



# Delivering value from discovery and development



# Delivering value from discovery and development

Cairn Energy PLC is an independent oil and gas exploration and development company listed on the London Stock Exchange.

*Cairn has its headquarters in Edinburgh, Scotland with additional offices in London, Norway and Senegal.*

*Cairn has discovered oil and gas in a variety of locations throughout the world. Today the business holds a balanced portfolio of exploration and development assets and is focused on three geological regions: the Atlantic Margin, North West Europe and the Mediterranean.*







2014 key story – Read more on page 13

Senegal

## Basin opening exploration success

Cairn has discovered oil in the first and second wells of its Senegal exploration programme, opening a new basin on the Atlantic Margin.

*Cairn's exploration and appraisal assets in the Atlantic Margin, North West Europe and the Mediterranean are underpinned by its core development assets in the North Sea.*



North Sea

## Developing a sustainable business

Kraken and Catcher, two major North Sea fields, are the Group's core development projects and will provide free cash flow from 2017.

2014 key story – Read more on page 17

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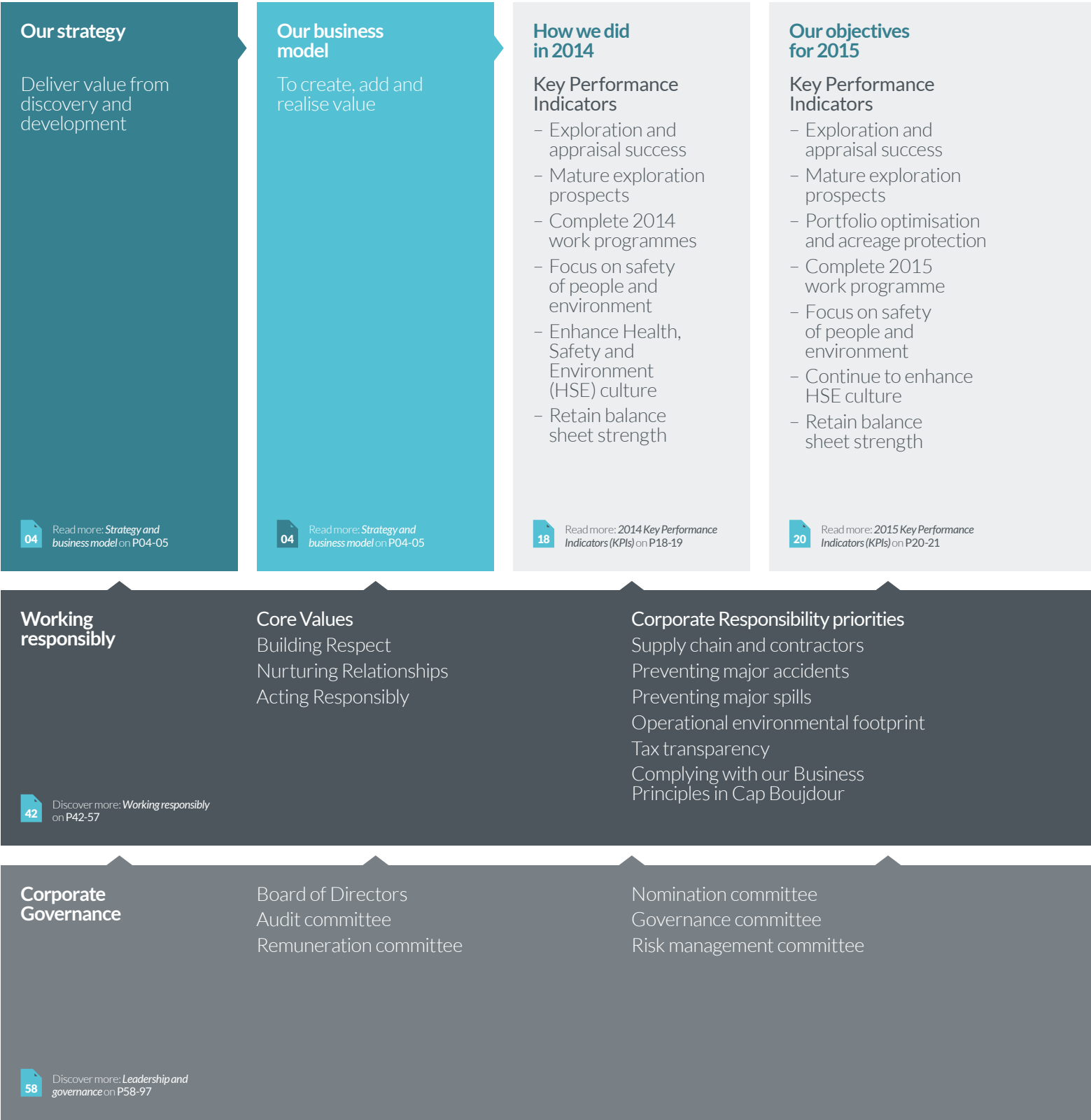
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### The principal risks we are managing

