonus, LTIP and SIP, subject to plan rules.
Notice period[1]	• 12 months' notice by the director or by the Company.
Termination payment	• See separate disclosure below.
Restrictive covenants	• During employment and for 12 months after leaving.

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.

Exit payment policy for executive directors

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. The committee will have the authority to settle legal claims against the Group (e.g. for unfair dismissal, discrimination or whistle blowing) that arise on termination. The committee may also authorise the provision of outplacement services and pay reasonable legal expenses associated with the termination.

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 (in cash and/or share awards as determined by the committee) 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 share awards granted pursuant to the Company's deferred bonus arrangements will lapse immediately. However, if such cessation occurs by reason of death, injury, permanent disability, or because the individual's employing company or part of the business in which he/she is employed is transferred out of the Group, retirement with the agreement of the Company, or in any other circumstances determined by the committee other than where an individual has been summarily dismissed (in each case, a 'good leaver'), those awards will not lapse and will normally continue to vest at the end of the original vesting period. The committee may determine that a deferred bonus award should vest before the normal time in certain circumstances, for example where an individual has died. The committee also has the discretion to time pro-rate any awards held by such a good leaver.

As a general rule, if an executive director ceases employment, all unvested awards granted pursuant to the Company's long-term incentive arrangements under the 2009 LTIP and 2017 LTIP will lapse immediately. However, if such cessation occurs by reason of death, injury, permanent disability (or, for 2009 LTIP awards, 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 normally 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. The committee may determine that an award should vest before the normal time in certain circumstances, for example where an individual has died. 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. Any holding period attached to the share awards would normally continue to apply.

If an executive director ceases employment, 2017 LTIP awards subject to a holding period will normally be released (or if structured as nil-cost options, become exercisable) on the original timescales. These awards will, however, lapse where cessation occurs due to the individual's gross misconduct, or if the committee considers it appropriate, the individual's bankruptcy. The committee has the discretion to accelerate the release of shares in certain circumstances, for example death. For 2009 LTIP awards subject to a holding period at the time an executive director ceases employment, awards will normally be released on cessation of employment.

Directors' Remuneration Report
continued

On a change of control of the Company resulting in the termination of his employment, the current Chief Executive is entitled to compensation of a sum equal to his annual basic salary as at the date of termination of employment. As noted and explained in previous reports, the committee recognises that this provision is no longer in accordance with best practice. It was not included in the contract of the CFO that was entered into on his appointment in 2014, and will not be included in the contracts of other future appointees to the Board; however, it continues to apply to the current Chief Executive.

In the event of a change of control or winding up of the Company, treatment of share awards will be in accordance with the relevant plan rules. The committee has the discretion to disapply time pro-rating in the event of a change of control.

If there is a demerger or special dividend, the committee may allow awards to vest on the same basis as for a change of control.

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.

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 2016 and explains how Cairn's approved Directors' Remuneration Policy that was in force during that period was implemented. It also summarises how the new Directors' Remuneration Policy set out on pages 101 to 110 will be applied in 2017, assuming it is approved by shareholders at the AGM to be held on 19 May 2017.

In accordance with the Regulations, this part of the report will be subject to an advisory vote at the above noted AGM.

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 2016
Members of the remuneration committee
The members of the remuneration committee during the year were as follows:

- M. Jacqueline Sheppard QC (Chair of the committee);
- Iain McLaren;
- Ian Tyler; and
- Peter Kallos.

The individuals who served on the committee, each of whom is an independent non-executive director of the Company, 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 76 and 77 and details of attendance at the committee's meetings during 2016 are shown on pages 86 and 98.

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. The Chief Executive is not involved in any discussions in respect of his own remuneration. During the year, the committee also received material assistance and advice on remuneration policy from the Company Secretary.

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 2016	Fees for committee assistance in 2016[1]	Other services provided to the Company during 2016
New Bridge Street[2,3]	Appointed by the committee to give periodic advice on various aspects of the directors' remuneration packages. Also assisted with the preparation of the Directors' Remuneration Report and provided support on a number of miscellaneous remuneration related projects (including the formulation of the new policy).	£54,797	None
Deloitte LLP[3]	Appointed by the Company's management team but provided assistance to the committee in relation to the design, communication and implementation of the new policy.	£74,943	Provided advice on various aspects of remuneration practice across the Group.
Ernst & Young LLP	Appointed by the Company to carry out an independent verification of its achievement against performance conditions applicable to the Company's LTIPs and share option schemes.	N/A – no advice provided to the committee	Internal auditors of the Company throughout the year.
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.	£28,019	General legal services to the Group throughout the year.

Notes:

1 The bases for charging the fees set out in the 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.

3 Both New Bridge Street and Deloitte LLP are members of the Remuneration Consultants Group and their work is governed by the Code of Conduct in relation to executive remuneration consulting in the UK.

4 The committee reviews the performance and independence of all its advisers on a continuous basis.

Statement of shareholder voting at general meetings

The table below shows the voting outcome at the last general meeting(s) at which shareholders were asked by the Company to approve a resolution relating to its Directors' Remuneration Report and Directors' Remuneration Policy:

Description of resolution	Date of general meeting	Number of votes 'For' and 'Discretionary'	% of votes cast	Number of votes 'Against'	% of votes cast	Total number of votes cast	Number of votes 'Withheld'[1]
To approve the 2015 Directors' Remuneration Report	12 May 2016	423,241,645	98.80%	5,138,296	1.20%	428,379,941	26,717,122
To approve Directors' Remuneration Policy	15 May 2014	379,512,480	98.06%	7,495,533	1.94%	387,008,013	1,045,923

Note:

1 A vote withheld is not a vote in law.

The committee welcomed the endorsement of both the above resolutions that was shown by the vast majority of shareholders and gave due consideration to any concerns raised by investors who did not support the resolutions.

Payments to past directors during 2016 (audited)

Dr Mike Watts and Jann Brown stood down as executive directors on 15 May 2014 and subsequently ceased employment with the Group on 17 October 2014. As explained in the Annual Report on Remuneration for the year ended 31 December 2014, both of these individuals were treated as 'good leavers' for the purposes of the Company's incentive schemes and were, therefore, allowed to retain their outstanding awards under the 2009 LTIP (subject to time pro-rating). Details of these awards that vested and/or were exercised during 2016 have been included in the relevant sections of this part of the report.

No other payments were made to past directors during the year to 31 December 2016.

Directors' Remuneration Report
continued

Single total figure table for 2016 (audited)

The tables below set out the remuneration received by executive directors and non-executive directors during the year in the following categories.

Salary + Benefits + Pension + SIP + Bonus + Long-Term Incentive = **Total Remuneration**

Executive directors

		Fixed elements of pay					Pay for performance			
	Financial year	Salary and fees	Benefits[1]	Pension[2]	SIP[3]	Fixed element subtotal	Bonus[4]	Long-term incentives[5]	Performance element subtotal	Total remuneration
Directors										
Simon Thomson	**2016**	**£554,390**	**£31,358**	**£83,159**	**£7,200**	**£676,107**	**£444,399**	**£961,095**	**£1,405,494**	**£2,081,601**
	2015	£546,197	£29,217	£81,930	£7,200	£664,544	£409,648	£217,975	£627,623	£1,292,167
James Smith	**2016**	**£360,579**	**£25,119**	**£54,087**	**£7,196**	**£446,981**	**£283,055**	**–**	**£283,055**	**£730,036**
	2015	£355,250	£27,840	£53,288	£7,200	£443,578	£266,438	–	£266,438	£710,016

Notes:

1 Taxable benefits available to the executive directors during 2016 were a company car/car allowance, private health insurance, death-in-service benefit and a gym and fitness allowance. This package of taxable benefits was unchanged from 2015.

2 Additional disclosures relating to the pension provision for the executive directors during 2016 are set out on page 114.

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 2016 are set out on page 121.

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 scheme for 2016 is provided on pages 114 to 117.

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 2016 are provided on pages 117 to 121.

6 Following the end of the year to 31 December 2016, 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 not aware of any such circumstances.

Non-executive directors

		Fixed elements of pay				Pay for performance			
	Financial year	Salary and fees[1]	Benefits	Pension[2]	Fixed element subtotal	Bonus[2]	Long-term incentives[2]	Performance element subtotal	Total remuneration
Directors									
Ian Tyler	**2016**	**£160,000**	**–**	**–**	**£160,000**	**–**	**–**	**–**	**£160,000**
	2015	£160,000	–	–	£160,000	–	–	–	£160,000
Todd Hunt	**2016**	**£74,900**	**–**	**–**	**£74,900**	**–**	**–**	**–**	**£74,900**
	2015	£74,900	–	–	£74,900	–	–	–	£74,900
Iain McLaren	**2016**	**£84,900**	**–**	**–**	**£84,900**	**–**	**–**	**–**	**£84,900**
	2015	£84,900	–	–	£84,900	–	–	–	£84,900
Alexander Berger	**2016**	**£74,900**	**–**	**–**	**£74,900**	**–**	**–**	**–**	**£74,900**
	2015	£74,900	–	–	£74,900	–	–	–	£74,900
M. Jacqueline Sheppard QC	**2016**	**£84,900**	**–**	**–**	**£84,900**	**–**	**–**	**–**	**£84,900**
	2015	£84,900	–	–	£84,900	–	–	–	£84,900
Keith Lough	**2016**	**£74,900**	**–**	**–**	**£74,900**	**–**	**–**	**–**	**£74,900**
	2015[3]	£47,341	–	–	£47,341	–	–	–	£47,341
Peter Kallos	**2016**	**£74,900**	**–**	**–**	**£74,900**	**–**	**–**	**–**	**£74,900**
	2015[3]	£25,555	–	–	£25,555	–	–	–	£25,555

Notes:

1 The annual fee for each of the non-executive directors (other than the Chairman) for 2016 was £74,900. In addition, a further annual fee of £10,000 was payable to both Iain McLaren and M. Jacqueline 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 Keith Lough and Peter Kallos were appointed as directors on 14 May 2015 and 1 September 2015 respectively. Their fees for 2015 reflect the period from those dates to the year end.

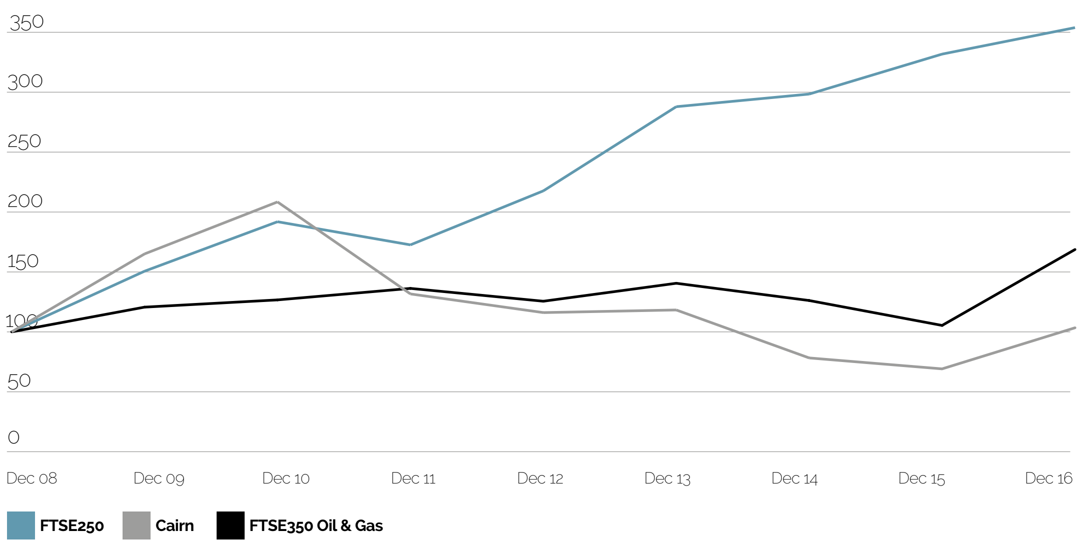
TSR performance graph and further information on Chief Executive pay

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 350 Oil & Gas Producers Index over the last eight years. These comparisons have been chosen on the basis that: Cairn was a constituent member of the FTSE 250 Index for the whole of 2016; and the FTSE 350 Oil & Gas Producers Index comprises companies who are exposed to broadly similar risks and opportunities as Cairn.

The table beneath the graph illustrates the movements in the total remuneration of the Company's Chief Executive during the same eight-year period.

Performance graph – comparison of eight-year cumulative TSR on an investment of £100



Total remuneration of Chief Executive during the same eight-year period

Financial year	Chief Executive	Total remuneration of Chief Executive[1]	Annual variable element award rates for Chief Executive (as % of max. opportunity)	Long term incentive vesting rates for Chief Executive (as % of original award level)
2016	Simon Thomson	£2,081,601	80.2%	81.7%
2015	Simon Thomson	£1,292,167	75%	23.4%
2014	Simon Thomson	£1,073,425	78.5%	0%
2013	Simon Thomson	£962,765	63%	0%
2012	Simon Thomson	£1,018,570	86%	0%
2011	Simon Thomson	£3,405,719	82%	121%
2011[2]	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:

1 The amounts disclosed 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 112.

2 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).

Directors' Remuneration Report
continued

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 2016 remuneration package, the percentage change from 2015 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	% change in annual bonus
Chief Executive	1.50%	7.33%[1]	8.48%
All Group employees	1.92%[2]	0.01%	14.83%

Notes:
1 The above increase in the Chief Executive's taxable benefits is largely attributable to a rise in the costs of his company car provision for 2016.
2 The standard level of salary increase across the Group in 2016 was 1.5%. However, a small number of individuals received higher percentage increases which raised the average for all employees to 1.92%.

Executive directors' base salaries during 2016
Based on a review carried out in December 2015, the following salary increases for executive directors became effective on 1 January 2016:

2016 Annual salary details

	Job title	Annual salary as at 31 December 2015	**Annual salary as at 1 January 2016**	% increase with effect from 1 January 2016
Current directors				
Simon Thomson	Chief Executive	£546,197	**£554,390**	1.5%
James Smith	CFO	£355,250	**£360,579**	1.5%

The increases shown in the above table for both Simon Thomson and James Smith were consistent with the level of standard annual salary increase awarded to other employees on 1 January 2016.

Executive directors' pension provision during 2016 (audited)
As highlighted in the Directors' Remuneration Policy described on pages 101 to 110, 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.

James Smith is a member of the Company scheme and, during the year, received Company contributions up to his statutory annual allowance. The balance of his 15% of basic salary entitlement was paid as additional salary.

During the year, Simon Thomson received an amount equal to 15% of his annual basic salary in the form of additional salary as his pension arrangements have already reached the relevant lifetime limit.

Details of the actual amounts of pension contributions/additional salary that were paid to the executive directors during 2016 are set out in the 'pension' column of the single total figure table on page 112.

Annual bonus – 2016 structure and outcome (audited)
During 2016, Cairn operated annual cash bonus schemes for all employees and executive directors. The maximum level of bonus award for executive directors and certain PDMRs for 2016 was 100% of annual salary (as at date of award).

For all participants other than the executive directors, 2016 bonus awards were based on individual, project-based and Company performance measures. Individual and project-based performance was measured through the Company's performance management system and Company performance conditions were based on annually defined KPIs.

As highlighted in last year's Annual Report on Remuneration, 90% of each executive director's bonus opportunity for 2016 was determined by reference to the extent to which certain Group KPIs were achieved, with the remaining 10% being dependent on the satisfaction of personal objectives. Taking into account commercial sensitivities around disclosure, a summary of the relevant targets, ascribed weightings and achievement levels is set out below.

2016 annual cash bonus scheme – Group KPI performance conditions (90% weighting) and achievement levels

KPI measures and performance achieved in 2016				Weighting	Bonus awarded
Purpose	2016 KPI	Measurement	2016 performance	(as % of allocated proportion of maximum opportunity)	
Deliver exploration and appraisal success					
Grow the reserves and resources base to provide a basis for future growth.	Progress the Senegal SNE discovery through the prudent investment of capital funds, de-risking the path to commerciality in a cost-effective and timely manner.	• 2C resource valuation; • 3C/1C ratio; and • Cumulative E&A investment divided by the 2C resources (US$/bbl).	• Four wells successfully drilled and evaluated on the SNE field for a cost within the original three well budget; • Net resources upgraded from 155.1 mmboe to 201.4 mmboe at year-end; • P10/P90 gross resources ratio narrowed; and • E&A investment level at <US$4/bbl.	24%	21.75%
	Discover commercial hydrocarbons.	• Invest E&A funds within budgetary guidance to add new volumes at industry-leading finding costs.	• Bellatrix-1 exploration and appraisal well discovered gas in shallower horizons; and • Laverda exploration well encountered 13ft net oil pay in a single Tay sand with recoverable P50 volumes estimated at 2-3 mmbbls.	5%	
Portfolio management					
Active portfolio management.	Develop an inventory of exploration and appraisal opportunities, including prospects and leads which meet Cairn's technical and commercial criteria and can provide drilling opportunities for the period 2017 onwards.	• Secure or mature four or more new independent opportunities from within or outwith the portfolio that meet the business's investment criteria.	• Awarded seven blocks, including two as operator, in the Norwegian 2016 Licence Round; • Farm-in to the Aurelia prospect in the Barents Sea. The well failed on reservoir quality and hydrocarbon type; and • Award of one licence option in 2015 Atlantic Margin Oil and Gas Exploration Licensing Round in the Porcupine Basin, offshore Ireland.	16%	10%

Directors' Remuneration Report
continued

2016 annual cash bonus scheme – Group KPI performance conditions (90% weighting) and achievement levels continued

KPI measures and performance achieved in 2016				Weighting	Bonus awarded
Purpose	2016 KPI	Measurement	2016 performance		(as % of allocated proportion of maximum opportunity)
Deliver operational excellence					
Deliver operational excellence in all 2016 activities.	Deliver all operated and non-operated E&A projects on schedule and budget, with full data recovery.	• Projects and products delivered to the quality required, on schedule and within budget.	• Four wells successfully drilled and evaluated on the SNE field for the original budgeted price of three; • Sangomar-Rufisque 3D seismic processing on schedule for delivery in Q1 2017; • Boujdour Maritime final interpreted volume for the merged 7,000km^2 completed; and • Final interpreted volumes for the Horda 3D in Norway and the West of Kraken 3D in the UK.	20%	17.55%
	Progress North Sea development projects, on time and budget.	• Ensure projects remain within capital guidance and first oil schedule remains within base case estimates with key milestones met.	• Kraken development remains on schedule with first oil anticipated in H1 2017. The latest capex estimate is >US$300 million or over 10% lower than the sanction estimate; • Key Kraken milestones set for 2016 have been accomplished including the completion of four producer and four injector wells; full subsea installation; the Safety Case was approved; and the FPSO left Singapore for UK waters; • Operator is targeting first oil in H2 2017 on Catcher; • Significant progress has been made on Catcher including the completion of eight wells, with further drilling ongoing. Substantial completion of the offshore installation and the FPSO hull has been delivered and fabrication of the topside modules is progressing well; and • Provided input and assurance to Operator on concept selection decision on Skarfjell.		
Maintain licence to operate (including HSE performance)					
Deliver value in a safe, secure and environmentally and socially responsible manner.	Minimise injuries and environmental incidents in 2016 operated activities: • Total Recordable Injury Rate (TRIR) target of less than 2.0 TRI/million hours. • No oil spills to the environment.	• TRIR of less than 2.0 TRI/million hours; and • Oil spills to the environment.	• TRIR of 1.05; and • Approximately 1 bbl of oil was released to the environment during testing of SNE appraisal wells in Senegal.	15%	11.6%
	Achieve targets for HSE leading performance indicators (LPIs) linked to elements of the HSE culture framework.	• Progress against HSE LPIs; and • Further embedding of HSE culture and behaviours.	• Improvements made to the CRMS with revision of CR policies, emergency and business continuity plans and travel risk assessments, security and support; • OSPAR reverification completed without issue; and • Work ongoing on HR People Management Manual and roll out of management training.		

2016 annual cash bonus scheme – Group KPI performance conditions (90% weighting) and achievement levels continued

KPI measures and performance achieved in 2016				Weighting	Bonus awarded
Purpose	2016 KPI	Measurement	2016 performance	(as % of allocated proportion of maximum opportunity)	
Deliver a sustainable business (maintain liquid reserves)					
Maintain a self-funding business plan.	Maintain liquid reserves including undrawn committed banking facilities to meet planned funding commitments plus a cushion at all times.	• Development of a funding strategy to ensure ability to execute value-generative plan, maintaining liquid reserves to meet planned commitments, whilst retaining a funding cushion.	• Funding headroom cushion maintained at all times; and • Significant cost reductions or deferrals achieved from original 2016 work programme will allow enlarged drilling programme and pursuit of new venture opportunities to be fully funded.	20%	18%
	Make tangible progress on Cairn India Limited (CIL) shares freeze by progress of action under the UK-India Investment Treaty.	• Milestones in the arbitration including filing of the Statement of Claim and India's filing of its Statement of Defence.	• Statement of claim submitted on schedule; • India's statement of defence submitted in February 2017; and • Agreement of Indian tax office in December 2016 that dividends are not restricted.		
Totals				**100%**	**78.9%**

2016 annual cash bonus scheme – individual performance conditions (10% weighting) and achievement levels

In early 2016, an external third party provider carried out a 360 degree review of each executive director. The personal objectives for each executive director for the year were developed from the personal development plans which were prepared following the conclusion of the review. In summary, these objectives related to a mixture of professional development, communication and leadership skills relating to the delivery of the key strategic targets of the business for the year.

Performance against the above objectives was assessed in early 2017 by means of interviews of the participants in the original 360 degree review. The report and recommendations were carefully considered by the committee, following which it determined that they had been achieved at a level of 91.5% in the case of Simon Thomson and 74.9% in the case of James Smith.

2016 annual cash bonus scheme – overview of awards and actual payments made

The application of the outturn from the above performance condition assessments resulted in the following bonuses becoming payable to Simon Thomson and James Smith:

		Simon Thomson		James Smith	
		Group KPI measures	Individual conditions	Group KPI measures	Individual conditions
Award elements	Weighting (as % of salary)	90%	10%	90%	10%
	x				
	Achievement level	78.90%	91.50%	78.90%	74.90%
	=				
	Award (as % of salary)	71.01%	9.15%	71.01%	7.49%
Total award	(as % of salary)	80.16%		78.50%	
	(as an amount)	£444,399		£283,055	

The remuneration committee considered that the above final award levels were appropriately reflective of overall performance during the year.

Long-term incentives during 2016

Introduction

During the year to 31 December 2016, the executive directors participated in the Company's 2009 LTIP, which was originally approved by shareholders at the AGM held on 19 May 2009.

The 2009 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.

Directors' Remuneration Report
continued

Long-term incentives during 2016 continued

Introduction continued

In the case of all awards under the 2009 LTIP (including those granted during 2013, 2014, 2015 and 2016), 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 2009 LTIP awards that were outstanding during 2016 is set out on pages 120 and 121.

In order to ensure that the 2009 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 under the 2009 LTIP 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, 2009 LTIP awards 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 which, had it been known at the relevant time, would have reasonably been expected to have resulted in such lower vesting being determined.

On any vesting of an award under the 2009 LTIP, 50% of the ordinary shares to which the holder has become entitled are released or become exercisable immediately, with the remaining 50% normally being released or becoming exercisable after a further period of one year.

LTIP – awards granted during 2016 (audited)

On 16 March 2016, the following awards under the LTIP were granted to executive directors:

						Face value (£'000) of ...		
	Type of award	Basis of award granted	Share price at date of grant[3]	No. of shares over which award originally granted	% of shares over which award originally granted that vest at threshold	...shares over which award originally granted[4]	...max. no. of shares to vest if all performance measures met[5]	Vesting determined by performance over
Directors								
Simon Thomson	Nil-cost option	3 x base salary of £554,390	£1.9407	856,994	20%	£1,663	£2,212	3 years until 15 March 2019
James Smith	Nil-cost option	3 x base salary of £360,579	£1.9407	557,395	20%	£1,082	£1,439	3 years until 15 March 2019

Notes:

1 Details of the performance conditions applicable to the awards granted in 2016 are provided above.

2 No price is payable by participants for their shares on the exercise of a nil-cost option granted under the LTIP.

3 This figure represents the average of the closing mid-market prices of a share in the Company over the three dealing days preceding the date of grant. (The actual closing price on 16 March 2015 was £2.045.)

4 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'.

5 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) and multiplying the result by the 'share price at date of grant'.

LTIP – awards vesting during the year (audited)

On 19 March 2016, the three-year performance period applicable to the awards granted under the 2009 LTIP on 20 March 2013 to various participants (including current and former executive directors) came to an end. Thereafter, the remuneration committee assessed the relevant performance conditions. The results of this assessment, which was completed on 22 March 2016, can be summarised as follows:

Performance measure	% of award subject to measure	Performance achieved 2013–2016	% 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/ absolute TSR performance.	100%	Cairn's TSR over the period placed it between the 3rd and 4th ranked companies in the comparator group. After careful consideration of a variety of factors, the committee also concluded that there had been a sustained improvement in the overall performance of the Company over the three years in question.	81.68%

Notes:

1 Further details of the performance conditions that applied to the above awards are set out on page 118.

2 At various points in the period 20 March 2013 to 19 March 2016, the committee was required to determine (in accordance with the approved remuneration policy in place at that time) 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 TSR calculations used to inform the committee's determinations in relation to the above awards were independently verified by Ernst & Young LLP.

The following table shows, for each current and former director, details of the 2009 LTIP awards that vested during the year:

	Type of award	Date of grant	No. of shares over which award originally granted	Date of vesting	% of award to vest as per performance condition assessment	No. of shares that vested (after taking account of any time pro-rating requirements)[1]	Value of shares vesting[2]
Current director[3]							
Simon Thomson	Nil-cost option	20 March 2013	565,732	22 March 2016	81.68%	462,065	£961,095
Former directors							
Jann Brown[4]	Nil-cost option	20 March 2013	460,129	22 March 2016	81.68%	197,850	£411,528
Dr Mike Watts[4]	Nil-cost option	20 March 2013	500,000	22 March 2016	81.68%	214,994	£447,188

Notes:

1 On the vesting of a 2009 LTIP award held by a current employee or executive director of the Group, 50% of the shares to which the holder has become entitled are available for immediate exercise, with the remaining 50% normally becoming exercisable after a further period of one year.

2 The values shown in this column have been calculated by multiplying the number of shares that vested by £2.08, being the closing mid-market price of a share in the Company on the day such vesting occurred. In the case of current directors, this value has been included in the single figure total for 2016.

3 James Smith was not employed by the Group in 2013 and was not, therefore, granted an LTIP award during that period.

4 As explained on page 111, both Jann Brown and Dr Mike Watts were categorised as 'good leavers' for the purposes of the 2009 LTIP rules with the result that their awards granted in 2013 vested at the same time as those held by all other participants. However, a pro-rata reduction was applied to the number of shares that vested in respect of these individuals' awards to reflect the proportion of the performance period that they were employed by the Group.

LTIP – awards exercised during 2016 (audited)

Details of vested LTIP awards (which are in the form of nil-cost options) that were exercised by current and former directors during the year to 31 December 2016 are as follows:

	Date of grant	Date of vesting	Date of exercise	Number of ordinary shares acquired on exercise	Exercise price	Market value of ordinary shares at date of exercise	Gain on exercise
Current director							
Simon Thomson	14 June 2012	17 June 2015	17 June 2016	60,148	Nil	£1.849	£111,184
	20 March 2013	22 March 2016	22 March 2016	231,032	Nil	£2.089	£482,686
Former director							
Jann Brown	14 June 2012	17 June 2015	17 March 2016	79,190	Nil	£1.982	£156,993
	20 March 2013	22 March 2016	24 March 2016	197,850	Nil	£2.058	£407,195
Dr Mike Watts	20 March 2013	22 March 2016	30 March 2016	214,994	Nil	£2.030	£436,438

Directors' Remuneration Report
continued

LTIP – other awards held by 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 2009 LTIP during 2016, set out below are details of the other unvested entitlements under the plan that were held by current executive directors during the year:

	Date of grant	Type of award	Basis of award granted	Share price at date of grant[2]	No. of shares over which award originally granted	% of shares over which award originally granted that vest at threshold	Face value (£'000) of… …shares over which award originally granted[3]	…max. no. of shares to vest if all performance measures met[4]	Vesting determined by performance over three years until…
Directors									
Simon Thomson	19 March 2014	Nil-cost option	3 x base salary of £538,125	£1.682	959,794	20%	£1,614	£2,147	18 March 2017
	19 March 2015	Nil-cost option	3 x base salary of £546,197	£1.868	877,190	20%	£1,639	£2,179	18 March 2018
James Smith	19 March 2014	Nil-cost option	3 x base salary of £350,000	£1.682	624,256	20%	£1,050	£1,396	18 March 2017
	19 March 2015	Nil-cost option	3 x base salary of £355,250	£1.868	570,529	20%	£1,066	£1,417	18 March 2018

Notes:
1 Further details of the performance conditions that apply to these awards are set out on page 118.
2 In the case of an award granted in 2014, this figure represents the closing mid-market price of a share in the Company on the day immediately preceding its date of grant. For a 2015 award, it is the average of such prices over the thirty days preceding the date of grant.
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'.
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 1.33% (being the vesting percentage that would apply on full satisfaction of all performance conditions to which the awards are subject) and multiplying the result by the appropriate 'share price at date of grant'.

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 2009 LTIP to executive directors that were outstanding during 2016.

Company	Comparator group applicable to LTIP awards granted on… 20 March 2013	19 March 2014	19 March 2015	16 March 2016
Africa Oil Corp.				✓
Afren PLC*	✓	✓	✓	
Aker BP ASA (formerly named Det Norske Oljeselskap ASA)			✓	✓
BG Group PLC*	✓	✓	✓	
Cobalt International Energy, Inc.				✓
DNO ASA	✓	✓	✓	✓
Dragon Oil PLC*			✓	
EnQuest PLC	✓	✓	✓	✓
Faroe Petroleum PLC	✓	✓	✓	✓
Genel Energy PLC	✓	✓	✓	✓
JKX Oil & Gas PLC	✓	✓		
Kosmos Energy Limited			✓	✓
Lundin Petroleum AB	✓	✓	✓	✓
Maurel & Prom				✓
Niko Resources Limited	✓	✓		
Nostrum Oil & Gas PLC			✓	✓
Ophir Energy PLC	✓	✓	✓	✓

Comparator group companies applicable to LTIP awards continued

Company	Comparator group applicable to LTIP awards granted on... 20 March 2013	19 March 2014	19 March 2015	16 March 2016
Petroceltic International PLC*	✓	✓	✓	✓
Premier Oil PLC	✓	✓	✓	✓
Rockhopper Exploration PLC	✓	✓	✓	✓
Salamander Energy PLC*	✓	✓		
Santos Limited	✓	✓	✓	✓
SOCO International PLC	✓	✓	✓	✓
Talisman Energy, Inc*	✓	✓		
Tullow Oil PLC	✓	✓	✓	✓

* Denotes companies that have delisted during the applicable performance period.

Participation of executive directors in all-employee share schemes during 2016

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 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 £1,800 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 2016/2017, the Company awarded two matching shares for every one partnership share purchased and intends to continue using this award ratio for the tax year 2017/2018.
- 'Free shares' – employees can be given up to £3,600 worth of ordinary shares free in each tax year. On 14 April 2016, an award of free shares was made to employees, including to 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.

Details of executive directors' SIP participation in 2016

Details of the shares purchased by and awarded to the executive directors under the SIP during the course of the year are as follows:

	Total SIP shares held at 1 January 2016	Free shares awarded on 14 April 2016 at a price of £2.043 per share	Partnership shares awarded on 6 May 2016 at a price of £2.0575 per share	Matching shares awarded on 6 May 2016 at a price of £2.0575 per share	Total SIP shares held at 31 December 2016
Directors					
Simon Thomson	16,049	1,762	875	1,750	20,436
James Smith	7,757	1,762	874	1,748	12,141

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 125.

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 a specified percentage of base salary. The level of this target holding was recently reviewed by the committee as part of the process surrounding the formulation of the new Directors' Remuneration Policy set out on pages 101 to 110; it was agreed that, subject to this new policy receiving shareholder approval, the level would be increased from 100% of salary to 200% of salary.

In order to facilitate the achievement of the above requirement, the share ownership policy also provides that, until the necessary 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.

Directors' Remuneration Report
continued

Shareholding guidelines for directors (audited) continued
The following table discloses the beneficial interest of each director in the ordinary shares of the Company as at 31 December 2016. It also highlights the fact that, on that date, the above shareholding requirements were satisfied by Simon Thomson, Chief Executive, but, in light of his relatively recent appointment as CFO, not by James Smith. However, James Smith does intend to build up his holding over time in accordance with the committee's policy and it is expected that he will reach the necessary levels within a period of three to five years from joining the Group.

	Shares held				Awards over shares under the LTIP		
	Ordinary shares[2]	Ordinary shares held in the SIP[3]	Total holding of ordinary shares	Value of holding as a % of salary on 1 January 2017[4]	Ordinary shares subject to vested but unexercised awards[5]	Ordinary shares subject to unvested awards[6]	Total interest in ordinary shares
Executive directors							
Simon Thomson	710,784	20,436	731,220	249%	231,033	2,693,978	3,656,231
James Smith	55,096	12,141	67,237	35%	–	1,752,180	1,819,417
Non-executive directors							
Ian Tyler	–	–	–	–	–	–	–
Todd Hunt	72,012	–	72,012	–	–	–	72,012
Iain McLaren	7,878	–	7,878	–	–	–	7,878
Alexander Berger	40,008	–	40,008	–	–	–	40,008
M. Jacqueline Sheppard QC	7,000	–	7,000	–	–	–	7,000
Keith Lough	–	–	–	–	–	–	–
Peter Kallos	–	–	–	–	–	–	–
	892,778	**32,577**	**925,355**		**231,033**	**4,446,158**	**5,602,546**

Notes:
1 Details of the Company's share ownership policy for executive directors are set out above.
2 Includes shares held by connected persons.
3 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.
4 Share price used is the average share price over the year to 31 December 2016.
5 This column shows all vested but unexercised awards under the LTIP that were held by the director concerned as at 31 December 2016.
6 This column shows all unvested and outstanding awards under the LTIP that were held by the director concerned as at 31 December 2016 (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 118.

Dilution of share capital pursuant to share plans during 2016
In any ten-year rolling period, the number of ordinary shares which may be issued in connection with the Company's 'discretionary share plans' (which includes both the LTIPs and the share option/award schemes used to incentivise less senior employees) 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.

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.

Board appointments with other companies during 2016
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.

Details of the non-executive positions with other companies that were held by Cairn's executive directors during 2016, and the fees that were payable, are as follows:

	Position held	Fees received for the year to 31 December 2016
Current directors		
Simon Thomson	Non-executive director, Graham's The Family Dairy Limited	**£35,000**

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 2015 and 2016.

	Financial Year 2015	**Financial Year 2016**	% change
Employee costs (US$m)	32.6	**30.4**	(6.7)%
Distributions (US$m)[1]	0	**0**	0%

Note:

1 For the purposes of the above table, 'Distributions' include amounts distributed to shareholders by way of dividend and share buyback.

Implementation of remuneration policy in 2017

The following table provides details of how the Company intends to implement the key elements of the new Directors' Remuneration Policy described on pages 101 to 110 during 2017, assuming it is approved by shareholders at the AGM to be held on 19 May 2017.

Remuneration element	Implementation during 2017
Base salary	Both of the executive directors received a 1% increase in base salary on 1 January 2017 – 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 both the current executive directors for the year to 31 December 2017 are as follows: • Simon Thomson, Chief Executive – £559,934; and • James Smith, CFO – £364,185.
Benefits	Executive directors will continue to receive the same benefits as in 2016.
Annual bonus	In accordance with the requirements of the policy, executive directors will be eligible to receive a bonus of up to 125% of base salary depending on the extent to which specified measures are satisfied over 2017. However, any bonus awarded to an executive director in excess of 100% of salary will be deferred into Cairn shares for a period of three years. 90% of the Chief Executive's and CFO's 2017 bonus opportunity will be based on the demanding Group KPIs described below (with details of the weightings specified in brackets): • **Deliver exploration and appraisal success** (25%); – Safely, cost effectively and successfully drill, evaluate and flow test appraisal wells on the SNE field in Senegal to allow preparation of the Evaluation Report and update the estimate of resources and capital required to develop the field in a timely manner. – Efficiently discover commercial quantities of hydrocarbons through maturation and drilling of select exploration and appraisal wells across the portfolio. Measured by: new commercial discoveries based on 2C resources found; cumulative net volumes found versus Group target; and finding efficiency expressed in US$/bbl versus industry benchmarks. • **Portfolio optimisation and replenishment** (16%); – Develop an inventory and timeline of exploration and appraisal opportunities which meet Cairn's technical and commercial criteria. Measured by increasing the prospect inventory by securing or maturing new independent opportunities from within or outwith the Company's portfolio. • **Deliver operational excellence** (24%); – Successfully progress development and production projects against key milestones including, as appropriate, capex, opex and sales volume targets. • **Maintain licence to operate** (20%); – Achieve leading HSSE indicators linked to four categories within the Group's Corporate Responsibility Management System (Business Relationships; Society and Communities; People; and the Environment). – Achieve lagging HSSE indicators set in line with IOGP targets and guidelines. – Investing in people and systems. • **Manage balance sheet strength** (15%) – Develop and implement a funding strategy that allows a value generative plan to be executed and ensures a minimum headroom cushion from existing sources of funding is maintained. – Make tangible progress under the UK-India bilateral treaty arbitration. The balance (10%) of the executive directors' bonuses for 2017 will be determined by reference to the achievement of personal objectives that are relevant to each individual's role within the business. The specific targets to be used for the purposes of the 2017 bonus scheme are commercially sensitive and have not, therefore, been set out in detail above. However, appropriate disclosure of group KPIs and group performance in relation to the 2017 bonus scheme will be included in next year's Annual Report on Remuneration.

Directors' Remuneration Report
continued

Remuneration element	Implementation during 2017
LTIP	It is intended that, following the Company's 2017 AGM, the executive directors will be granted awards pursuant to the rules of the new 2017 LTIP. These awards will, in aggregate, be over shares worth 250% of salary and will take the following forms: • A 'core award' over shares worth 200% of salary – the vesting of which will be dependent on relative TSR performance over a three year period versus a comparator group of peer companies (with 25% vesting for a median ranking rising on a straight-line basis to 100% vesting for upper quartile performance); and • A 'kicker award' over shares worth 50% of salary – vesting will be conditional on achieving both an upper quartile ranking in the comparator group and absolute TSR growth over the performance period of at least 100%. All shares that vest in relation to an award (whether 'core' or 'kicker') will be subject to an additional two year holding period. The comparator group against which the relative performance conditions are assessed will be the same as the one used for the purposes of the LTIP grants made in 2016 except that it will exclude Petroceltic International plc, who delisted during 2016, and will include Seplat Petroleum Development Company plc, a FTSE-listed oil company of similar size to Cairn.
SIP	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.
Pension	The Company will continue to contribute 15% of basic salary on behalf of executive directors or pay them an equivalent amount of additional salary.
Non-executive directors' fees	For 2017, both the annual non-executive director fee and the additional annual fee for chairing the audit and/or remuneration committees remain unchanged at £74,900 and £10,000 respectively.
Chairman's fees	The annual Chairman's fee for 2017 has been increased from £160,000 to £175,000.

The Directors' Remuneration Report was approved by the Board on 7 March 2017 and signed on its behalf by:

M. JACQUELINE SHEPPARD QC
Chair of the Remuneration Committee

Directors' Report

The directors of Cairn Energy PLC (registered in Scotland with Company Number SC226712) present their Annual Report and Accounts for the year ended 31 December 2016 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 19 May 2017.