- Lack of exploration success
- Execution of North Sea developments
- Restriction on sale of Cairn India Limited shareholding
- Operational and project performance

34 Read more: *How we manage risk* on P34-41

*“Cairn enters 2015 in a strong position with further drilling planned in Senegal to evaluate the scale of this world class asset. We are preparing, along with our joint venture partners, for a multi-well exploration and appraisal programme that has the ability to add substantial value for the company and all stakeholders.*

*In the last twelve months, we have actively managed the portfolio and streamlined the business to provide the Group with continued financial flexibility to deliver our active exploration, appraisal and development programmes.”*

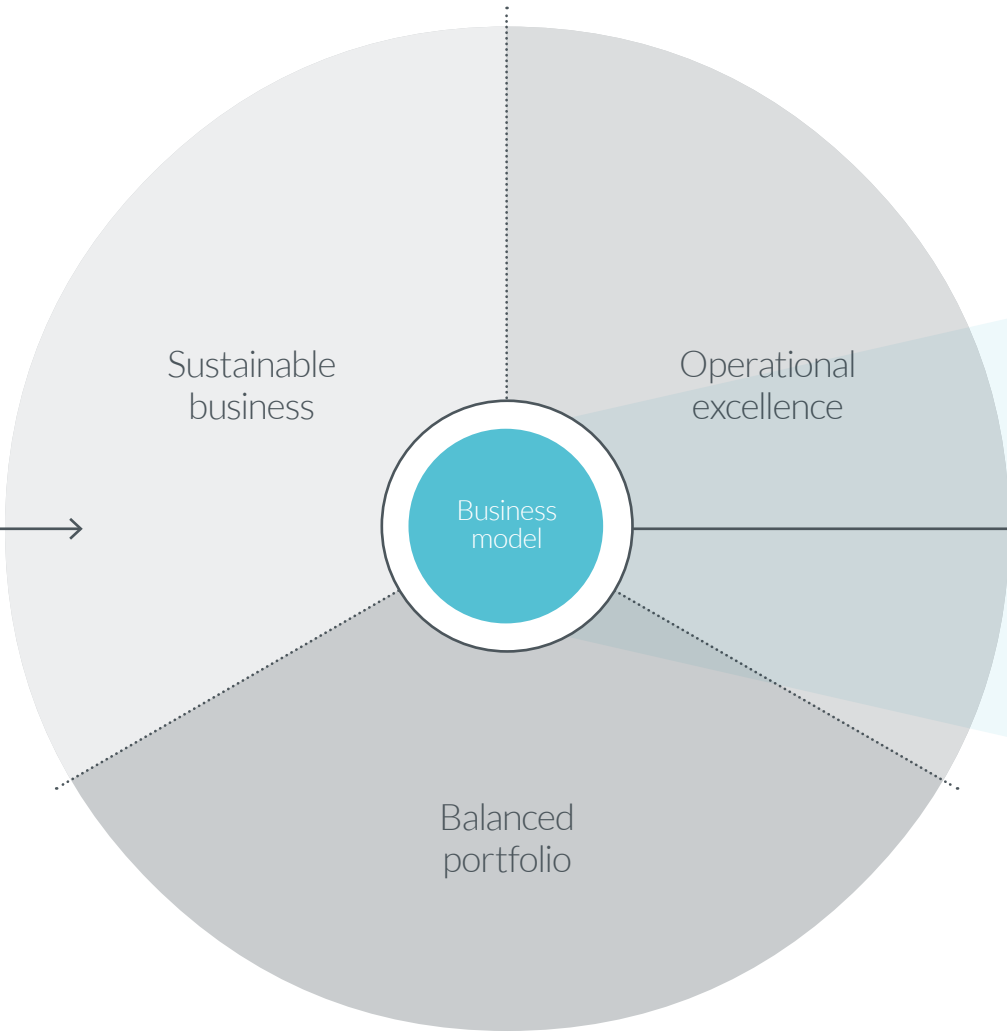
**Simon Thomson**  
Chief Executive

# Delivering value in 2014

Our strategy

Cairn’s strategy is to deliver value from discovery and development.

Cairn has the following Key Performance Indicators in place to monitor delivery of strategy.



## Delivering a sustainable business

What were our objectives in 2014 and what will they be in 2015?  
Maintain a self funding business plan.

How we delivered in 2014

- Secured a seven-year debt facility of up to US\$575m to part fund core North Sea developments
- Reduced capital expenditure prior to delivering free cash flow by ~US\$380m by selling a 10% interest in Catcher development (completed 2015)
- Reduced ongoing cost base through group reorganisation
- Continued to pursue release of restriction on Cairn India Limited shareholding

18 Discover more: 2014 Key Performance Indicators (KPIs) P18-19

## Maintaining a balanced portfolio

What were our objectives in 2014 and what will they be in 2015?  
Grow the reserves and resources base to provide a basis for future growth.

How we delivered in 2014

- Discovered oil offshore Senegal in both wells drilled in Senegal exploration programme
- Initiated non-operated well offshore Western Sahara
- Progressed the North Sea developments which remain on budget and on track for first oil in 2017
- Booked 2P reserves on Catcher development and 2C resources in Senegal
- Matured prospects in Senegal, Morocco and Norway to drill-ready status in 2015/2016
- Participated in UK 28th Licensing Round and Norwegian 2014 APA Licensing Round

18 Discover more: 2014 Key Performance Indicators (KPIs) P18-19

## Seeking operational excellence

What were our objectives in 2014 and what will they be in 2015?  
Deliver operational excellence in all activities and maintain licence to operate.