Results and dividend
The Group made a loss after tax of US$95.0 million (2015 loss of US$515.5 million).

The directors do not recommend the payment of a dividend for the year ended 31 December 2016.

Subsequent events that have occurred after the balance sheet date as at 31 December 2016 are included in Section 6.5 of the Notes to the Financial Statements.

Strategic Report
Details of the Group's strategy and business model during the year and the information that fulfils the requirements of the Strategic report can be found in the Strategic Report section on pages 4 to 9 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 further details of these plans are provided in the Directors' Remuneration report on pages 98 to 124. 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 his employment, the current Chief Executive is entitled to compensation pursuant to his service contract. Further details of the relevant provisions are set out in the Directors' Remuneration report on page 110. There are no agreements providing for compensation to the Chief Financial Officer or to employees on a change of control and no such provision will be included in the contracts of other future appointees to the Board.

Other than the Senior Secured Borrowing Base Facility Agreement entered into by the Company with BNP Paribas and other syndicated banks dated 18 July 2014 (the 'Facility Agreement'), 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. In terms of clause 9.2 of the Facility Agreement, if there is a change of control of the Company, any lender may cancel its commitment and declare its participation in all outstanding utilisations, together with accrued interest and all other amounts accrued immediately due and payable.

Corporate governance
The Company's Corporate Governance Statement is set out on pages 78 to 90 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 76 and 77. The beneficial interests of the directors in the ordinary shares of the Company are shown below:

	As at 31 December 2015	As at 31 December 2016	As at 6 March 2017
Simon Thomson	572,783	731,220	731,220
James Smith	62,853	67,237	67,237
Ian Tyler	0	0	0
Todd Hunt	72,012	72,012	72,012
Iain McLaren	7,878	7,878	7,878
Jackie Sheppard	7,000	7,000	7,000
Alexander Berger	40,008	40,008	40,008
Keith Lough	0	0	0
Peter Kallos	0	0	0
Nicoletta Giadrossi*	–	–	0

* Nicoletta Giadrossi was appointed as a non-executive director of the Company on 10 January 2017.

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 98 to 124.

None of the directors has a material interest in any contract, other than a service contract, in respect of each of the executive directors, 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 98 to 124.

Directors' Report
continued

Share capital
The issued share capital of the Company is shown in Section 6.1 of the Notes to the Financial Statements. As at 6 March 2017, 577,235,781 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.

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 therefor, 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 therefor, 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 2016 and 2 March 2017 (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 2016	% Share Capital	As at 2 March 2017	% Share Capital
MFS Investment Management	81,843,909	14.18	80,548,715	13.95
BlackRock	63,714,033	11.04	62,668,982	10.86
Hotchkis & Wiley	29,271,017	5.07	28,048,952	4.86
Franklin Templeton	28,204,236	4.89	22,092,949	3.83
Kames Capital	24,789,901	4.29	27,699,135	4.80
Aviva Investors	24,761,979	4.29	23,704,791	4.11
Majedie Asset Management	23,255,774	4.03	20,758,963	3.60
Fidelity International	16,600,387	2.88	17,517,364	3.03

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 Report section on pages 2 to 75 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 Section 3.6 of the Financial Statements.

Acquisition of own shares
In 2013, 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.

The Board decided to suspend the share buy-back programme as of 21 March 2014 and therefore no further shares have been repurchased by the Company since that date.

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 78 to 90, the Nomination Committee Report on pages 96 and 97 and in the Company's Articles of Association.

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 (a 'Qualifying Third Party Indemnity Provision'). The indemnity was in force throughout the last financial year and is currently in force. In May 2014, the Company entered into standalone deeds of indemnity with each of the directors, pursuant to which the directors have the benefit of an indemnity which is a Qualifying Third Party Indemnity Provision. The indemnities came into force upon execution of the deeds of indemnity and are 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.

Directors' Report
continued

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.

Directors' Responsibility Statement
The directors are responsible for preparing the Annual Report and Accounts, 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 (EU). 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 Group and Company 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 EU have been followed, subject to any material departures disclosed and explained in the financial statements; and
- 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.

The directors are responsible for the maintenance and integrity of the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Following careful review and consideration of the Cairn Energy PLC Annual Report and Accounts 2016 (the 'Accounts'), the directors consider that the Accounts, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the Group's performance, business model and strategy.

Each of the directors, whose names and functions are listed in the Board of Directors section on pages 76 and 77, 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 loss of the Group and Company; and
- the Strategic report section on pages 2 to 75 of this document 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.

Disclosure of Information to Auditors
The directors of the Company who held office at 31 December 2016 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 2017
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 12 noon (BST) on Friday 19 May 2017. The resolutions to be proposed at the AGM are set out and fully explained in the Circular containing the Notice of AGM which has been posted to shareholders together with this Annual Report and Accounts.

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
7 March 2017

Independent Auditors' Report to the Members of Cairn Energy PLC

Report on the financial statements

Our opinion

In our opinion:

- Cairn Energy PLC's group financial statements and company financial statements (the 'financial statements') give a true and fair view of the state of the group's and of the company's affairs as at 31 December 2016 and of the group's loss and the group's and the 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 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.

What we have audited

The financial statements, included within the Annual Report and Accounts (the 'Annual Report'), comprise:

- the group balance sheet as at 31 December 2016;
- the group income statement and group statement of comprehensive income for the year then ended;
- the group statement of cash flows for the year then ended;
- the group statement of changes in equity for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies and other explanatory information.

Certain required disclosures have been presented elsewhere in 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.

The financial reporting framework that has been applied in the preparation of the financial statements is IFRSs as adopted by the European Union and, as regards the company financial statements, as applied in accordance with the provisions of the Companies Act 2006, and applicable law.

Our audit approach

Context

The context for our audit is set by Cairn Energy PLC's ('Cairn') major activities in 2016 combined with an increasing oil price from a low base at the start of the year. In the year, Cairn has continued to progress their development assets in the Catcher and Kraken North Sea fields towards first oil production, which is targeted for the next 12 months, and continued their exploration and appraisal programme offshore Senegal. Away from core operations, Cairn's main focus has been dealing with the continued restriction on the ability to sell the remaining 10% holding in Cairn India and the ongoing discussions with the Indian Tax Authorities in relation to the final assessment order received in February 2016.

Overview

- Overall group materiality: $24.6 million which represents 1% of total assets.

- We performed the majority of audit work in the UK, with PwC Norway performing the audit work on the UK & Norway component. The group audit team visited Norway as part of the audit process.
- Our audit scope obtained coverage of over 97% of group total assets.

- Our key areas of audit focus were:
  - Risk of impairment of exploration/development assets and goodwill.
  - Potential impact on tax provisions of the tax enquiry in relation to Cairn India Limited.
  - Going Concern.

Materiality

The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and in evaluating the effect of misstatements, both individually and on the financial statements as a whole.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

Overall group materiality	$24.6 million (2015: $23.1 million).
How we determined it	1% of Total assets.
Rationale for benchmark applied	We believe that total assets is 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 $1.2 million (2015: $1.15 million) as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons. We reported no potential adjustments to the Audit Committee.

Independent Auditors' Report to the Members of Cairn Energy PLC continued

How we tailored the audit scope

We tailored the scope of our audit to ensure that we performed enough work to be able to give an opinion on the financial statements as a whole, taking into account the geographic structure of the group, the location of accounting processes and controls, and the industry in which the group operates.

For operating purposes, the group is structured around three key segments: UK & Norway, Senegal and International. During 2016, UK & Norway has seen the majority of the development activity, with the main exploration activity occurring in Senegal.

For accounting purposes, the group is structured into 24 reporting units (or 'components'). The majority of the finance function is based in Edinburgh, other than the UK & Norway component which is primarily accounted for in Stavanger, Norway. Our PwC Norway audit team performed the audit work on the UK & Norway component and all other audit work was performed by our UK audit team.

Our group scoping was based on total assets, consistent with our approach to materiality, and identified six financially significant components, comprising a high proportion of total group assets, which required an audit of their complete financial information. A further two components were identified as significant from a risk perspective due to the carrying value of their exploration and development assets. Finally, one additional component was subject to procedures at the exploration assets financial statement line item (FSLI) level, and one at the accounts payable FSLI level to obtain sufficient coverage.

The UK team attended an audit planning meeting in Norway, as well as being directly involved in the scoping and review of the work performed by PwC Norway, and maintained contact throughout the execution and completion of the audit, including an audit clearance call involving PwC in the UK and Norway.

Our group audit approach resulted in coverage of over 97% of the consolidated total assets – our key benchmark for planning and scoping our audit.

The scope of our audit and our areas of focus

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) ('ISAs (UK & Ireland)').

We designed our audit by determining materiality and assessing the risks of material misstatement in the financial statements. In particular, we looked at where the directors made subjective judgements, for example in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. As in all of our audits we also addressed the risk of management override of internal controls, including evaluating whether there was evidence of bias by the directors that represented a risk of material misstatement due to fraud.

The risks of material misstatement that had the greatest effect on our audit, including the allocation of our resources and effort, are identified as 'areas of focus' in the table below. We have also set out how we tailored our audit to address these specific areas in order to provide an opinion on the financial statements as a whole, and any comments we make on the results of our procedures should be read in this context. This is not a complete list of all risks identified by our audit.

Area of focus

Risk of impairment of exploration/development assets and goodwill

The risk has remained consistent with prior year due to the current outlook for oil prices remaining low compared with recent history. This has the potential to adversely impact the value of exploration and development assets.

Exploration assets of $471.3m relate to costs incurred where there is expected future activity but no approved development plan at present, primarily Cairn's discovery offshore Senegal. Development assets of $735.1m reflect spend to 31 December 2016 on Catcher and Kraken. There has been $150.5m of exploration and $276.6m of development additions in 2016. Both of these asset categories require an impairment review only if an impairment trigger is identified.

The goodwill balance of $118.9m arose on the acquisitions of Agora and Nautical in 2012. As required by IAS 36, an annual impairment review is carried out on this balance.

Relevant indicators of impairment in the Oil & Gas industry include:

- unsuccessful exploration efforts;
- sustained low oil price environment;
- changes to exploration plans;
- changes to reserves estimates; and
- consolidated net assets being significantly more than the market capitalisation of the group.

When an impairment review and calculation is performed, there are significant judgements in relation to the underlying assumptions such as:

- long term oil price;
- reserve estimates;
- production volume profiles;
- cost profiles and escalation applied; and
- discount rates.

We focused on this area due to the significant values and the nature of the judgements and assumptions management are required to make in determining the existence of impairment triggers and the amount of impairment.

Refer to notes 2.1, 2.2 and 2.6 to the accounts

How our audit addressed the area of focus

We tested management's impairment review of goodwill and capitalised exploration and development costs by performing the work described below and found that all management assumptions were within a reasonable range.

We read management's assessment of impairment triggers and did not identify any additional triggers which had not yet been considered by management.

Specific work was then performed over the impairment review including:

- comparing the assumptions used within the impairment review models to approved budgets and business plans and other evidence of future intentions for individual exploration properties, which we found to be materially consistent;
- comparing reserves and production profiles and matching capital and operating expenditure forecasts to group approved values or operator estimates, which we found to be materially consistent;
- benchmarking of key assumptions including commodity price and discount rate and inflation against external data and recent public announcements from other oil companies. We found certain assumptions used by Cairn, including the long-term oil price, to be at the upper end of a reasonable range, while other assumptions, for example the use of a 3 year forward curve, were towards the lower end of a reasonable range; in combination, we consider the assumptions used by Cairn to be reasonable and in line with other market participants;
- reviewing the mathematical accuracy of key formulae in the impairment models without exception;
- reviewing management's sensitivity analysis and performing additional sensitivity analysis over key assumptions in the model in order to assess the potential impact of a range of possible outcomes. For Catcher and Kraken, we determined that the calculation was most sensitive to assumptions relating to the oil price; and
- assessing the inclusion of all appropriate assets and liabilities in the cash generating unit and in particular given that the recoverable amount is determined based on a fair value less costs of disposal, the inclusion or exclusion of certain tax related balances and agreed that while all relevant balances had been included, we identified one error in the allocation of tax balances which was adjusted for by management.

After performing the testing above, we identified one exploration asset where the evidence of future activity was sufficiently judgemental that we proposed an immaterial adjustment which was recorded by management. Other than this one item we concluded that no further impairment was required.

Potential impact on tax provisions of tax enquiry in relation to Cairn India Limited 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. In February 2016, a final assessment order was received from the Indian tax authorities for an amount of $4.3 billion (290 billion INR) including interest and penalties. Cairn are continuing to contest this order in a court of international arbitration and at this point, there is still no certainty over the outcome. Management have made judgements relating to the likelihood of an obligation arising and whether there is a need to recognise a provision or disclose a contingent liability. We therefore focused on this area as a result of the uncertainty and the potential material impact to the group. Refer to Note 5.5 to the financial statements.	In assessing the potential impact of the assessment order from the Indian tax authorities we performed the following procedures. In previous years we: – understood the group reconstruction under review, and the potential basis for any claim, including the relevant legislation and other precedent; – read correspondence received by the Group from the Indian tax authorities; – discussed with management the advice and action they had taken with regards to the enquiry and reviewed any associated documents; and – discussed certain aspects of the matter directly with the group's legal advisers. In the current year we have reconfirmed our understanding and performed the following additional procedures: – read correspondence received by the Group from the Indian tax authorities in the current year and discussed with management the advice and action taken as a result; – discussed certain aspects of the matter directly with the group's legal advisers; and – agreed the calculation of the contingent liability based on prevailing exchange rates. We concluded that the position adopted in the financial statements was reasonable based on the work we performed, in particular: – management'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. We also considered whether this ongoing enquiry would have any impact on the carrying value of the investment in Cairn India Limited of $656.1m. We noted that while the group are restricted from selling the investment, this is a restriction directly on them and not all market participants, and therefore it does not affect the fair value of the underlying investment, which is the basis on which it is carried in the consolidated balance sheet.
Going Concern We focused on this area as the Group is in the exploration and development phase and is therefore reliant on having sufficient funding to progress their asset portfolio. As the group currently has no significant cash-generating assets in operation, there is a finite cash resource to fund ongoing activities and therefore we have focused on whether there are sufficient cash resources in place to allow the group to continue as a going concern. In addition, the restriction on selling the remaining Cairn India shares noted above means the Group is currently unable to access the value in this investment to fund operations. During 2014, the group negotiated a debt facility to partially fund the development of Catcher and Kraken, and are required to meet a liquidity test to allow them to drawdown this facility. Cairn are also planning to drill 2 exploration wells in UK & Norway and 2 appraisal wells in Senegal over the next 12-18 months which will be funded from existing cash resources. We believe this risk has remained consistent from last year as the Group does not yet have revenue-producing assets and has continued to incur operating and capital expenditure.	In assessing the appropriateness of the going concern assumption used in preparing the financial statements, we: – reviewed the cash flow requirements of the Group over the next 12 months based on budgets and forecasts; – understood what forecast expenditure is committed and what could be considered discretionary; – considered the liquidity of existing assets on the balance sheet, including the Cairn India investment; – reviewed the terms associated with the debt agreement and the amount of the facility available for drawdown; and – considered potential downside/upside scenarios and the resultant impact on available funds. Our conclusion on going concern is below.

Going concern
Under the Listing Rules we are required to review the directors' statement, set out on page 140, in relation to going concern. We have nothing to report having performed our review.

Under ISAs (UK & Ireland) we are required to report to you if we have anything material to add or to draw attention to in relation to the directors' statement about whether they considered it appropriate to adopt the going concern basis in preparing the financial statements. We have nothing material to add or to draw attention to.

As noted in the directors' statement, the directors have concluded that it is appropriate to adopt the going concern basis in preparing the financial statements. The going concern basis presumes that the group and 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 company's ability to continue as a going concern.

Other required reporting
Consistency of other information and compliance with applicable requirements
Companies Act 2006 reporting
In our opinion, based on the work undertaken in the course of the audit:
- 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; and
- the Strategic Report and the Directors' Report have been prepared in accordance with applicable legal requirements.

In addition, in light of the knowledge and understanding of the group, the company and their environment obtained in the course of the audit, we are required to report if we have identified any material misstatements in the Strategic Report and the Directors' Report. We have nothing to report in this respect.

Independent Auditors' Report to the Members of Cairn Energy PLC continued

ISAs (UK & Ireland) reporting
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 company acquired in the course of performing our audit; or – otherwise misleading.	We have no exceptions to report.
• the statement given by the directors on page 128, in accordance with provision C.1.1 of the UK Corporate Governance Code (the 'Code'), 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 and company's position and performance, business model and strategy is materially inconsistent with our knowledge of the group and company acquired in the course of performing our audit.	We have no exceptions to report.
• the section of the Annual Report on pages 91 to 95, as required by provision C.3.8 of the Code, 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.

The directors' assessment of the prospects of the group and of the principal risks that would threaten the solvency or liquidity of the group
Under ISAs (UK & Ireland) we are required to report to you if we have anything material to add or to draw attention to in relation to:

• the directors' confirmation on page 41 of the Annual Report, in accordance with provision C.2.1 of the Code, that they have carried out a robust assessment of the principal risks facing the group, including those that would threaten its business model, future performance, solvency or liquidity.	We have nothing material to add or to draw attention to.
• the disclosures in the Annual Report that describe those risks and explain how they are being managed or mitigated.	We have nothing material to add or to draw attention to.
• the directors' explanation on page 40 of the Annual Report, in accordance with provision C.2.2 of the Code, as to how they have assessed the prospects of the group, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the group will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.	We have nothing material to add or to draw attention to.

Under the Listing Rules we are required to review the directors' statement that they have carried out a robust assessment of the principal risks facing the group and the directors' statement in relation to the longer-term viability of the group. Our review was substantially less in scope than an audit and only consisted of making inquiries and considering the directors' process supporting their statements; checking that the statements are in alignment with the relevant provisions of the Code; and considering whether the statements are consistent with the knowledge acquired by us in the course of performing our audit. We have nothing to report having performed our review.

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 company, or returns adequate for our audit have not been received from branches not visited by us; or
- the 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.

Directors' remuneration
Directors' remuneration report – Companies Act 2006 opinion
In our opinion, the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006.

Other Companies Act 2006 reporting
Under the Companies Act 2006 we are required to report to you if, in our opinion, certain disclosures of directors' remuneration specified by law are not made. We have no exceptions to report arising from this responsibility.

Corporate governance statement
Under the Listing Rules we are required to review the part of the Corporate Governance Statement relating to ten further provisions of the Code. We have nothing to report having performed our review.

Responsibilities for the financial statements and the audit
Our responsibilities and those of the directors
As explained more fully in the Directors' Responsibility Statement set out on page 128, the directors are responsible for the preparation of the 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 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.

What an audit of financial statements involves

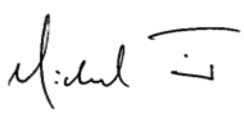
An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- whether the accounting policies are appropriate to the group's and the 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.

We primarily focus 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.

We test and examine information, using sampling and other auditing techniques, to the extent we consider necessary to provide a reasonable basis for us to draw conclusions. We obtain audit evidence through testing the effectiveness of controls, substantive procedures or a combination of both.

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. With respect to the Strategic Report and Directors' Report, we consider whether those reports include the disclosures required by applicable legal requirements.



MICHAEL TIMAR (SENIOR STATUTORY AUDITOR)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Glasgow
7 March 2017

- 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

Group Income Statement
For the year ended 31 December 2016

	Section	2016 US$m	2015 US$m
Continuing operations			
Pre-award costs	42	**(17.7)**	(35.2)
Unsuccessful exploration costs	21	**(70.3)**	(97.4)
Administrative and other expenses	43	**(34.9)**	(29.7)
Impairment of intangible exploration/appraisal assets	21	**(25.3)**	(17.9)
Impairment of property, plant & equipment – development assets	22	**–**	(25.1)
Gain on disposal of oil and gas assets	23	**–**	26.6
Operating loss		**(148.2)**	(178.7)
Impairment of available-for-sale financial asset	31	**–**	(318.6)
Finance income	45	**14.0**	19.8
Finance costs	46	**(17.3)**	(20.3)
Loss before taxation from continuing operations		**(151.5)**	(497.8)
Taxation			
Tax credit/(charge)	52	**56.5**	(17.7)
Loss for the year attributable to equity holders of the parent		**(95.0)**	(515.5)
Loss per ordinary share – basic (cents)	47	**(16.56)**	(90.26)
Loss per ordinary share – diluted (cents)	47	**(16.56)**	(90.26)

Group Statement of Comprehensive Income
For the year ended 31 December 2016

	Section	2016 US$m	2015 US$m
Loss for the year		**(95.0)**	(515.5)
Other comprehensive income/(expense) – items that may be recycled to profit or loss			
Surplus/(deficit) on valuation of financial asset	31	**272.1**	(318.6)
Deferred tax credit on valuation of financial asset	52	**–**	9.5
Valuation movement recycled to income statement	31	**–**	318.6
Deferred tax credit on valuation movement recycled to income statement	52	**–**	(9.5)
Currency translation differences		**(104.2)**	(63.5)
Other comprehensive income/(expense) for the year		**167.9**	(63.5)
Total comprehensive income/(expense) for the year attributable to equity holders of the parent		**72.9**	(579.0)

Group Balance Sheet
As at 31 December 2016

	Section	2016 US$m	2015 US$m
Non-current assets			
Intangible exploration/appraisal assets	2.1	**471.3**	423.4
Property, plant & equipment – development assets	2.2	**735.1**	579.6
Intangible assets – goodwill	2.6	**118.9**	131.9
Other property, plant & equipment and intangible assets		**1.9**	3.9
Available-for-sale financial asset	3.1	**656.1**	384.0
		1,983.3	1,522.8
Current assets			
Income tax asset	5.3	**26.1**	33.0
Inventory		**–**	0.7
Other receivables	3.3	**113.7**	148.9
Cash and cash equivalents	3.2	**334.9**	602.8
		474.7	785.4
Total assets		**2,458.0**	2,308.2
Current liabilities			
Trade and other payables	3.4	**123.0**	120.1
		123.0	120.1
Non-current liabilities			
Deferred tax liabilities	5.4	**62.7**	48.8
Provisions – decommissioning	2.4	**79.6**	37.1
Provisions – other		**2.8**	2.8
		145.1	88.7
Total liabilities		**268.1**	208.8
Net assets		**2,189.9**	2,099.4
Equity attributable to equity holders of the parent			
Called-up share capital	6.1	**12.4**	12.4
Share premium	6.1	**488.0**	487.1
Shares held by ESOP/SIP Trusts	6.1	**(10.2)**	(23.0)
Foreign currency translation	6.1	**(250.1)**	(146.2)
Capital reserves – non-distributable	6.1	**40.8**	40.8
Merger reserve	6.1	**255.9**	255.9
Available-for-sale reserve		**272.1**	–
Retained earnings		**1,381.0**	1,472.4
Total equity		**2,189.9**	2,099.4

The financial statements on pages 135 to 176 were approved by the Board of Directors on 7 March 2017 and signed on its behalf by:

JAMES SMITH
Chief Financial Officer

SIMON THOMSON
Chief Executive

Group Statement of Cash Flows
For the Year Ended 31 December 2016

	Section	2016 US$m	2015 US$m
Cash flows from operating activities			
Loss before taxation		**(151.5)**	(497.8)
Unsuccessful exploration costs		**70.3**	97.4
Depreciation and amortisation		**2.7**	3.4
Share-based payments charge		**16.7**	15.2
Impairment of intangible exploration/appraisal assets		**25.3**	17.9
Impairment of property, plant & equipment – development assets		**–**	25.1
Gain on disposal of oil and gas assets		**–**	(26.6)
Inventory disposal/write-down		**0.7**	(0.2)
Impairment of available-for-sale financial asset		**–**	318.6
Finance income		**(14.0)**	(19.8)
Finance costs		**17.3**	20.3
Interest paid		**–**	(0.2)
Income tax received from operating activities		**6.8**	23.6
Other receivables movement	3.3	**(0.8)**	4.3
Trade and other payables movement	3.4	**6.0**	6.1
Provisions movement		**(0.1)**	(2.4)
Net cash used in operating activities		**(20.6)**	(15.1)
Cash flows from investing activities			
Expenditure on intangible exploration/appraisal assets		**(149.1)**	(208.4)
Expenditure on property, plant & equipment – development assets		**(125.2)**	(114.2)
Income tax received from investing activities		**28.7**	28.2
Proceeds on disposal of oil and gas assets		**–**	54.7
Movement on inventory		**0.6**	0.8
Purchase of other property, plant & equipment and intangible assets		**(4.5)**	(2.1)
Interest received		**2.3**	3.6
Net cash used in investing activities		**(247.2)**	(237.4)
Cash flows from financing activities			
Facility fees and bank charges		**(5.0)**	(6.3)
Proceeds from exercise of share options		**0.9**	0.1
Net cash flows used in financing activities		**(4.1)**	(6.2)
Net decrease in cash and cash equivalents		**(271.9)**	(258.7)
Opening cash and cash equivalents at beginning of year		**602.8**	869.3
Foreign exchange differences		**4.0**	(7.8)
Closing cash and cash equivalents	3.2	**334.9**	602.8

Group Statement of Changes in Equity
For the Year Ended 31 December 2016

	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 2015	499.4	(26.7)	(82.7)	296.7	–	1,976.4	2,663.1
Loss for the year	–	–	–	–	–	(515.5)	(515.5)
Deficit on valuation of financial assets	–	–	–	–	(318.6)	–	(318.6)
Deferred tax credit on valuation of financial assets	–	–	–	–	9.5	–	9.5
Valuation movement recycled to income statement	–	–	–	–	318.6	–	318.6
Deferred tax credit on valuation movement recycled to income statement	–	–	–	–	(9.5)	–	(9.5)
Currency translation differences	–	–	(63.5)	–	–	–	(63.5)
Total comprehensive income/(expense)	–	–	(63.5)	–	–	(515.5)	(579.0)
Share-based payments	–	–	–	–	–	15.2	15.2
Exercise of employee share options	0.1	–	–	–	–	–	0.1
Cost of shares vesting	–	3.7	–	–	–	(3.7)	–
At 31 December 2015	499.5	(23.0)	(146.2)	296.7	–	1,472.4	2,099.4
Loss for the year	–	–	–	–	–	(95.0)	**(95.0)**
Surplus on valuation of financial assets	–	–	–	–	272.1	–	**272.1**
Currency translation differences recycled on disposal of subsidiary	–	–	0.3	–	–	(0.3)	**–**
Currency translation differences	–	–	(104.2)	–	–	–	**(104.2)**
Total comprehensive income/(expense)	**–**	**–**	**(103.9)**	**–**	**272.1**	**(95.3)**	**72.9**
Share-based payments	–	–	–	–	–	16.7	**16.7**
Exercise of employee share options	0.9	–	–	–	–	–	**0.9**
Cost of shares vesting	–	12.8	–	–	–	(12.8)	**–**
At 31 December 2016	**500.4**	**(10.2)**	**(250.1)**	**296.7**	**272.1**	**1,381.0**	**2,189.9**

Section 1 – Basis of Preparation

This section contains the Group's going concern statement and 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. The accounting policies have been consistently applied to all the years presented.

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 2016 were authorised for issue in accordance with a resolution of the directors on 7 March 2017. 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. The registered company number is SC226712.

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 financial statements comply with the Companies Act 2006 as applicable to companies using International Financial Reporting Standards ('IFRS').

The Group's financial statements are prepared on a going concern basis.

b) Accounting standards
Cairn prepares its financial statements in accordance with applicable IFRS, issued by the International Accounting Standards Board ('IASB') as adopted by the EU, and interpretations issued by the IFRS Interpretations Committee, and Companies Act 2006 applicable to companies reporting under IFRS. The Group's financial statements are also consistent with IFRS as issued by the IASB as they apply to accounting periods ended 31 December 2016.

Effective 1 January 2016, Cairn has adopted the following amendments to standards:
- Annual improvements to IFRSs 2012-2014 Cycle
- Amendments to IFRS 10 Consolidated Financial Statements
- Amendments to IFRS 11 Joint Arrangements
- Amendments to IFRS 12 Disclosure of Interests in Other Entities
- Amendments to IAS 1 Presentation of Financial Statements
- Amendments to IAS 16 Property, Plant and Equipment
- Amendments to IAS 27 Separate Financial Statements
- Amendments to IAS 28 Investments in Associates and Joint Ventures
- Amendments to IAS 38 Intangible Assets

The adoption of these amendments has had no material impact on Cairn's results or financial statement disclosures.

The following new standards issued by the IASB and endorsed by the EU have yet to be adopted by the Group:
- IFRS 9 Financial Instruments (effective 1 January 2018)
- IFRS 15 Revenue from Contracts with Customers (effective 1 January 2018)

The adoption of these standards is not expected to have a material impact on Cairn's results or financial statement disclosures. The impact of IFRS 15 shall be further assessed on commencement of production, expected in 2017.

The following new accounting standards and amendments to existing standards have been issued but are not yet effective and have not yet been endorsed by the EU:
- IFRS 16 Leases (effective 1 January 2019)
- Amendments to IFRS 2 Share Based Payments (effective 1 January 2018)
- Amendments to IAS 7 Statement of Cash Flows (effective 1 January 2017)
- Amendments to IAS 12 Income Taxes (effective 1 January 2017)
- Clarifications to IFRS 15 Revenue from Contracts with Customers (effective 1 January 2018)

The Group is currently assessing the impact of adopting the new accounting standards noted above on its audited consolidated financial statements.

The Group has not early adopted any other standard, amendment or interpretation that was issued but is not yet effective.

Section 1 – Basis of Preparation continued

1.1 Significant Accounting Policies continued

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. Intercompany balances and transactions between Group companies are eliminated on consolidation, though foreign exchange differences arising on intercompany 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 arrangements

Cairn is a partner (joint operator) in oil and gas exploration and development licences which are unincorporated joint arrangements. All of the Group's current interests in these arrangements are determined to be joint operations. A full list of oil and gas licence interests can be found on pages 177 and 178.

Costs incurred relating to an interest in a joint operation are capitalised in accordance with the Group's accounting policies for oil and gas assets as appropriate (sections 2.1 and 2.2). All of the Group's intangible exploration/appraisal assets and property, plant & equipment – development assets are related to interests in joint operations.

Cairn's working capital balances relating to joint operations are included in other receivables (section 3.3) and trade and other payables (section 3.4). Any share of finance income or costs generated or incurred by the joint operation is included within the appropriate income statement account.

e) Foreign currencies

These financial statements continue to be presented in US dollars (US$), the functional currency of the parent.

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 (or an approximation thereof where not materially different). 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 financial statements of the parent and subsidiary undertakings in their functional currency. Where applicable, the Group translates subsidiary financial statements 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 2016	**YTD Average 2016**	Closing 2015	YTD Average 2015
Great British Pound	**0.811**	**0.738**	0.679	0.654
Norwegian Kroner	**8.640**	**8.395**	8.842	8.048

1.2 Going Concern

The directors have considered the factors relevant to support a statement of going concern.

In assessing whether the going concern assumption is appropriate, the Board and Audit Committee considered the Group cash flow forecasts under various scenarios, identifying risks and mitigants and ensuring the Group has sufficient funding to meet its current commitments as and when they fall due for a period of 12 months from the date of signing these financial statements.

The directors have a reasonable expectation that the Group will continue in operational existence for this 12-month period and have therefore used the going concern basis in preparing the financial statements.

The Board and Audit Committee assessments of risk and mitigants to the Group's operational existence beyond this 12-month period is included in the viability statement on page 40.

Section 2 – Assets and Investments: Oil and Gas Assets and Decommissioning Provisions

This section focuses on the assets in the balance sheet which form the core of Cairn's business. This section quantifies the financial impact of the operations for the year fully described in the operational review on pages 16 to 21.

Included are details of the appraisal and exploration wells in Senegal, the development projects in the UK North Sea and the impairment reviews and tests performed on the Group's assets.

Significant accounting judgements in this section:

Impairment testing of oil and gas assets and related goodwill

The Group's net book value currently remains in excess of its market value, indicating that the assets may be impaired.

Cairn reduced its long-term oil price assumption to US$70 per boe to reflect ongoing market conditions. The Group's three-year short-term assumption remains linked to the forward curve. Impairment tests resulted in impairment charges of US$11.0m against UK North Sea exploration assets in the Greater Catcher area, and US$14.3m on the Spanish Point appraisal prospect in Ireland.

Key estimates and assumptions in this section:

Impairment testing of Intangible exploration/appraisal assets and Property, plant & equipment – development assets

Where an indicator of impairment is identified on an intangible exploration/appraisal asset or a development asset, an impairment test is conducted in accordance with the Group's accounting policies. The test compares either the carrying value of the asset or the carrying value of the cash-generating unit ('CGU') containing the asset, to the recoverable amount of that asset or CGU.

The recoverable amount of an asset represents its fair value less costs of disposal. This is based on either a verifiable third party arm's length transaction from which a fair value can be obtained or, where there is no such transaction, the fair value less costs of disposal of an asset is calculated using discounted post-tax cash flow models over the field life of the asset.

The key assumptions used in the Group's discounted cash flow models reflect past experience and take account of external factors. These assumptions include:

- Short/medium-term oil price based on a three-month average forward curve for three years from the balance sheet date;
- Long-term oil price of US$70 per boe (2015: US$80 per boe) escalated at 2.0% (2015: 2.0%) per annum;
- Reserve estimates of discovered resource (2P and 2C) based on P50 reserve estimates;
- Production profiles based on Cairn's internal estimates which are not materially different from those of the operators;
- Cost profiles for the development of the field and subsequent operating costs supplied by the operator and escalated at 2.0% (2015: 2.0%) per annum; and
- Post-tax discount rates of 10% (2015: 10%).

Impairment testing of goodwill

The goodwill arising from past corporate transactions in the UK & Norway region is tested for impairment by comparing the recoverable amount against the carrying value of the underlying oil and gas assets in the UK & Norway operating segment. As with the assets above, fair value less costs of disposal are based on discounted post-tax cash flow models where 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.

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.

Decommissioning estimates

Provisions for decommissioning are based on the latest estimates provided by operators, subject to review by Cairn and adjustment where deemed necessary. Costs provided to date are an estimate of the cost that would be incurred to remove and decommission facilities that existed at the year end and to plug and abandon development wells drilled to that date. Costs are escalated at 2.0% per annum (2015: 2.0%) and discounted at a risk-free rate of 2.0% (2015: 2.0%).

Section 2 – Assets and Investments: Oil and Gas Assets and Decommissioning Provisions 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, pre-award costs, 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 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. 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.

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 assets, after testing for impairment (see below).

Proceeds from the disposal or farm down of part or all of an exploration asset are credited initially to that interest with any excess being credited 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;
- Changes in the oil price or other market conditions indicate that discoveries may no longer be commercial; 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 any property, plant & equipment – development assets within the same CGU and tested for impairment. Any impairment arising is recognised in the income statement for the year. Where there are no development assets within the CGU, the excess of the carrying amount of the exploration/appraisal asset over its recoverable amount is charged immediately to the income statement.

2.1 Intangible Exploration/Appraisal Assets continued

	Senegal US$m	UK & Norway US$m	International US$m	**Total US$m**
Cost				
At 1 January 2015	166.8	217.6	125.1	509.5
Foreign exchange	–	(20.8)	(0.5)	(21.3)
Additions	61.4	32.3	58.8	152.5
Disposals	–	(11.6)	–	(11.6)
Unsuccessful exploration costs	–	(44.2)	(100.8)	(145.0)
At 31 December 2015	228.2	173.3	82.6	**484.1**
Foreign exchange	–	(13.4)	0.3	**(13.1)**
Additions	102.1	40.9	7.5	**150.5**
Unsuccessful exploration costs	–	(28.2)	(57.7)	**(85.9)**
At 31 December 2016	**330.3**	**172.6**	**32.7**	**535.6**
Impairment				
At 1 January 2015	–	24.2	68.3	92.5
Foreign exchange	–	(1.6)	(0.5)	(2.1)
Impairment charge	–	16.7	1.2	17.9
Unsuccessful exploration costs	–	–	(47.6)	(47.6)
At 31 December 2015	–	39.3	21.4	**60.7**
Foreign exchange	–	(6.4)	0.3	**(6.1)**
Impairment charge	–	11.0	14.3	**25.3**
Unsuccessful exploration costs	–	–	(15.6)	**(15.6)**
At 31 December 2016	**–**	**43.9**	**20.4**	**64.3**
Net book value				
At 31 December 2014	166.8	193.4	56.8	417.0
At 31 December 2015	228.2	134.0	61.2	423.4
At 31 December 2016	**330.3**	**128.7**	**12.3**	**471.3**

Senegal
Cairn has drilled six wells offshore Senegal in two years; two basin-opening discoveries in 2014 and four successful exploration/appraisal wells. The four well campaign, which completed in 2016, included the BEL-1 exploration and appraisal well and the additional SNE-2, SNE-3 and SNE-4 appraisal wells. The successful appraisal programme confirmed the resource base of the SNE-1 discovery made in 2014.

Additions in the year of US$102.1m include US$78.2m of drilling costs associated with the exploration and appraisal wells completed in the period and costs of US$5.4m in preparation for the 2017 appraisal programme which commenced in January 2017 with the SNE-5 appraisal well. A further US$18.5m of non-well specific exploration costs were incurred in the year.

Capitalised costs of US$330.3m at 31 December 2016 include US$84.6m relating to the FAN-1 discovery of 2014 which has yet to be appraised.

UK & Norway
Additions in the current year of US$40.9m include the cost of two exploration wells; one completed in the Greater Catcher Area in the UK North Sea and the second being a farm-in to the unsuccessful Aurelia well in the Norwegian Barents Sea. Further additions in 2016 relate to the cost of seismic data purchase and ongoing evaluation costs on other licence areas.

The dual prospect well in the Greater Catcher Area encountered commercial volumes of hydrocarbons in the upper Laverda prospect while the deeper Slough prospect was dry. Costs, therefore, remain capitalised at the year end. The Aurelia well was unsuccessful and related costs of US$9.9m were charged to the income statement in 2016.

Further unsuccessful costs written off in the year include US$8.4m relating to the Kraken West discovery, drilled in 2015, and US$6.6m on the Grosbeak discovery, south of Skarfjell. Following further evaluation, neither discovery is now considered to be commercial.

The remaining US$3.3m of unsuccessful costs charged in 2016 relate to other licence interests relinquished in the region.

Section 2 – Assets and Investments: Oil and Gas Assets and Decommissioning Provisions continued

2.1 Intangible Exploration/Appraisal Assets continued

UK & Norway continued

During 2015 two wells were drilled; the successful Kraken West appraisal well, noted above, and the unsuccessful Crossbill exploration well. Unsuccessful costs of US$44.2m were charged to the income statement for 2015; US$23.7m on the relinquished Bonneville satellite discovery, US$12.7m on the Crossbill well and US$7.8m on other exploration licences where no further activity was planned.

Disposal proceeds of US$11.6m in 2015 arose on the farm down of a 10% working interest in the Catcher asset; refer to section 2.3 for further details.

Exploration costs remaining capitalised at the year-end of US$139.7m include costs of US$97.6m relating to discovered resource across two fields; the Norwegian Skarfjell discovery where progress towards development continues, and costs of the Laverda discovery in the UK North Sea. The remaining US$42.1m of cost has been incurred across 18 of the Group's remaining exploration licences held in the UK and Norwegian North Sea, the Norwegian Sea and the Barents Sea.

International

Unsuccessful exploration costs of US$42.1m (US$57.7m of cost net of impairment of US$15.6m) were written off on relinquished licences. US$31.7m was charged on the C-19 licence, offshore Mauritania and US$7.0m on FEL 1/14 offshore Ireland. Further costs of US$3.4m were charged on Morocco and Greenland.