How we delivered in 2014

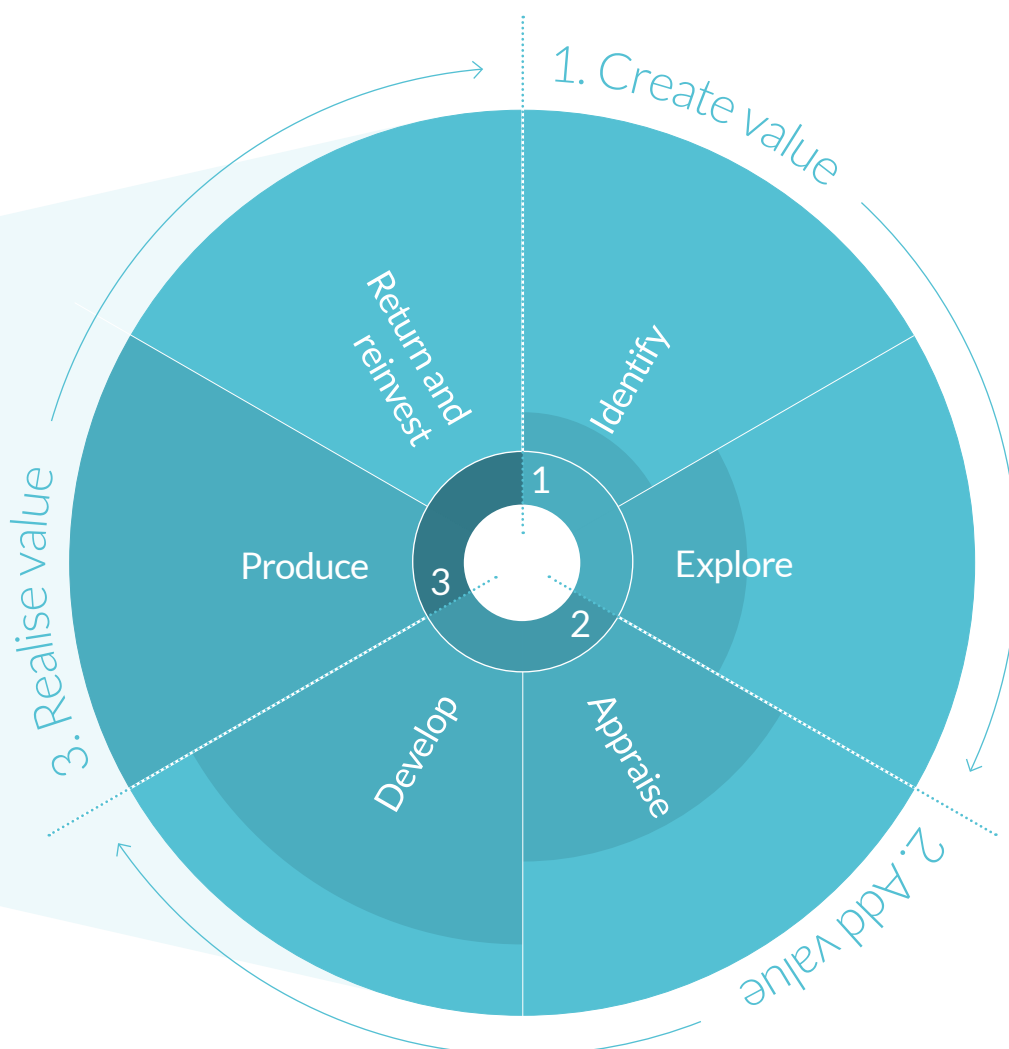
- Operated drilling programme with two wells offshore Senegal and one well offshore Morocco
- Two operated seismic campaigns offshore Malta and Republic of Ireland
- No spills to the environment
- Despite focus on safety, one Lost Time Incident (LTI) occurred; incident was thoroughly investigated and measures taken to avoid similar incidents happening again

18 Discover more: 2014 Key Performance Indicators (KPIs) P18-19

## Our business model

Cairn's business model is to create, add and realise value throughout the oil and gas life-cycle within a sustainable, self funding business.

Throughout this process the portfolio is closely managed to ensure assets are delivering optimum value.



## 1. Create value

Cairn seeks to create value through the discovery of hydrocarbon resources. Opportunities are accessed from the existing portfolio, from government licensing rounds and through acquisition.

### How we delivered in 2014

- Made two significant oil discoveries offshore Senegal
- Applied for and awarded interests in both the UK and Norwegian licensing rounds
- Farmed-in to Group's first licence in the Barents Sea, an emerging region
- Applied for Norwegian operatorship

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Discover more: *Operational review*  
P22-27

## 2. Add value

Cairn looks to add value through optimising existing assets, seeing hidden value in assets that others may have overlooked, and through asset swaps and exchanges.

### How we delivered in 2014

- Received approval for the Field Development Plan (FDP) of the Catcher development, a major UK North Sea field, from the UK Department of Energy and Climate Change (DECC)
- Catcher and Kraken developments remain on track for first oil in 2017
- Booked 2P reserves on Catcher development and 2C resources in Senegal

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Discover more: *Operational review*  
P22-27

## 3. Realise value

Cairn has a proven track record of realising value for shareholders and then reinvesting in the business as well as returning cash to shareholders. Cairn is careful to maintain a strong balance sheet which can fund the Group's exploration programmes which offer growth opportunities.

The success of Cairn's exploration and investment in India allowed the company to return a total of US\$4.5 billion to shareholders in the last six years.