Costs remaining at the year-end of US$12.3m include US$5.6m, US$5.8m and US$0.9m on Ireland, Malta and Western Sahara (Boujdour Maritime) licences respectively.

Impairment review

At the year end, Cairn reviewed its intangible exploration/appraisal assets for indicators of impairment. Indicators were identified where future exploration plans remains uncertain or where the carrying value of assets related to discovered resource may not be fully recovered through future development and production.

Impairment tests identified impairment on the Group's intangible exploration assets, resulting in a charge of US$25.3m to the 2016 income statement. Of the charge, US$11.0m relates to the Laverda discovery, within the Greater Catcher area, and US$14.3m relates to the Spanish Point appraisal prospect, offshore Ireland, within the International portfolio. The 2015 charge of US$17.9m included US$16.7m on impairment of satellite fields within the Catcher development area in the UK and Norway region and US$1.2m on Greenland licence costs.

2.2 Property, Plant & Equipment – Development Assets

Accounting policy

Costs

All costs incurred after the technical feasibility and commercial viability of producing hydrocarbons has been demonstrated are capitalised within development assets on a field-by-field basis. Subsequent expenditure is capitalised only where it either enhances the economic benefits of the development asset or replaces part of the existing development asset. Any remaining costs associated with the part replaced are expensed.

Costs of borrowings relating to the ongoing construction of development assets and facilities are capitalised during the development phase of the project. Capitalisation ceases once the asset is ready to commence production.

Net proceeds from any disposal, part disposal or farm down of development assets are credited against the appropriate portion of previously capitalised cost. A gain or loss on disposal of a development asset is recognised in the income statement to the extent that the net proceeds, measured at fair value, exceed or are less than the appropriate portion of the net capitalised costs.

Impairment

Development assets are reviewed for indicators of impairment at the balance sheet date. Indicators of impairment for the Group's development assets include:

- Downward revisions of reserve estimates;
- Increases in cost estimates for development projects; or
- A decrease in the oil price or other negative changes in market conditions.

Impairment tests are carried out on each development asset at the balance sheet date where an indicator of impairment is identified. The test compares the carrying value of an asset to its recoverable amount based on the higher of its fair value less costs of disposal or value in use. Where the fair value less costs of disposal supports the carrying value of the asset, no value-in-use calculation is performed.

If it is not possible to calculate the fair value less costs of disposal of an individual asset, the fair value less costs of disposal is calculated for the CGU containing the asset and tested against the carrying value of the assets and liabilities in the CGU for impairment. Where an asset can be tested independently for impairment, this test is performed prior to the inclusion of the asset into a CGU for further impairment tests.

If the carrying amount of the asset or CGU exceeds its recoverable amount, an impairment charge is made.

2.2 Property, Plant & Equipment – Development Assets continued

Accounting policy continued

Where there has been a charge for impairment in an earlier period that charge will be reversed in a later period where there has been a change in circumstances to the extent that the recoverable amount is higher than the net book value at the time. In reversing impairment losses, the carrying amount of the asset will be increased to the lower of its original carrying value or the carrying value that would have been determined (net of depletion) had no impairment loss been recognised in prior years.

Decommissioning

At the end of the producing life of a field, costs are incurred in plugging and abandoning wells, removing subsea installations and decommissioning production facilities. Cairn recognises the full discounted cost of decommissioning as an asset and liability when the obligation to rectify environmental damage arises. The decommissioning asset is included within property, plant & equipment – development assets with the cost of the related installation. The liability is included within provisions.

Revisions to the estimated costs of decommissioning which alter the level of the provisions required are also reflected in adjustments to the decommissioning asset. The amortisation of the asset is calculated on a unit of production basis based on proved and probable reserves. The amortisation of the asset is included in the depletion and decommissioning charge in the income statement and the unwinding of discount of the provision is included within finance costs.

	UK & Norway US$m	**Total US$m**
Cost		
At 1 January 2015	467.8	467.8
Foreign exchange	(32.5)	(32.5)
Additions	230.6	230.6
Disposals	(61.2)	(61.2)
At 31 December 2015	604.7	**604.7**
Foreign exchange	(125.2)	**(125.2)**
Additions	276.6	**276.6**
At 31 December 2016	**756.1**	**756.1**
Impairment		
At 1 January 2015	–	–
Impairment charge	25.1	25.1
At 31 December 2015	25.1	**25.1**
Foreign exchange	(4.1)	**(4.1)**
At 31 December 2016	**21.0**	**21.0**
Net book value		
At 31 December 2014	467.8	467.8
At 31 December 2015	579.6	579.6
At 31 December 2016	**735.1**	**735.1**

Significant progress was made on Cairn's two non-operated development projects in the UK North Sea. First oil production from the Kraken and Catcher fields is targeted for 2017.

In February 2016 Cairn increased its working interest in Kraken by 4.5% to 29.5%. The additional interest was acquired from First Oil plc for nominal consideration with Cairn liable for working capital liabilities that existed at the date of the agreement. US$15.8m is therefore included within additions relating to this increase. Further additions on the Kraken development were US$165.3m (2015: US$150.9), including an increase of US$26.3m (2015: US$24.5m) in the decommissioning asset.

On Catcher, additions during the year of US$95.5m (2015: US$79.7m) include US$65.2m (2015: US$70.1m), settled on Cairn's behalf by Dyas under the carry agreement detailed below in section 2.3. Additions also include US$26.5m (2015: US$7.8m) for the Catcher decommissioning asset increase.

During 2015, disposals of US$61.2m relate to the farm down of a 10% working interest in Catcher; see section 2.3.

Section 2 – Assets and Investments: Oil and Gas Assets and Decommissioning Provisions
continued

2.3 Gain on Disposal of Oil and Gas Assets
In January 2015, Cairn completed the farm down of 10% of the Group's working interest in the Catcher development, satellite fields and surrounding exploration acreage to Dyas. Under the terms of the deal, Dyas funds Cairn's exploration and development costs in respect of the licences up to a cap of US$182.0m, from an effective economic date of 1 January 2014.

On completion of the transaction, Cairn received cash proceeds of US$54.7m (US$36.5m under the carry, US$18.2m as a refund of the 10% share of costs from 1 January 2014) and recognised the remaining carry as a receivable at its discounted, post-tax fair value of US$44.7m. US$11.6m of the proceeds received were allocated to exploration assets and credited against previously capitalised exploration costs. The remaining proceeds and carry receivable were allocated to development assets.

The disposal of 10% of the Group's working interest in the development asset (with related working capital adjustments) resulted in a gain on disposal of US$26.6m and a tax credit of US$4.6m in the 2015 income statement.

2.4 Provisions – Decommissioning

	Exploration well abandonment US$m	Decommissioning of development assets US$m	**Total US$m**
At 1 January 2016	6.2	30.9	**37.1**
Foreign exchange	(1.0)	(10.3)	**(11.3)**
Unwinding of discount	0.1	0.9	**1.0**
Provided in year	–	52.8	**52.8**
At 31 December 2016	**5.3**	**74.3**	**79.6**

The decommissioning provisions represent the present value of decommissioning costs related to the Kraken and Catcher development projects. The provisions are based on operator estimates, subject to internal review and amendment where considered necessary and using assumptions based on existing technology and the current economic environment, with a discount rate of 2% per annum (2015: 2%). The reasonableness of these assumptions is reviewed at each reporting date to take into account any material changes required.

The decommissioning provisions represent management's best estimate of the obligation arising based on work undertaken at the balance sheet date. Actual decommissioning costs will depend upon the prevailing market conditions for the work required at the relevant time.

The decommissioning of the Group's development assets is forecast to occur between 2026 and 2034.

2.5 Capital Commitments

	2016 US$m	2015 US$m
Oil and gas expenditure:		
Intangible exploration/appraisal assets	**126.4**	150.3
Property, plant & equipment – development assets	**603.9**	887.9
Contracted for	**730.3**	1,038.2

Capital commitments represent Cairn's share of obligations in relation to its interests in joint operations. These commitments include Cairn's share of the capital commitments of the joint operations themselves.

The capital commitments for intangible exploration/appraisal assets primarily relate to operations in Senegal and UK & Norway.

The capital commitments for property, plant & equipment – development assets include US$395.1m (2015: US$411.0m) relating to two lease commitments due within the next eight years. The lease terms for these assets have not yet commenced. The future minimum rentals payable under these leases are aged as follows:

	2016 US$m	2015 US$m
Not later than one year	**10.4**	–
After one year but not more than five years	**219.2**	189.5
After five years	**165.5**	221.5
	395.1	411.0

The Group has no further material capital expenditure committed at the balance sheet date.

2.6 Intangible Assets – Goodwill

Accounting policy
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 CGU 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 years.

In testing for impairment, goodwill arising on business combinations is allocated from the date of acquisition to the group of CGUs 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 CGU, or group of CGUs, 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.

	UK & Norway US$m	**Total US$m**
Net book value		
At 1 January 2015	145.1	145.1
Foreign exchange	(13.2)	(13.2)
At 1 January 2016	131.9	**131.9**
Foreign exchange	(13.0)	**(13.0)**
At 31 December 2016	**118.9**	**118.9**

Goodwill is fully allocated to the UK & Norway operating segment. At 31 December 2016, the goodwill impairment test did not identify any impairment.

Section 2 – Assets and Investments: Oil and Gas Assets and Decommissioning Provisions continued

2.7 Impairment Testing Sensitivity Analysis

UK & Norway

At 31 December 2016, impairment tests were conducted on the Group's exploration/appraisal assets, development assets and goodwill. This resulted in an impairment charge of US$11.0m on exploration/appraisal assets; see section 2.1.

The recoverable amount for all assets is based on fair value less costs of disposal estimated using discounted cash flow modelling. The key assumptions used in determining the fair value are often subjective, such as the future oil price assumption, or reliant upon the performance of operational partners for delivering development projects on time and within approved budgets. With Cairn's two North Sea development projects nearing first oil production, the Group have increased confidence over the likelihood of the production commencing in line with internal estimates. Sensitivity analysis performed on delays to production did not indicate a material impact on the Group's impairment test calculations.

Cairn has run sensitivities on its long-term oil price assumption of US$70, using alternate long-term price assumptions of US$65 and US$60 and a long-term assumption equal to the forward curve price at the end of the Group's three year short term assumption.

The impact of these changes on the carrying value of the Group's assets at the balance sheet date is summarised below:

	Reduction in long-term oil price assumption to:		
	US$65 US$m	US$60 US$m	Forward Curve US$m
Impairment of intangible assets – exploration/appraisal assets	(14.0)	(16.0)	(19.0)
Impairment of property, plant & equipment – development assets	(16.9)	(58.0)	(114.7)
Impairment of goodwill	(30.5)	(93.3)	(124.3)
Total impairment	**(61.4)**	**(167.3)**	**(258.0)**

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. Cairn's reserve estimates do not materially differ from those of the operators.

Senegal

The Group's exploration assets in Senegal, containing the two 2014 discoveries, has been tested for impairment as a single cash generating unit. No impairment was identified. Further downside sensitivity performed on the Group's oil price assumption did not identify an impairment using any of the alternate price scenarios noted above.

International

The Group's portfolio of international assets was reviewed for indicators of impairment and impairment of US$14.3m was recorded on the Group's appraisal asset in Ireland. As the remaining assets in this segment are at an early stage in the exploration life-cycle, any impairment test would not be sensitive to changes in the oil price or any other key assumption; if an indicator of impairment was identified on a remaining asset that asset would be impaired in full.

Section 3 – Assets and Investments: Financial Assets and Working Capital

Cairn's liquid cash resources supported by the undrawn secured borrowing facility ensure the Group is fully funded to meet its current exploration and development programme despite the current restriction on the sale of shares in Cairn India Limited.

This section focuses on those assets, together with the working capital position of the Group at the year end.

Significant accounting judgements in this section:
Available-for-sale financial asset
The Group's 9.8% shareholding in Cairn India Limited is classified as a non-current available-for-sale financial asset and the closing book value of the asset represents the quoted market price of the Group's residual holding. Although Cairn is currently not able to sell its stake, there is no restriction in the wider market where Cairn India Limited shares trade freely at this price.

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 asset represents 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 the available-for-sale asset 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
Fair value	
As at 1 January 2015	702.6
Deficit on valuation	(318.6)
As at 1 January 2016	**384.0**
Surplus on valuation	**272.1**
As at 31 December 2016	**656.1**

The available-for-sale financial asset represents 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 or trading gains.

At 31 December 2016, the value of the investment in Cairn India Limited had increased to US$656.1m. The significant accumulated deficit during 2015 of US$318.6m was recycled to the 2015 income statement and recorded as impairment.

Cairn is currently restricted from selling its shares in Cairn India Limited. See section 5.5.

The Group is exposed to equity price risks arising from the listed equity investments it holds in Cairn India Limited.

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 the available-for-sale financial asset is recycled through the income statement.

Section 3 – Assets and Investments: Financial Assets and Working Capital 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 asset was INR 242.15 US$3.56 (2015: INR 138.10/US$2.09). The movement in the Cairn India Limited share price over the current and prior year 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 various scenarios including 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 US$ at the daily rate.

As at 31 December 2016	**Effect on loss for year US$m**	**Effect on equity US$m**
Increase to the highest share price in 2016 – INR 266 (US$3.95)	**–**	**56.4**
Decrease of 10% on closing share price in 2016 – INR 217 (US$3.21)	**–**	**(65.6)**
Decrease to the two-year average share price to 31 December 2016 – INR 180.28 (US$2.76)	**–**	**(148.4)**
Decrease to the lowest share price in 2016 – INR 110 (US$1.62)	**(85.5)**	**(357.5)**

As at 31 December 2015	Effect on loss for year US$m	Effect on equity US$m
Increase to the highest share price in 2015 – INR 259 (US$4.17)	–	359.5
Decrease of 10% on closing share price in 2015 – INR 124 (US$1.88)	(38.4)	(38.4)
Decrease to the lowest share price in 2015 – INR 123 (US$1.84)	(45.2)	(45.2)
Decrease of 20% on closing share price in 2015 – INR 110 (US$1.67)	(76.8)	(76.8)
Decrease of 30% on closing share price in 2015 – INR 97 (US$1.46)	(115.2)	(115.2)

3.2 Cash and Cash Equivalents

	2016 US$m	2015 US$m
Cash at bank	**24.0**	54.2
Short-term bank deposits	**147.7**	465.2
Money market funds	**137.5**	83.4
Tri-party repurchase transactions	**25.7**	–
Cash and cash equivalents	**334.9**	602.8

Cash and cash equivalents earn interest at floating rates. Short-term investments are made for varying periods ranging from instant access to unlimited but generally not more than three months depending on the cash requirements of the Group.

3.2 Cash and Cash Equivalents continued

Cairn invests surplus funds into high-quality liquid investments, including money market funds, short-term bank deposits and tri-party repurchase transactions ('repos'). Cairn limits the placing of such funds and other investments to banks or financial institutions that have ratings of A- or above from at least two of 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 credit default swap 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. Where investments are made in repos, collateral is fixed income debt securities with a minimum rating of BBB- which is managed by Euroclear. No adjustment is made to the counterparty credit rating to reflect the collateral held when assessing investment options. The Group's Treasury function manages the credit risk associated with such investments as detailed in note 3.6.

On 18 July 2014, Cairn Energy PLC signed a seven-year reserve-based lending facility with a syndicate of six international banks (BNP Paribas, Commonwealth Bank of Australia, DNB Bank ASA, HSBC Bank PLC, Société Générale and Standard Chartered Bank) which was effective 1 August 2014. Until completion of the Catcher and Kraken developments, the facility can be utilised to fund development costs on those projects and facility finance costs. No amounts have been drawn under the facility, with maximum available currently forecast to be US$350.0m–US$400.0m during the course of the development projects. The facility may also be utilised to issue letters of credit and performance guarantees for the Cairn Group of up to US$175.0m. Following completion, the facility can be used for general corporate purposes.

Interest on outstanding debt will be charged at the appropriate LIBOR for the currency drawn plus an applicable margin. The facility is subject to bi-annual redeterminations, has a market standard suite of covenants and is cross-guaranteed by all Group companies party to the facility. Debt is repayable in line with the amortisation of bank commitments over the period from 1 July 2018 to the final maturity date of 30 June 2021.

Details of guarantees granted under the facility can be found in note 6.3.

3.3 Other Receivables

	2016 US$m	2015 US$m
Prepayments	**21.4**	18.4
Other receivables	**58.0**	81.1
Joint operation receivables	**34.3**	49.4
	113.7	148.9

Prepayments include US$14.6m (2015: US$14.6m) of facility arrangement fees which will be amortised over the expected useful life of the facility commencing from the date the facility is drawn down.

Other receivables include US$50.6m (2015: US$43.1m) of dividends receivable from Cairn India Limited, US$2.1m (2015: US$27.4m) of the remaining Dyas carry relating to the 10% Catcher disposal (see section 2.3) and US$5.3m (2015: US$3.7m) of other amounts due. In 2015, other receivables included costs incurred by Cairn on behalf of joint operations of US$6.9m which were reimbursed during 2016. The Dyas carry was recorded at its initial fair value at the date of the transaction and is released to development assets based on the payments made by Dyas on Cairn's behalf.

Joint operation receivables include Cairn's working interest share of the receivables relating to joint operations and amounts recoverable from partners in joint operations. The Group's other receivables predominantly relate to investing and financing activities. Therefore, the movement in other receivables through operating cash flows, reported in the cash flow statement, is not significant.

At 31 December 2016 and 31 December 2015, no material amount within the Group's other receivables or joint operation receivables was past due or impaired. In determining the recoverability of other receivables the Group carries out a risk analysis based on the type and age of the outstanding receivable.

3.4 Trade and Other Payables

	2016 US$m	2015 US$m
Trade payables	**3.1**	2.6
Other taxation and social security	**2.1**	1.5
Other payables	**1.4**	1.6
Joint operation payables	**98.7**	99.5
Accruals	**17.7**	14.9
	123.0	120.1

Joint operation payables include Cairn's share of the trade and other payables of operations in which the Group participates. Where Cairn is operator of the joint operation, joint operation payables also include amounts that Cairn will settle and recover from partners.

Trade and joint operation payables primarily relate to investing activities in the cash flow statement. Movements in accruals, other taxes and other payables are recorded though operating cash flows.

Section 3 – Assets and Investments: Financial Assets and Working Capital continued

3.5 Financial Instruments

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		Fair value	
	2016 US$m	2015 US$m	**2016 US$m**	2015 US$m
Loans and receivables				
Cash and cash equivalents	**334.9**	602.8	**334.9**	602.8
Joint operation receivables	**34.3**	49.4	**34.3**	49.4
Other receivables	**58.0**	81.1	**59.2**	91.9
Available-for-sale financial assets				
Listed equity shares	**656.1**	384.0	**656.1**	384.0
	1,083.3	1,117.3	**1,084.5**	1,128.1

All of the above loans and receivables are current and held at amortised cost. There are no material impairments of loans and receivables.

Financial liabilities

Carrying amount and fair value	**2016 US$m**	2015 US$m
Amortised cost		
Trade payables	**3.1**	2.6
Joint operation payables	**98.7**	99.5
Accruals	**17.7**	14.9
Other payables	**1.4**	1.6
	120.9	118.6

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 other than provisions have a maturity of less than 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 2016 the Group held the following financial instruments measured at fair value:

Assets measured at fair value – Level 1	**2016 US$m**	2015 US$m
Available-for-sale financial assets		
Equity shares – listed	**656.1**	384.0
	656.1	384.0

3.6 Financial Risk Management: Objectives and Policies

The main risks arising from the Group's financial instruments are liquidity risk, credit risk and foreign currency risk. The Board of Cairn Energy PLC, through the Treasury Sub-Committee, reviews and agrees policies for managing each of these risks and these are summarised below. The Group is also exposed to market risk arising from equity price fluctuations on available-for-sale financial assets (see section 3.1 for details).

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

3.6 Financial Risk Management: Objectives and Policies continued
The primary financial assets and liabilities comprise cash, short and medium-term deposits, notice accounts, tri-party purchase transactions ('repos'), certificates of deposit, money market liquidity funds, listed equity shares (Cairn India Limited only), 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 issues and other forms of non-investment-grade debt finance are reviewed by the Board, when appropriate.

Liquidity risk
The Group closely monitors and manages its liquidity risk using both short and long-term cash flow projections, supplemented by debt and equity financing plans and active portfolio management. Cash forecasts are regularly produced and sensitivities run for different scenarios including, but not limited to, changes in and delays of development projects. The Group's forecasts show that the Group will be able to operate within its current debt facilities and have financial headroom for the 12 months from the date of approval of the 2016 Annual Report and Accounts.

Details of the Group's debt facilities can be found in section 3.2. The Group is subject to quarterly forecast liquidity tests as part of the debt facility agreement. The Group has complied with the liquidity requirements of this test at all times during the year. The Group runs various sensitivities on its liquidity position on a quarterly basis throughout the year. Further details are noted in the viability statement provided on page 40.

The Group currently has surplus cash that is invested in a combination of money market liquidity funds, repos, notice accounts and term deposits with a number of international and UK financial institutions, ensuring sufficient liquidity to enable the Group to meet its short and medium-term expenditure requirements.

Credit risk
Credit risk arises from cash and cash equivalents, investments with banks and financial institutions and joint operations.

Joint operation 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. These policies limit counterparty exposure, maturity, collateral and take account of published ratings, market measures and other market information. The limits are set to minimise the concentration of risks and therefore mitigate the risk of financial loss through counterparty failure. Where investments are made in repos, collateral is fixed income debt securities with a minimum rating of BBB- which is managed by Euroclear. No adjustment is made to the counterparty credit rating to reflect the collateral held when assessing investment options.

It is Cairn's policy to invest with banks or other financial institutions that firstly offer the greatest degree of security in the view of the Group and, secondly the most competitive interest rates. Repayment of principal is the overriding priority and this is achieved by diversification and shorter maturities to provide flexibility. The Board continually re-assesses the Group's policy and updates as required.

At the year end the Group does not have any significant concentrations of bad debt risk. As at 31 December 2016 the Group had investments with 13 counterparties (2015: 24) to ensure no concentration of counterparty investment risk. The reduction in the number of counterparties holding investments reflects the Group's reduced cash balance. The maturity of these investments ranged from instant access to one month.

The maximum credit risk exposure relating to financial assets is represented by the carrying value as at the balance sheet date.

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.

The Group also aims where possible to hold surplus cash, debt and working capital balances in the functional currency of the subsidiary, 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.

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 exposure to fluctuations in foreign exchange and interest rates.

The following table demonstrates the sensitivity to movements in the US$:GBP and US$:NOK exchange rates, with all other variables held constant, on the Group's monetary assets and liabilities. The Group's exposure to foreign currency changes for all other currencies is not material.

	2016		2015	
	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$	**(1.3)**	**71.8**	0.8	69.0
10% decrease in sterling to US$	**(27.0)**	**(71.8)**	(0.8)	(69.0)
10% increase in Norwegian Kroner to US$	**0.9**	**16.1**	3.6	19.6
10% decrease in Norwegian Kroner to US$	**(0.9)**	**(16.1)**	(3.6)	(19.6)

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 its three regional business units of Senegal, UK & Norway and International.

This section also includes details of employee benefits paid in the year and finance income and costs.

4.1 Segmental Analysis

Operating segments

Cairn's business model is to create, add and realise value from a balanced portfolio. To ensure focus on Senegal, while actively managing the balanced portfolio, from 1 January 2016 Cairn implemented a new organisational structure based around three groups of Senegal, UK & Norway and International. These three business units, based on geographical regions, form the Group's operating segments. Prior year comparatives have been restated to reflect the new organisational structure.

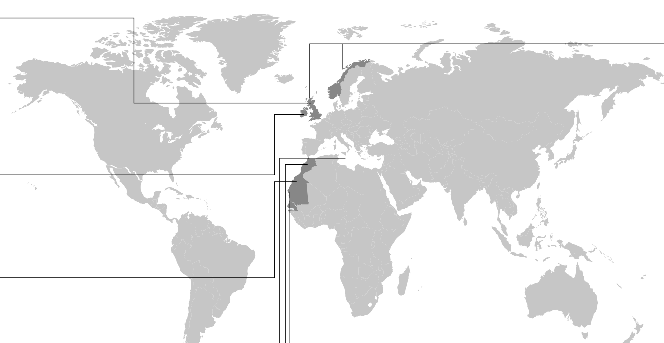
Each business unit is headed by a regional director (a regional director may be responsible for more than one business unit) and the Board monitors the results of each separately for the purposes of making decisions about resource allocation and performance assessment.

The Senegal business units focus is on appraising the successful 2014 discoveries offshore Senegal and to identify further exploration prospects for future drilling. The UK & Norway business unit includes exploration activities in the North Sea, Norwegian Sea and Barents Sea and management of the Group's development assets in the UK North Sea. The International business unit consists of all other regions where Cairn currently holds (or held during the year) exploration licences, including Greenland, Ireland, Morocco, Western Sahara, Mauritania and the Mediterranean.

The Other Cairn Energy Group segment exists to accumulate the activities and results of the holding company and other unallocated expenditure and net assets/liabilities including amounts of a corporate nature not specifically attributable to any of the business units.

Geographical information: non-current assets

Non-current assets for this purpose consist of intangible exploration/appraisal assets; property, plant & equipment – development assets; intangible assets – goodwill; and other property, plant & equipment and intangible assets.



OTHER

2016	2015
US$1.2m	US$3.6m

INTERNATIONAL

Republic of Ireland

2016	2015
US$5.6m	US$24.9m

Mauritania

2016	2015
nil	US$31.1m

Malta

2016	2015
US$5.8m	US$5.2m

Western Sahara

2016	2015
US$0.9m	nil

UK & NORWAY

UK

2016	2015
US$760.5m	US$626.9m

Norway

2016	2015
US$104.0m	US$87.0m

Goodwill (allocated to segment)

2016	2015
US$118.9m	US$131.9m

SENEGAL

2016	2015
US$330.3m	US$228.2m

4.1 Segmental Analysis continued

The segment results for the year ended 31 December 2016 are as follows:

	Senegal US$m	UK & Norway US$m	International US$m	Other Cairn Energy Group US$m	**Total US$m**
Pre-award costs	–	(8.5)	(2.8)	(6.4)	**(17.7)**
Unsuccessful exploration costs	–	(28.2)	(42.1)	–	**(70.3)**
Depreciation	–	(0.3)	–	(0.4)	**(0.7)**
Amortisation	–	–	–	(2.0)	**(2.0)**
Inventory write-down	–	–	–	(0.7)	**(0.7)**
Administrative expenses	–	(2.9)	(0.8)	(27.8)	**(31.5)**
Impairment of oil and gas assets	–	(11.0)	(14.3)	–	**(25.3)**
Operating loss	**–**	**(50.9)**	**(60.0)**	**(37.3)**	**(148.2)**
Interest income	–	0.5	–	3.5	**4.0**
Other finance income and costs	–	(2.0)	(0.1)	(5.2)	**(7.3)**
Loss before taxation	**–**	**(52.4)**	**(60.1)**	**(39.0)**	**(151.5)**
Tax credit	–	56.5	–	–	**56.5**
Profit/(loss) for the year	**–**	**4.1**	**(60.1)**	**(39.0)**	**(95.0)**
Capital expenditure	**102.1**	**318.0**	**7.5**	**0.8**	**428.4**
Total assets	**341.8**	**1,080.0**	**31.6**	**1,004.6**	**2,458.0**
Total liabilities	**16.7**	**217.6**	**17.6**	**16.2**	**268.1**
Non-current assets	**330.3**	**983.4**	**12.3**	**1.2**	**1,327.2**

Non-current assets for this purpose consist of intangible exploration/appraisal assets; property, plant & equipment – development assets; intangible assets – goodwill; and other property, plant & equipment and intangible assets.

All transactions between the segments are carried out on an arm's length basis.

Section 4 – Results for the Year continued

4.1 Segmental Analysis continued

The segment results for the year ended 31 December 2015 were as follows:

	Senegal US$m	UK & Norway US$m	International US$m	Other Cairn Energy Group US$m	Total US$m
Pre-award costs	–	(27.6)	(3.8)	(3.8)	(35.2)
Unsuccessful exploration costs	–	(44.2)	(53.2)	–	(97.4)
Inventory disposal/write-down	–	–	–	(0.2)	(0.2)
Depreciation	–	(0.3)	(0.1)	(0.6)	(1.0)
Amortisation	–	–	–	(2.4)	(2.4)
Administrative expenses	–	(2.1)	(0.3)	(23.7)	(26.1)
Impairment of oil and gas assets	–	(41.8)	(1.2)	–	(43.0)
Gain on disposal of oil and gas assets	–	26.6	–	–	26.6
Operating loss	–	(89.4)	(58.6)	(30.7)	(178.7)
Impairment of available-for-sale financial asset	–	–	–	(318.6)	(318.6)
Interest income	–	1.4	–	2.2	3.6
Interest expense	–	(0.3)	–	–	(0.3)
Other finance income and costs	–	1.1	–	(4.9)	(3.8)
Loss before taxation	–	(87.2)	(58.6)	(352.0)	(497.8)
Tax (charge)/credit	–	(27.2)	–	9.5	(17.7)
Loss for the year	–	(114.4)	(58.6)	(342.5)	(515.5)
Capital expenditure	61.4	263.1	58.8	1.9	385.2
Total assets	249.6	977.9	74.4	1,006.3	2,308.2
Total liabilities	29.4	139.5	23.1	16.8	208.8
Non-current assets	228.2	845.8	61.2	3.6	1,138.8

4.2 Pre-Award Costs

During the year, the Group incurred total pre-award costs of US$17.7m (2015: US$35.2m). US$8.5m (2015: US$15.5m) of pre-award costs were incurred in the UK & Norway, including licensing round applications. Further costs of US$9.2m (2015: US$7.4m) were incurred in pursuit of new opportunities in other regions which complement the Group's current licence interests and risk appetite. Pre-award costs include a combined US$3.9m (2015: US$17.1m) of seismic data acquisition.

In the recent 2016 APA Norwegian licensing round and the 23rd Norwegian licensing round, Cairn was awarded non-operated interests in five licences – PL853 (Cairn 40%), PL854 (Cairn 40%), PL875 (Cairn 40%), PL884 (Cairn 30%) and PL885 (Cairn 30%) and operatorship in three licences – PL856 (Cairn 75%), PL877 (Cairn 60%) and PL880 (Cairn 60%).

In the 2015 APA Norwegian licensing round, Cairn was awarded non-operated interests in four licences – PL828 (Cairn 40%), PL747B (Cairn 40%), PL840 (Cairn 20%), PL844 (Cairn 20%) and operatorship in PL842 (Cairn 40%).

4.3 Administrative and Other Expenses

	2016 US$m	2015 US$m
Administrative expenses	**34.2**	29.5
Inventory disposal/write-down	**0.7**	0.2
	34.9	29.7

Administrative expenses in 2016 include charges of US$7.2m (2015: US$4.3m) incurred defending the Group's tax position in India through the ongoing arbitration. Also included are US$3.5m (2015: US$3.3m) in respect of operating lease payments.

4.4 Employee Benefits: Staff Costs, Share-Based Payments and Directors' Emoluments

(a) Staff costs

	2016 US$m	2015 US$m
Wages and salaries	**27.9**	30.2
Social security costs	**8.2**	7.0
Other pension costs	**2.5**	2.4
Share-based payments charge	**16.7**	15.2
	55.3	54.8

Staff costs are shown gross before amounts recharged to joint operations and include the costs of share-based payments. The share-based payments charge represents amounts in respect of equity-settled options.

The monthly average number of full-time equivalent employees, including executive directors and individuals employed by the Group working on joint operations, was:

	Number of employees	
	2016	2015
UK	**132**	135
Norway	**22**	18
Senegal	**1**	–
Morocco	**1**	2
Greenland	**–**	2
Group	**156**	157

(b) Share-based payments

Income statement charge

	2016 US$m	2015 US$m
Included within gross staff costs:		
SIP	**0.7**	0.8
Share Options – Approved Plan	**0.1**	0.3
Share Options – Unapproved Plan	**1.0**	1.9
LTIP	**12.3**	11.8
Employee Share Award Scheme	**2.6**	0.4
	16.7	15.2

Details of those awards with a significant impact on the results for the current and prior year are given below together with a summary of the remaining awards.

Section 4 – Results for the Year continued

4.4 Employee Benefits: Staff Costs, Share-Based Payments and Directors' Emoluments continued

(b) Share-based payments continued

Share-based payment schemes and awards details

The Group operates a number of share award 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'):

	2016 WAFV £	2016 WAGP/WAEP £	2016 Number of shares	2015 WAFV £	2015 WAGP/WAEP £	2015 Number of shares
SIP – free shares	**2.04**	**2.04**	**225,536**	1.45	1.70	245,458
SIP – matching shares	**1.94**	**1.94**	**173,762**	1.45	1.73	209,952
Share Options – Approved Plan	**–**	**–**	**–**	0.17	1.82	393,879
Share Options – Unapproved Plan	**–**	**–**	**–**	0.17	1.84	3,705,901
LTIP	**1.35**	**1.94**	**8,866,203**	1.01	1.85	8,818,917
Employee Share Award Scheme	**1.64**	**1.98**	**1,838,606**	1.75	1.79	186,780
			11,104,107			13,560,887

The awards existing under the LTIP with the weighted average grant price ('WAGP') are as follows:

	2016		2015	
	Number	WAGP (£)	Number	WAGP (£)
Outstanding as at 1 January	**21,768,838**	**2.02**	18,024,165	2.28
Granted during the year	**8,866,203**	**1.94**	8,818,917	1.85
Exercised during the year	**(2,730,487)**	**2.80**	(486,886)	2.87
Lapsed during the year	**(833,364)**	**2.78**	(4,587,358)	2.62
Outstanding at 31 December	**27,071,190**	**1.89**	21,768,838	2.02
Weighted average remaining contractual life of outstanding awards		**1.2 years**		1.4 years

The awards existing under all share schemes other than the LTIP with the weighted average of the grant price, exercise price and notional exercise prices ('WAGP/WAEP') are as follows:

	2016		2015	
	Number	WAGP/WAEP (£)	Number	WAGP/WAEP (£)
Outstanding at 1 January	**14,916,477**	**2.03**	15,778,749	2.26
Granted during the year	**2,237,904**	**1.98**	4,741,970	1.82
Exercised during the year	**(771,363)**	**1.86**	(347,629)	1.87
Lapsed during the year	**(3,679,295)**	**2.68**	(5,256,613)	2.56
Outstanding at 31 December	**12,703,723**	**1.84**	14,916,477	2.03
Weighted average remaining contractual life of outstanding awards		**7.8 years**		7.9 years

Assumptions and inputs

The fair value of the Cairn Energy PLC LTIP scheme awards was calculated using a Monte Carlo model. The primary inputs to the model are consistent with those of the other share award schemes, 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 page 118.

The other Cairn Energy PLC share awards during 2016 were also valued using a Monte Carlo model. Awards in prior years were valued similarly. Cairn Energy PLC share options were exercised on a regular basis throughout the year, subject to the normal employee dealing bans imposed by the Company at certain times. The weighted average share price during the year was £1.902 (2015: £1.653).

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 2016, further details are below.
- 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 pages 120 and 121, over a 10-year period to the date of award.

4.4 Employee Benefits: Staff Costs, Share-Based Payments and Directors' Emoluments continued

(b) Share-based payments continued

Assumptions and inputs continued

The following assumptions and inputs apply:

Scheme name	Volatility	Risk-free rate per annum	Lapse due to withdrawals per annum
SIP	0% – 34%	0% – 1.91%	0% – 5%
Approved and Unapproved Plans	29% – 34%	0.29% – 2.71%	5%
LTIP	29% – 34%	0.29% – 2.33%	0%
Employee Share Award Scheme	0% – 31%	0% – 1.30%	5%

Employee exercise trigger point assumptions

For 2016 awards, the assumption used for the Employee Share Award Scheme awards is that employees will exercise awards equally each year over the following seven years following the three-year anniversary of the award. This assumption is modified for the LTIP awards such that awards are assumed to be exercised 10% on the three-year anniversary of the award date and 22.5% each year thereafter up until the seventh anniversary date.

(c) 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 98 to 124. Directors' remuneration, their pension entitlements, and any share awards vested during the year are 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.

	2016 US$m	2015 US$m
Short-term employee benefits	**6.0**	6.4
Termination benefits	**–**	0.7
Post-employment benefits	**0.4**	0.6
Share-based payments	**4.4**	4.4
	10.8	12.1

In addition employer's national insurance contributions for key management personnel in respect of short-term employee benefits were US$0.8m (2015: US$0.9m).

Share-based payments shown above represent the cost to the Group of key management personnel's participation in the Company's share schemes, measured under IFRS 2.

During 2016, 905,940 shares awarded to key management personnel vested under the LTIP (2015: 295,186).

4.5 Finance Income

	2016 US$m	2015 US$m
Bank and other interest receivable	**4.0**	3.6
Dividend income	**8.2**	11.6
Unwinding of discount – other receivables	**1.8**	4.6
	14.0	19.8

Dividend income is receivable from Cairn India Limited. See section 3.1.

Section 4 – Results for the Year continued

4.6 Finance Costs

	2016 US$m	2015 US$m
Bank overdraft interest	**–**	0.3
Other finance charges	**5.3**	5.8
Unwinding of discount – provisions	**1.0**	0.1
Exchange loss	**11.0**	14.1
	17.3	20.3

4.7 Earnings per Ordinary Share

Basic and diluted earnings per share are calculated using the following measures of loss:

	2016 US$m	2015 US$m
Loss and diluted loss attributable to equity holders of the parent	**(95.0)**	(515.5)

The following reflects the share data used in the basic and diluted earnings per share computations:

	2016 '000	2015 '000
Weighted average number of shares	**576,733**	576,336
Less weighted average shares held by ESOP and SIP Trusts	**(3,111)**	(5,244)
Basic and diluted weighted average number of shares	**573,622**	571,092
Anti-dilutive shares:		
LTIP awards	**18,048**	15,885
Approved and Unapproved Plans	**3,980**	365
Employee share awards	**1,629**	166
Anti-dilutive number of shares	**23,657**	16,416

Section 5 – Taxation

This section highlights the Group's taxation policies, including both the accounting policy and wider strategy and governance policies.

Analysis is provided of the Group's income statement charges and credits and deferred tax movements through the balance sheet.

Significant accounting judgements in this section:

Deferred taxation

In prior years, Cairn recognised a deferred tax asset in respect of UK North Sea oil and gas assets. This deductible temporary difference represented eligible field allowances on the Kraken and Catcher assets and tax losses available to offset future taxable profits from those assets offset by other taxable temporary differences.

At each reporting date, Cairn reviews the carrying value of deferred tax assets to assess whether it is probable that taxable profits will be available against which the Group can utilise unused tax losses and allowances which give rise to the asset.

Given the sustained low oil price forecast, Cairn does not believe that it is probable that UK North Sea assets will generate the taxable profits necessary to allow the temporary differences reflected in the deferred tax asset to be utilised in full. The Group therefore reversed its remaining deferred tax asset in the prior year. Deferred tax assets are therefore only recognised to the extent that they offset deferred tax liabilities.

Contingent liability – Indian tax

Cairn has been resolutely defending the Group's tax position in India following the tax issue raised and subsequent demand notice issued by the Indian Income Tax department. Cairn has filed a claim under the UK India bilateral investment treaty with the Indian Government and international arbitration proceedings have commenced. Based on the strengths of Cairn's legal arguments, no provision is made in the financial statements for any claim made by the Indian Income Tax Department.