### How we delivered in 2014

- Sold a 10% interest in the Catcher development project, reducing capital expenditure by ~US\$380m, whilst importantly continuing to benefit from the remaining 20% stake in the development (completed 2015)
- Continued to pursue release of restriction on Cairn India Limited shares

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Discover more: *Operational review*  
P22-27



# Highlights of 2014

## Financial

- Group net cash at 31 December 2014 of US\$869m
- Seven year Reserve Based Lending bank facility of up to US\$575m remains undrawn
- Cairn is currently unable to access the value of its ~10% residual shareholding in Cairn India Limited (CIL) valued at US\$703m at 31 December 2014
- Completion of a farm out agreement to Dyas UK Limited for the sale of 10% interest in the Catcher development in the UK North Sea
- A total of 56.1 mmbbl booked as 2P reserves at 31 December 2014 and 171.6 mmbbl booked as 2C Contingent Resources on a net working interest basis

## Exploration

### Atlantic Margin – Senegal

- FAN-1 discovered high quality, light oil in multiple stacked deepwater fans, SNE-1 discovered high quality oil in the upper clastic target of the Shelf Edge prospect; Senegal evaluation plan to be submitted by Joint Venture (JV), Cairn Operator 40% Working Interest (WI), Q2 2015
- Preliminary estimates of the gross Contingent Resource for SNE-1: P50, 330 mmbbls recoverable. Initial gross STOIP estimates for the FAN-1 well: P50, 950 mmbbls. Resource estimates confirmed by ERC Equipoise Ltd audit
- Based on early evaluation, a programme of three firm and three optional exploration and appraisal wells is envisaged to begin in 2015
- Capital Markets Day on Senegal on 11 May 2015

### Atlantic Margin – Western Sahara

- Exploration well in Cap Boujdour contract area completed in March 2015 (Kosmos Operator, Cairn 20% WI). Well encountered hydrocarbons but the discovery was non-commercial and the well has been plugged and abandoned

### North West Europe

- Catcher and Kraken developments in the UK North Sea on track for first oil from 2017; targeted peak net production to Cairn of ~22,500 boepd
- Catcher
  - Field Development Plan approved Q2 2014 now in execution phase
  - Development drilling scheduled to commence in the middle of 2015
  - Construction of the FPSO hull started in Q1 2015
- Kraken
  - Development drilling scheduled to commence in the middle of 2015
  - FPSO construction continues in Singapore and fabrication of main process modules has started
- Programme of non-operated wells in North Sea:
  - Three wells completed in 2014, Ensis and Atlas in Norway and Aragon in the UK – all three wells were plugged and abandoned
  - West of Kraken, UK North Sea (EnQuest Operator, Cairn 25% WI) operations are close to completion
  - Crossbill, Norwegian North Sea (Wintershall Operator, Cairn 20% WI), operations to commence in Q2 2015
  - Additional non-operated wells for 2015 remain subject to final investment decision within the different partnerships
- UK 28th Licensing Round awards: Cairn was awarded four licences in Q4 2014
- Norwegian 2014 Licensing Round: Cairn was awarded five licences in Q1 2015
- Process to pre-qualify as Operator in Norway under way
- Pursuing recent entry into Barents Sea with possible applications in 23rd Licence Round in late 2015



## Chairman's statement

Ian Tyler

## Cairn is well positioned



*2014 was a challenging year both for Cairn and for the wider E&P industry. In January, Cairn was notified of the previous Indian Government's decision to freeze our 10% holding in Cairn India Limited, following the introduction of retrospective tax legislation.*

**Ian Tyler**  
Chairman  
9 March 2015

During the second half of the year and continuing into 2015, oil prices have fallen sharply, causing all players in the sector to reassess capital plans and focus on cost efficiency. On a more positive front, the Senegal discoveries in Cairn's significant acreage position offshore West Africa provide a material opportunity for the company to create substantial shareholder value from a potentially world class asset.

During the year, we reconfirmed our strategy to deliver value from discovery and development within a sustainable, self-funding business model. Cairn is well positioned with a strong balance sheet and is well funded through to cash flow sustainability from our North Sea assets. Furthermore, management's early action, which included a fundamental rationalisation of the business whilst retaining our core geological and exploration skills, has ensured that the company can operate effectively in the current low oil price environment.