Key estimates and assumptions in this section:

Future taxable profits used in determining whether it is appropriate to recognise a deferred tax asset are based on the key assumptions used in impairment testing, detailed in section 2.1. Downside sensitivities are used to determine the extent to which future taxable profits are probable.

Accounting policy

The total tax charge or credit represents the sum of current tax and deferred tax.

The current tax credit is based on the taxable 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. In Norway, tax refunds may be claimed on qualifying exploration activities and related overhead costs; the tax refundable is included as a tax credit in the period in which the qualifying expenditure is incurred.

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 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.

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 operations 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.

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.

5.1 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. Cairn's aim is 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's UK activities are focused on assets in development, with no saleable production at present, there are currently no taxable profits in the UK. Taxable profits in other jurisdictions, where Cairn's assets are in the early stages of the value creation cycle, are also minimal and as a result there were no cash payments of corporation taxes made during the year (2015: nil).

Section 5 – Taxation continued

5.1 Tax Strategy and Governance continued

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, it is acknowledged that this will not always be possible, for example where transactions are complex or there is a lack of maturity in the tax regime in the relevant jurisdiction in which the Group are operating. In such circumstances Cairn 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.

5.2 Tax (Credit)/Charge on Loss for the Year

Analysis of tax (credit)/charge on loss for the year

	2016 US$m	2015 US$m
Current tax credits:		
Norwegian tax refunds receivable	**(26.5)**	(37.1)
	(26.5)	(37.1)
Deferred tax (credit)/charge:		
Norwegian deferred tax charges	**13.3**	4.7
Reduction in UK supplementary charge tax rate	**–**	45.6
Reversal of eligibility to future field allowances on disposal of UK development asset	**–**	13.7
Release of provision on disposal of UK development asset	**–**	(18.7)
Reversal of UK deferred tax asset	**–**	22.4
Release of provision on carried interests due to change in tax rate	**(8.4)**	(3.4)
UK deferred tax credits realised	**(34.9)**	–
Recycled from other comprehensive income on impairment of financial assets	**–**	(9.5)
Total deferred tax (credit)/charge	**(30.0)**	54.8
Total tax (credit)/charge on loss	**(56.5)**	17.7
Tax included in other comprehensive income:		
Deferred tax credit on valuation of financial assets	**–**	(9.5)
Deferred tax credit on valuation movement recycled to income statement	**–**	9.5
Total tax charge in other comprehensive income	**–**	–

Norwegian deferred tax charges includes a charge of US$14.2m (2015: charge of US$5.2m) on temporary differences in respect of non-current assets and a credit of US$0.9m (2015: credit of US$0.5m) on losses and other temporary differences.

Expenditure incurred on Cairn's behalf by Dyas BV under the carry agreement (see note 2.3), capitalised in Property, plant and equipment – development assets, creates a deferred tax liability. UK deferred tax credits of US$34.9m were realised to offset this deferred tax liability.

5.2 Tax (Credit)/Charge on Loss for the Year continued

Factors affecting tax (credit)/charge for the year

A reconciliation of income tax charge 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:

	2016 US$m	2015 US$m
Loss before taxation	**(151.5)**	(497.8)
Loss before tax multiplied by the UK statutory rate of corporation tax of 20% (2015: 20.25%)	**(30.3)**	(100.8)
Effect of:		
Special tax rates and reliefs applying to oil and gas activities	**(21.2)**	(71.5)
Impact of change in UK tax rate on opening deferred tax	**–**	89.5
Impact of increase in available investment allowance	**(19.5)**	–
Impact on deferred tax of adjustments in respect of prior year	**(5.0)**	1.7
Temporary differences not recognised	**21.3**	100.5
Release of provision on carried interests due to change in tax rate	**(5.5)**	(3.4)
Foreign exchange movements	**0.1**	(1.7)
Other	**3.6**	3.4
Total tax (credit)/charge on loss	**(56.5)**	17.7

The reconciliation shown above has been based on the average UK statutory rate of corporation tax for 2016 of 20% (2015: 20.25%).

The UK main rate of corporation tax is currently 20% (21% prior to 1 April 2015).

The applicable UK statutory tax rate applying to North Sea oil and gas activities is 40%. The applicable rate applying to the prior year was 50%. The reduction in rate, enacted in September 2016, was effective from 1 January 2016. The applicable Norwegian rate applying to oil and gas activities is 78%. The change in the UK tax rate had no impact either on the Group's UK net deferred tax position at 31 December 2016 or on the tax credit for the year.

The increase in available investment allowance is a result of the increase in Cairn's working interest in the Kraken development from 25% to 29.5%. See section 2.2 for details.

5.3 Income Tax Asset

The income tax asset of US$26.1m (2015: US$33.0m) relates to cash tax refunds due from the Norwegian authorities on the tax value of exploration and other qualifying expenses incurred in Norway during the year. This refund will be received in 2017.

Section 5 – Taxation continued

5.4 Deferred Tax Assets and Liabilities

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**
Deferred tax assets				
At 1 January 2015	(82.1)	188.3	–	106.2
Foreign exchange	6.4	(9.8)	–	(3.4)
Deferred tax charge through income statement	(35.0)	(24.6)	–	(59.6)
Deferred tax movement on additions to development assets in respect of carried interests	(43.2)	–	–	(43.2)
At 1 January 2016	(153.9)	153.9	–	**–**
Foreign exchange	6.2	(6.2)	–	**–**
Deferred tax credit through income statement	(14.5)	57.9	–	**43.4**
Deferred tax movement on additions to development assets in respect of carried interests	(43.4)	–	–	**(43.4)**
At 31 December 2016	**(205.6)**	**205.6**	**–**	**–**
Deferred tax liabilities				
At 1 January 2015	(73.7)	9.1	2.9	(61.7)
Foreign exchange	10.2	(1.7)	(0.4)	8.1
Deferred tax credit through income statement	4.2	3.1	(2.5)	4.8
At 1 January 2016	(59.3)	10.5	–	**(48.8)**
Foreign exchange	(0.6)	0.1	–	**(0.5)**
Deferred tax charge through income statement	(14.4)	1.0	–	**(13.4)**
At 31 December 2016	**(74.3)**	**11.6**	**–**	**(62.7)**

Deferred tax liabilities of US$62.7m (2015: US$48.8m) relate solely to deferred tax liabilities in Norway.

Recognised deferred tax assets

As at the balance sheet date, no net deferred tax asset or liability has been recognised in the UK (2015: no net deferred tax asset or liability recognised) as other temporary differences and tax losses are only recognised to the extent that they offset the UK deferred tax liability arising on business combinations and carried interests attributable to UK Ring-Fence trading activity, as it is not considered probable that future profits will be available to recover the value of the asset given the detrimental change in market conditions continuing to impact the oil and gas industry.

A deferred tax asset has been recognised in respect of Norwegian tax losses of US$11.6m (2015: US$10.5m) against a Norwegian deferred tax liability arising from business combinations and expenditure on assets for which current tax refunds have been claimed.

5.4 Deferred Tax Assets and Liabilities continued

Unrecognised deferred tax assets

No deferred tax asset has been recognised on the following as it is not considered probable that it will be utilised in future periods:

	2016 US$m	2015 US$m
UK fixed asset temporary differences	**349.3**	294.2
UK Ring Fence trading losses	**169.3**	260.1
UK non-Ring-Fence trading losses	**3.4**	3.7
UK non-Ring-Fence pre-trade losses	**6.4**	5.5
UK excess management expenses	**305.1**	288.6
UK non-trade deficits	**68.8**	64.3
UK temporary differences on share-based payments	**37.7**	21.0
UK other temporary differences	**0.1**	0.3
Greenlandic tax losses	**1,003.9**	1,031.3
Temporary differences in respect of available-for-sale financial asset	**2.7**	274.8

At the balance sheet date, the Group has US$683.3m (2015: US$567.9m) UK Ring Fence trading losses available to offset against future UK Ring Fence trading profits. A deferred tax asset has been recognised in respect of US$514.0m (2015: US$307.8m) of these losses, offsetting in full a deferred tax liability on Ring Fence fixed asset temporary differences. No deferred tax asset has been recognised on the remaining UK Ring Fence losses of US$169.3m (2015: US$260.1m) as it is not considered probable that this amount will be utilised in future periods.

The deferred tax liability recognised on UK Ring Fence fixed asset temporary differences of US$205.6m (2015: US$153.9m) includes temporary differences in respect of investment allowances (previously field allowances) of US$693.5m (2015: US$722.2m) on the Catcher and Kraken developments which will reduce future Ring Fence profits subject to supplementary charge.

5.5 Contingent Liability – Indian Tax Assessment

Cairn UK Holdings Limited ('CUHL'), a direct subsidiary of Cairn Energy PLC, is in receipt of an assessment order from the Indian Income Tax Department ('IITD') relating to the intra-group restructuring undertaken in 2006 prior to the IPO of CIL in India, which cites a retrospective amendment to Indian tax law introduced in 2012. Cairn strongly contests the basis of this attempt to retrospectively tax the group for an internal restructuring.

The assessment order is in the amount of INR102bn (approximately US$1.5bn) plus interest backdated to 2007 totalling INR 188bn (approximately US$2.8bn). The total assets of CUHL have a value at the balance sheet date of US$749.3m (comprising principally the group's 9.8% shareholding in CIL) and any recovery by the Indian authorities would be limited to such assets.

CUHL is pursuing its rights under Indian law to appeal the assessment, both in respect of the basis of taxation and the quantum assessed. CUHL's 9.8% shareholding in CIL was originally attached by the IITD in January 2014 and CUHL continues to be restricted by the IITD from selling such shares. See section 3.1.

Furthermore, Cairn has also commenced international arbitration proceedings against the Republic of India under the UK-India Bilateral Investment Treaty (the 'Treaty'), on the basis that India's actions have breached the Treaty by (1) expropriating Cairn's property without adequate and just compensation, (2) denying fair and equitable treatment to Cairn in respect of its investments and (3) restricting Cairn's right to freely transfer funds in connection with its investment. Based on detailed legal advice, Cairn is confident that it will be successful in such arbitration.

The seat of arbitration has been agreed as The Hague in the Netherlands and Cairn has filed its Statement of Claim which clearly demonstrates that applying the retrospective amendment to Cairn and seizing US$1bn worth of CIL shares was in breach of the UK-India Investment Treaty obligations of fair and equitable treatment and its protections against expropriation. The Republic of India's Statement of Defence was filed in early February 2017 with evidential hearings now expected to take place in January 2018.

Cairn has asked the arbitration panel either to order India to withdraw its unlawful tax demand and compensate Cairn for the harm suffered by the seizure of the CIL shares, being not less than US$1.1bn (plus costs); or, if the tax demand remains in place, compensate Cairn for the quantum of the tax assessment and the harm suffered by the seizure of the CIL shares, being together not less than US$5.6bn (plus costs).

Section 6 – Capital Structure and Other Disclosures

This section includes details of Cairn's issued share capital and equity reserves.

Other disclosures include details on auditors' remuneration and post balance sheet events. Details on the Group's policy on the award of non-audit work to the auditors can be found in the Report of the Audit Committee and on the Group's web site.

Significant accounting judgements in this section:
There are no significant accounting judgements in this section.

Key estimates and assumptions in this section:
There are no key estimates or assumptions in this section.

6.1 Issued Capital and Reserves

Called-up share capital

	Number 231/169p ordinary '000	231/169p ordinary '000
Allotted, issued and fully paid ordinary shares		
At 1 January 2015	576,264	12.4
Issued and allotted for employee share options	80	–
At 1 January 2016	**576,344**	**12.4**
Issued and allotted for employee share options	**392**	**–**
Issued and allotted to ESOP trust	**500**	**–**
At 31 December 2016	**577,236**	**12.4**

Share premium

	2016 US$m	2015 US$m
At 1 January	**487.1**	487.0
Arising on shares issued for employee share options	**0.9**	0.1
At 31 December	**488.0**	487.1

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 2016 of US$1.9m (2015: US$16.7m). The number of shares held by the Cairn Energy PLC Employees' Share Trust at 31 December 2016 was 670,914 (2015: 3,721,956) and the market value of these shares was £1.6m/US$2.0m (2015: £5.9m/US$8.7m).

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 2016 of US$8.3m (2015: US$6.3m). The number of shares held by the Cairn Energy PLC Share Incentive Plan Trust at 31 December 2016 was 1,599,559 (2015: 1,158,137) and the market value of these shares was £3.8m/US$4.7m (2015: £1.8m/US$2.7m).

Foreign currency translation
Unrealised foreign exchange gains and losses arising on consolidation of subsidiary undertakings are taken directly to reserves. 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.

Merger and capital reserves
The merger reserve of US$255.9m arose in 2012 on shares issued by Cairn on the acquisition of Capricorn Norge AS. Capital reserves – non-distributable of US$40.8m, of which US$0.7m relates to Cairn Energy PLC the Company, include non-distributable amounts arising on various Group acquisitions and the capital redemption reserve arising from the 2013/2014 share buy-back programme.

Available-for-sale reserve
The available-for-sale reserve represents fair value movements on the available-for-sale financial asset (see section 3.1) which arose during 2016. As at 31 December 2015 the deficit for the year had been recycled to the income statement as impairment.

6.2 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. The Group is subject to quarterly forecast liquidity tests as part of the reserve-based lending facility. The Group has complied with the capital requirements of this test at all times during the year.

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 (see section 3.2) or undertake other such restructuring activities as appropriate. No significant changes were made in the objectives, policies or processes during the year ended 31 December 2016.

Capital and net debt were made up as follows:

	2016 US$m	2015 US$m
Continuing operations		
Trade and other payables	**123.0**	120.1
Less cash and cash equivalents	**(334.9)**	(602.8)
Net funds less payables	**(211.9)**	(482.7)
Equity	**2,189.9**	2,099.4
Capital and net funds less payables	**1,978.0**	1,616.7
Gearing ratio	**0%**	0%

6.3 Guarantees

It is normal practice for the Group to issue guarantees in respect of obligations during the normal course of business.

Details of the Group's reserve-based lending facility can be found in section 3.2. On entering into the facility certain subsidiaries granted cross-guarantees to each of the lenders.

The Group also provided the following guarantees at 31 December 2016:

- Various guarantees under the borrowing facility for the Group's operational commitments for the current year of US$1.3m (2015: US$7.6m)
- A guarantee under the borrowing facility for the Group's Associate Membership of Oil Spill Response Limited (OSRL) of US$100.0m (2015: US$100.0m)
- Parent company guarantees for the Group's obligations under joint operating agreements and other contracts.

Section 6 – Capital Structure and Other Disclosures continued

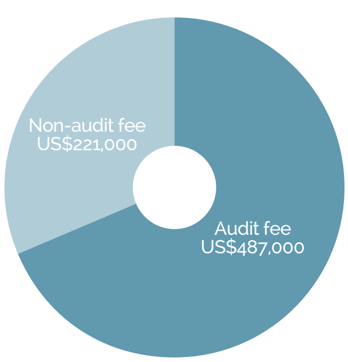
6.4 Auditors' Remuneration

	2016 US$'000	2015 US$'000
Fees payable to the Group's auditors and its associate firms for:		
Audit fees:		
Auditing of the accounts of the Group and the Company	**275**	308
Auditing of the accounts of subsidiaries	**212**	303
	487	611
Non-audit fees:		
Audit-related assurance services	**104**	109
Tax advisory services	**–**	12
Other assurance services relating to corporate finance transactions	**81**	133
Non-audit services not included above	**36**	23
	221	277
Total fees	**708**	888

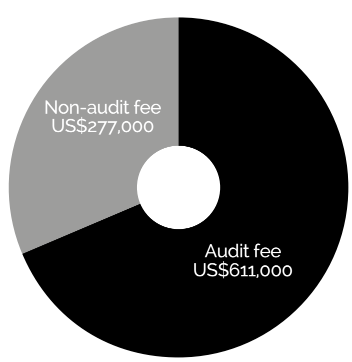
The Group has a policy in place for the award of non-audit work to the auditors which requires audit committee approval (see the Audit Committee Report on pages 91 to 95).

Fees payable to the Group's auditors in 2016 include a reduction of US$2,300 (2015: US$46,000) within audit fees and an increase of US$4,900 (2015: US$49,000) within audit-related assurance services relating to prior year work, billed in the current year and not included in prior year disclosures. The split of audit fees to non-audit fees payable to the auditors is as follows:

2016 Fees to Auditors



2015 Fees to Auditors



6.5 Post-Balance Sheet Events

FlowStream – Stream Financing Facility

On 2 March 2017, the Group secured funding of US$75m from FlowStream Commodities Ltd ('FlowStream') in exchange for the proceeds from 4.5% of Kraken production. FlowStream's entitlement to Kraken production reduces to 1.35% if FlowStream achieves a 10% return and reduces to 0.675% after FlowStream achieves a 15% return. An additional tranche of US$125m in return for further proceeds from production across Kraken and Catcher is available, subject to mutual consent, at Cairn's option. FlowStream's sole recourse for the funding is to its production from the assets. The agreement is subject to approval from the UK Oil and Gas Authority.

Exploration Finance Facility

On 3 March 2017, Cairn entered into a NOK 500m (~US$60m) Exploration Finance Facility allowing the Group to borrow against any Norwegian tax refunds from future exploration. The facility is provided by BNP Paribas and Commonwealth Bank of Australia. Interest on outstanding debt will be charged at NIBOR plus an applicable margin. The facility is available to draw until 31 December 2018 and the final maturity is 31 December 2019.

Farm-in to FEL 2/14 in Ireland

Subsequent to the year-end, Cairn has agreed a farm-in to FEL 2/14 in Ireland, with partners Providence Resources Plc (Providence) and Sosina. The 53/6-A well on the licence is planned to spud in June 2017, subject to the necessary regulatory consents, targeting both the Druid and the Drombeg targets. As a result of the proposed transaction, the equity interests in FEL 2/14 will be Providence (Operator 56%), Cairn (30%) and Sosina (14%). In the event of a potentially commercial discovery at Druid or Drombeg and joint operator approval of the drilling of an appraisal well, Cairn will have the option to take over Operatorship of the licence. Under the terms of the farm-in Cairn will pay an additional 15% share of costs, over the Group's working interest of 30%, up to a monetary cap.

The farm-in is subject to the approval of the Government of Ireland.

Company Balance Sheet
As at 31 December 2016

	Section	2016 US$m	2015 US$m
Non-current assets			
Investments in subsidiaries	7.6	**2,800.4**	2,815.5
Current assets			
Other receivables	7.3	**16.1**	17.0
Cash and cash equivalents	7.2	**–**	0.7
		16.1	17.7
Total assets		**2,816.5**	2,833.2
Current liabilities			
Trade and other payables	7.4	**61.4**	54.4
Bank overdraft	7.2	**0.4**	–
Total liabilities		**61.8**	54.4
Net assets		**2,754.7**	2,778.8
Equity			
Called-up share capital	6.1	**12.4**	12.4
Share premium	6.1	**488.0**	487.1
Shares held by ESOP/SIP Trusts	6.1	**(10.2)**	(23.0)
Capital reserves – non-distributable	6.1	**0.7**	0.7
Merger reserve	6.1	**255.9**	255.9
Retained earnings		**2,007.9**	2,045.7
Total equity		**2,754.7**	2,778.8

The financial statements on pages 169 to 176 were approved by the Board of Directors on 7 March 2017 and signed on its behalf by:

JAMES SMITH
Chief Financial Officer

SIMON THOMSON
Chief Executive

Company Statement of Cash Flows
For the Year Ended 31 December 2016

	Section	2016 US$m	2015 US$m
Cash flows from operating activities			
Loss before taxation		**(41.7)**	(15.7)
Share-based payments charge		**2.6**	2.5
Impairment of investment in subsidiary		**26.0**	–
Finance income		**–**	(0.4)
Finance costs		**5.3**	5.7
Other receivables movement		**0.9**	3.6
Trade and other payables movement		**9.9**	(13.0)
Net cash generated from/(used in) operating activities		**3.0**	(17.3)
Cash flows from investing activities			
Interest received		**–**	0.1
Net cash from investing activities		**–**	0.1
Cash flows from financing activities			
Facility, arrangement fees and bank charges		**(5.0)**	(6.2)
Proceeds from exercise of share options		**0.9**	0.1
Net cash flows used in financing activities		**(4.1)**	(6.1)
Net decrease in cash and cash equivalents		**(1.1)**	(23.3)
Opening cash and cash equivalents at beginning of year		**0.7**	24.0
Closing cash and cash equivalents	7.2	**(0.4)**	0.7

Company Statement of Changes in Equity
For the Year Ended 31 December 2016

	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 2015	499.4	(26.7)	256.6	2,049.9	2,779.2
Loss for the year	–	–	–	(15.7)	(15.7)
Total comprehensive expense for the year	–	–	–	(15.7)	(15.7)
Share-based payments	–	–	–	15.2	15.2
Exercise of employee share options	0.1	–	–	–	0.1
Cost of shares vesting	–	3.7	–	(3.7)	–
At 31 December 2015	499.5	(23.0)	256.6	2,045.7	2,778.8
Loss for the year	**–**	**–**	**–**	**(41.7)**	**(41.7)**
Total comprehensive expense for the year	**–**	**–**	**–**	**(41.7)**	**(41.7)**
Share-based payments	**–**	**–**	**–**	**16.7**	**16.7**
Exercise of employee share options	**0.9**	**–**	**–**	**–**	**0.9**
Cost of shares vesting	**–**	**12.8**	**–**	**(12.8)**	**–**
At 31 December 2016	**500.4**	**(10.2)**	**256.6**	**2,007.9**	**2,754.7**

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 largely consistent with Cairn Energy PLC Group Financial Statements. Refer to section 6.1 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 less costs of disposal calculated using the same assumptions as noted for the testing of goodwill impairment in section 2.6.

7.1 Basis of Preparation
The Financial Statements have been prepared in accordance with IFRS as adopted by the European Union.

The Company applies consistent accounting policies as applied by the 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 2016 was US$41.7m (2015: US$15.7m).

7.2 Cash and Cash Equivalents

	2016 US$m	2015 US$m
Cash at bank	**–**	0.7
Bank overdraft	**(0.4)**	–
	(0.4)	0.7

7.3 Other Receivables

	2016 US$m	2015 US$m
Prepayments	**14.9**	14.8
Other receivables	**1.2**	2.2
	16.1	17.0

Prepayments relate to facility fee incurred during 2014 which will be amortised over the expected useful life of the facility commencing from the date the facility is drawn down.

As at 31 December 2016 and 31 December 2015, no amount of the Company's other receivables were past due or impaired.

7.4 Trade and Other Payables

	2016 US$m	2015 US$m
Trade payables	**0.1**	0.1
Amounts payable to subsidiary undertakings	**59.6**	52.2
Other taxation and social security	**0.1**	0.2
Accruals	**1.6**	1.9
	61.4	54.4

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.

	2016 US$m	2015 US$m
Financial assets: Carrying amount and fair value		
Loans and receivables		
Cash and cash equivalents	**–**	0.7
Other receivables	**1.2**	2.2
	1.2	2.9

All of the above financial assets are current and unimpaired.

	2016 US$m	2015 US$m
Financial liabilities: Carrying amount and fair value		
Amortised cost		
Trade payables	**0.1**	0.1
Accruals	**1.6**	1.9
Bank overdraft	**0.4**	–
Amounts payable to subsidiary undertakings	**59.6**	52.2
	61.7	54.2

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 (2015: less than one year).

Financial risk management: risk and objectives

The Company's financial risk management policies and objectives are consistent with those of the Group detailed in Section 3.6.

The Company is not exposed to material foreign currency exchange rate risk.

Section 7 – Notes to the Company Financial Statements continued

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, estimated discounted cash flows are risk-weighted for future exploration success.

Discounted future net cash flows are calculated using an estimated short-term oil price based on the forward curve and long-term oil price of US$70 per boe (2015: long-term oil price of US$80 per boe), escalation for prices and costs of 2.0% (2015: 2.0%), and a discount rate of 10% (2015: 10%). Full details on the assumptions used for valuing oil and gas assets can be found in section 2.

	Subsidiary undertakings US$m	**Total US$m**
Cost		
At 1 January 2015	3,643.1	3,643.1
Additions	10.8	10.8
At 31 December 2015	3,653.9	**3,653.9**
Additions	10.9	**10.9**
At 31 December 2016	**3,664.8**	**3,664.8**
Impairment		
At 1 January 2015 and 31 December 2015	838.4	**838.4**
Impairment charge	26.0	**26.0**
At 31 December 2016	**864.4**	**864.4**
Net book value		
At 31 December 2014	2,804.7	2,804.7
At 31 December 2015	2,815.5	2,815.5
At 31 December 2016	**2,800.4**	**2,800.4**

Additions during the year of US$10.9m (2015: US$10.8m) relate to the Company's investment in Capricorn Oil Limited. These represent the award of share options of the Company to the employees of Capricorn Energy Limited (a principal subsidiary of Capricorn Oil Limited).

At the year end, investments in subsidiaries were reviewed for indicators of impairment and impairment tests conducted where indicators found. Given that the market capitalisation of Cairn is less than its net book value, impairment tests were conducted on all investments in subsidiaries held by the Company. The Company'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$26.0m was made to the income statement in 2016.

The Company's subsidiaries as at the balance sheet date are set out below. The Company holds 100% of the voting rights and beneficial interests in the ordinary shares of the following companies:

Direct holdings

	Business	Country of incorporation	Country of operation	Registered office address
Capricorn Oil Limited	Holding company	Scotland	Scotland	50 Lothian Road, Edinburgh, EH3 9BY
Cairn UK Holdings Limited	Holding company	Scotland	Scotland	50 Lothian Road, Edinburgh, EH3 9BY

Indirect holdings – Capricorn Oil Limited group

	Business	Country of incorporation	Country of operation	Registered office address
Agora Oil and Gas (UK) Limited	Exploration	Scotland	UK	50 Lothian Road, Edinburgh, EH3 9BY
Alba Resources Limited	Exploration	Scotland	UK	50 Lothian Road, Edinburgh, EH3 9BY
Avannaa Exploration Limited	Exploration	England	Greenland	6th Floor, 20 Berkeley Square, London, W1J 6EQ
Capricorn Energy Limited	Holding company	Scotland	Scotland	50 Lothian Road, Edinburgh, EH3 9BY
Capricorn Energy Search Limited	Exploration	Scotland	India	50 Lothian Road, Edinburgh, EH3 9BY
Capricorn Exploration and Development Company Limited	Exploration	Scotland	Morocco	50 Lothian Road, Edinburgh, EH3 9BY
Capricorn Exploration Limited	Exploration	Scotland	Scotland	50 Lothian Road, Edinburgh, EH3 9BY
Capricorn Greenland Exploration 1 Limited+	Holding company	Scotland	Scotland	50 Lothian Road, Edinburgh, EH3 9BY
Capricorn Greenland Exploration A/S	Exploration	Greenland	Greenland	Qullilerfik 2, 6, Box 1718, 3900 Nuuk, Greenland
Capricorn Ireland Limited	Exploration	Scotland	Republic of Ireland	50 Lothian Road, Edinburgh, EH3 9BY
Capricorn Malta Limited	Exploration	Scotland	Malta	50 Lothian Road, Edinburgh, EH3 9BY
Capricorn Mauritania Limited	Exploration	Scotland	Mauritania	50 Lothian Road, Edinburgh, EH3 9BY
Capricorn Norge AS	Exploration	Norway	Norway	P.O. Box 400, Sentrum, 4002, Stavanger
Capricorn Oil and Gas Tunisia GmbH	Non-trading	Switzerland	Non-trading	c/o Confidas Treuhand AG, Gubelstrasse 5, Postfach 1524, CH-6301 Zug
Capricorn Petroleum Limited	Holding company	Scotland	Scotland	50 Lothian Road, Edinburgh, EH3 9BY
Capricorn Resources Management Limited	Royalty interest	Scotland	Mongolia	50 Lothian Road, Edinburgh, EH3 9BY
Capricorn Senegal Limited	Exploration	Scotland	Senegal	50 Lothian Road, Edinburgh, EH3 9BY
Capricorn Spain Limited	Exploration	Scotland	Spain	50 Lothian Road, Edinburgh, EH3 9BY
Nautical Holdings Limited+	Holding company	England	UK	6th Floor, 20 Berkeley Square, London, W1J 6EQ
Nautical Italia SRL	Exploration	Italy	Italy	Piazza Pietro Merolli n. 2, 00151 Roma
Nautical Petroleum AG	Production	Switzerland	UK	Chollerstrasse 35, 6300 Zug
Nautical Petroleum Limited	Exploration and Development	England	UK	6th Floor, 20 Berkeley Square, London, W1J 6EQ
Transunion Petroleum Italia SRL	Exploration	Italy	Italy	Piazza Pietro Merolli n. 2, 00151 Roma
UAH Limited+	Holding company	England	UK	6th Floor, 20 Berkeley Square, London, W1J 6EQ

+ Exempt from audit under Section 480 of the Companies Act.

Section 7 – Notes to the Company Financial Statements continued

7.7 Capital Management

Capital and net debt were made up as follows:

	2016 US$m	2015 US$m
Trade and other payables	**61.4**	54.4
Cash and cash equivalents	**0.4**	(0.7)
Net debt	**61.8**	53.7
Equity	**2,754.7**	2,778.8
Capital and net debt	**2,816.5**	2,832.5
Gearing ratio	**2%**	2%

7.8 Related Party Transactions

The Company's subsidiaries are listed in section 7.6. The following table provides the Company's balances which are outstanding with subsidiary companies at the balance sheet date:

	2016 US$m	2015 US$m
Amounts payable to subsidiary undertakings	**59.6**	52.2
	59.6	52.2

The amounts outstanding are unsecured and repayable on demand and will be settled in cash.

The following table provides the Company's transactions with subsidiary companies recorded in the loss for the year:

	2016 US$m	2015 US$m
Amounts invoiced to subsidiaries	**13.7**	10.4
Amounts invoiced by subsidiaries	**6.6**	10.8

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 98 to 124.

	2016 US$m	2015 US$m
Emoluments	**3.2**	3.3
Share-based payments	**1.4**	0.3
	4.6	3.6

Pension contributions were made on behalf of directors in 2016 of US$0.2m (2015: US$0.2m).

462,065 LTIP share awards to directors vested during 2016 (2015: 120,297). Share-based payments shown above represent the market value at vesting date of these awards.

Other transactions

During the year the Company did not make any purchases in the ordinary course of business from an entity under common control (2015: US$nil).

Licence List
As at 31 December 2016

Country	Asset name	Licence	Block(s)	Operator	Cairn interest (%)
UK and Norway					
UK	KEDDINGTON	PEDL005	TF/38b & TF/49b	Egdon	10
UK	EAKRING/DUKES WOOD	PEDL118	SK/65c & SK/66d	Egdon	18.3
UK	KIRKLINGTON	PEDL203	SK/65b	Egdon	18.3
UK	LOUTH	PEDL339	TF/38c	Egdon	10
UK	KRAKEN	P1077	9/2b	EnQuest	29.5
UK	CATCHER	P1430	28/9a	Premier	20
UK	LAVERDA	P2070	28/4a	Premier	36
UK	SUNBEAM	P2077	28/8a	Premier	36
UK	KRAKEN EXTENSION	P2148	9/2c	EnQuest	29.5
UK	SCYLLA	P2149	9/6	Cairn	100
UK	EKLAND	P2184	22/18c & 22/19d	Premier	25
UK	THUNDER EXTENSION	P2198	210/29b & 210/30c	TAQA	50
NOR	KLARA	PL159C	6507/3	Statoil	18
NOR	LANGBEIN	PL159E	6507/3	Statoil	18
NOR	AURELIA	PL226	7222/1	Eni	10
NOR	AURELIA	PL226B	7222/2 & 7222/3	Eni	10
NOR	BERGAND	PL248C	35/11 (two parts)	Statoil	20
NOR	GROSBEAK	PL378	35/12 (two parts)	Wintershall	20
NOR	SKARFJELL	PL418	35/8 & 35/9	Wintershall	20
NOR	STÅLULL	PL630	31/1 & 35/10	Statoil	20
NOR	TETHYS	PL682	35/9	Bayerngas	30
NOR	DIONE	PL747	35/8	Bayerngas	40
NOR	DIONE EXTENSION	PL747B	35/8	Bayerngas	40
NOR	OFTENÅSEN	PL748	34/2 & 34/5	Aker BP	20
NOR	LYNGHAUG	PL758	6508/1, 6608/10 & 6608/11	Lundin	35
NOR	MERKUR	PL787	35/9	Bayerngas	30
NOR	MORKEL	PL788	34/9 & 35/4, 35/5, 35/7, 35/8 & 35/10	Wintershall	50
NOR	RAUDÅSEN	PL790	34/2 & 34/5	Aker BP	25
NOR	GRANNES	PL800	6508/1 & 6508/2	Lundin	35
NOR	HAVHEST	PL828	36/4	Statoil	40
NOR	DOMPAP	PL840	6608/7 & 6608/8	Statoil	20
NOR	STORHAUG	PL842	6608/10, 6608/11 & 6608/12	Cairn	40
NOR	BYHAUGEN	PL844	6609/5, 6609/6, 6609/8 & 6609/9	Dong	20
NOR	ROSSI	PL853	7322/9	Lundin	40
NOR	FLIPPER	PL854	7322/3 & 7323/1	Statoil	40
NOR	PRINSESSE	PL856	7228/11	Cairn	75

Licence List
As at 31 December 2016

Country	Asset name	Licence	Block(s)	Operator	Cairn interest (%)
International					
Ireland	SPANISH POINT	FEL 2/04	35/8, 35/9	Capricorn Ireland Ltd	38
Ireland	SPANISH POINT NORTH	FEL 4/08	35/2b, 35/3b, 35/4a	Capricorn Ireland Ltd	38
Ireland	LO 16/18	LO 16/18	34/29, 34/30, 35/26, 43/4, 43/5, 44/1	Capricorn Ireland Ltd	100
Malta	BLOCKS 1, 2 and 3	Area 03	N/A	Capricorn Malta Ltd	60
Morocco	BOUJDOUR MARITIME	Boujdour Maritime	I-XVII	Kosmos Energy LLC	20

Country	Asset name	Licence	Block(s)	Operator	Cairn interest (%)
Senegal					
Senegal	RUFISQUE OFFSHORE, SANGOMAR OFFSHORE AND SANGOMAR DEEP OFFSHORE	Sangomar-Rufisque	N/A	Capricorn Senegal Ltd	40

Glossary

The following are the main terms and abbreviations used in this report:

Corporate

3Rs	Cairn core values: Respect, Relationships and Responsibility
AGM	Annual General Meeting
Board	the Board of Directors of Cairn Energy PLC
Cairn	Cairn Energy PLC and/or its subsidiaries as appropriate
Cairn India/CIL	Cairn India Limited and/or its subsidiaries as appropriate
Capricorn	Capricorn Oil Limited and/or its subsidiaries as appropriate
CEO	Chief Executive Officer
CERT	Crisis and Emergency Response Team
CFO	Chief Financial Officer
Company	Cairn Energy PLC
COO	Chief Operating Officer
CR	Corporate Responsibility
CRMS	Corporate Responsibility Management System
CSL	Capricorn Senegal Limited
CUHL	Cairn UK Holdings Limited
ELT	Exploration Leadership Team
ESOP	employee share trust
FAN	FAN oil discovery
Group	the Company and its subsidiaries
IMT	Incident Management Team
IS	information systems
LTIP	Long Term Incentive Plan
MT	Management Team
RMC	Risk Management Committee
SIP	Share Incentive Plan
SLT	Senior Leadership Team
SNE	SNE oil discovery

Other

1C	Denotes low estimate scenario of contingent resources
1P	Proved reserves, denotes low estimate scenario
2C	Denotes best estimate scenario of contingent resources
2D/3D	two-dimensional/three-dimensional
2P	Proved plus probable reserves, denotes best estimate scenario
3C	Denotes high estimate scenario of contingent resources
3P	Proved plus probable plus possible reserves, denotes high estimate scenario
ABC	anti-bribery and corruption
ALARP	as low as reasonably practicable
APA	awards in predefined area (Norwegian licensing rounds)
AQI	Audit Quality Inspection
bbl	barrel
bn	billion
boe	barrel(s) of oil equivalent
boepd	barrel(s) of oil equivalent per day
BOP	blow out preventer
bopd	barrels of oil per day
bps	basis points
BST	British Standard Time
capex	capital expenditure
CDS	credit default swap
CIL	Cairn India Limited
CIS	Commonwealth of Independent States
COP21	2015 Paris Climate Conference
CSR	corporate social responsibility
DC	drill centre
DECC	Department of Energy and Climate Change
DEFRA	Department for Environment Food & Rural Affairs
E&A	exploration and appraisal
E&P	exploration and production
EAA	environmental area assessment
EIA	Environmental Impact Assessment
EITI	Extractive Industries Transparency Initiative
ERP	enterprise resource platform
ESA	exploration study agreement
ESIA	Environmental and Social Impact Assessment
EU	European Union
EY	Ernst & Young LLP
FDP	field development plan
FEED	front end engineering design
FEL	frontier exploration licence
FID	final investment decision
FPSO	floating production, storage and offloading
FRC	Financial Reporting Council
ft	foot
GBP	Great British Pound
GHGs	greenhouse gases
GMT	Greenwich Mean Time
GRI	Global Reporting Initiative
H1/2	first/second half
HR	human resources
HRIA	Human Rights Impact Assessment
HSE	health, safety and environment
HSSE	health, safety, security and environment
IAS	International Accounting Standards

Glossary continued

Other

IASB	International Accounting Standards Board
IFC	International Finance Corporation
IFRS	International Financial Reporting Standards
IIP	Investors in People
IITD	Indian Income Tax Department
INDC	intended national determined contribution
INR	Indian rupee
IOGP	International Association of Oil & Gas Producers
IP	investment proposal
IPCC	Intergovernmental Panel on Climate Change
IPIECA	International Petroleum Industry Environmental Conservation Association
IPO	initial public offering
ITT	invitation to tender
JV	joint venture (referring to industry term, not IFRS definition)
KPI	Key Performance Indicator
LIBOR	London Interbank Offered Rate
LPI	leading performance indicator
LTI	lost time incident/injury
LTIF	lost time injury frequency
m	million
mmbbls	million barrels of oil
mmboe	million barrels of oil equivalent
mmbopd	million barrels of oil per day
MMO	marine mammal observer
mmscfd	million standard cubic feet of gas per day
MSA	Modern Slavery Act
MSG	multi stakeholder group
NCS	Norwegian Continental Shelf
NGO	non-governmental organisation
NIBOR	Norwegian Interbank Offered Rate
NOC	national oil company
OECD	Organisation for Economic Co-operation and Development
ONHYM	Office National des Hydrocarbures et des Mines
OPEC	Organisation of Petroleum Exporting Countries
opex	operating expenditure
OSPAR	(Oslo/Paris) Convention for the Protection of the Marine Environment of the North-East Atlantic
P10	estimate with a 10% probability of being equal or exceeded, low degree of certainty
P50	estimate with a 50% probability of being equal or exceeded, medium degree of certainty
P90	estimate with a 90% probability of being equal or exceeded, high degree of certainty
PCDP	Public Consultation and Disclosure Plan
PDMR	person discharging managerial responsibility
PDP	project delivery process
PSC	production sharing contract
PwC	PricewaterhouseCoopers LLP
Q1/2/3/4	quarter 1/2/3/4
RBL	reserves-based lending
SDGs	United Nations Sustainable Development Goals
STOIIP	stock-tank oil initially in place
TD	target depth
TRIR	total recordable injuries rate
TSR	total shareholder return
TVDSS	total vertical depth sub sea
UK	United Kingdom
UKCS	UK Continental Shelf
UN	United Nations
UNGC	United Nations Global Compact
US$	United States of America dollar
WEC	well engineering and construction
WI	working interest
YE	year-end
YTD	year to date

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