Senegal presents an exciting opportunity which we continue to evaluate. As a result of the reduction in oil prices, Cairn is able to benefit from substantially lower industry costs as we prepare for the 2015 appraisal and exploration programme.

In India, we note the comments made by the new BJP Government about the impact of retrospective tax legislation and the negative signal it sends to the international investment community. Our approach to date has been to focus on engagement with the Government of India and resolving this matter clearly continues to be a high priority.

Following the 2014 AGM, as part of our long term succession planning, a number of significant changes to the Board took effect: Sir Bill Gammell retired as non-executive Chairman and I succeeded him in this role. Dr Mike Watts, Deputy Chief Executive and Jann Brown, Managing Director and Chief Financial Officer stepped down as Executive Directors. James Smith was appointed as Chief Financial Officer. James joined in March 2014 from Rothschild where he had been a longstanding adviser to Cairn. Finally, Dr James Buckee retired as a non-executive director. After standing down as Executive Directors, Mike and Jann continued in senior roles for six months focused entirely on seeking to resolve the tax situation in India.

I would like to recognise and thank both our employees and our contractors for all their hard work and diligence in getting Cairn through a difficult year in 2014 and into a position of strength as we look forward to 2015.

# Two significant discoveries offshore Senegal



*Cairn's strategy is to create and deliver value from the discovery and development of hydrocarbon resources. We achieve this from a balanced portfolio and a sustainable, self-funding business model.*

**Simon Thomson**  
Chief Executive  
9 March 2015

The combination of balance sheet strength, development stage assets with a clear path to cash flow generation and a balanced exploration and appraisal portfolio allows the Company to fund future exploration activity and to repeat the cycle of creating, adding and realising shareholder value. In 2014, we positioned the Group for future growth by:

- i. Discovering oil offshore Senegal in both wells drilled in the exploration programme.
- ii. Participating successfully in the UK 28th Licensing Round and Norwegian 2014 APA Licensing Round.
- iii. Selective farm-ins and farm-downs, including the sale of a 10% interest in the Catcher development in the North Sea.
- iv. Accelerating the financing of our development projects.
- v. Progressing the Catcher and Kraken developments, which remain on track with free cash flow generation anticipated from 2017.
- vi. Maturing prospects across our portfolio to drill ready status for 2015/16.
- vii. Booking 2P Reserves on the Catcher development and 2C Resources in Senegal.

2014 was marked by two significant discoveries offshore Senegal, successfully opening a new hydrocarbon basin, with the SNE-1 discovery recognised as potentially the largest global oil discovery in 2014. The discoveries occur in two separate plays and have significant follow on potential within our acreage.

The Cairn team planned and executed a safe and successful two well exploration campaign in less than 20 months following the initial announcement of the farm-in to Senegal in early 2013. The strong JV partnership comprising Petrosen, ConocoPhillips and FAR Limited with Cairn as the Operator, has a shared vision of the prospectivity and potential of our large acreage position.

*“We start 2015 in a strong position to deliver an exciting programme across the portfolio, especially in Senegal, which has the potential to add substantial value beyond the discoveries made to date.”*

We have established an office in Dakar with a local and international team who are working closely with the Government, suppliers and local communities. I was delighted to lead a country visit in November 2014 along with executive management from ConocoPhillips to meet with President Macky Sall. We were encouraged by the support of the Senegalese authorities, and we all recognise that these discoveries, in the longer term, are potentially transformational for Senegal as a country, as well as for Cairn.

Cairn’s exploration and appraisal assets in the Atlantic Margin, North West Europe and the Mediterranean are underpinned by Kraken and Catcher, two major North Sea development projects. The future cash flows from these projects will support a self-funding, sustainable business model over the medium and long term. From 2017, we anticipate free cash flow from these assets with a production estimate of around 22,500 barrels of oil equivalent per day net to Cairn. We keep a disciplined focus on projects right across our portfolio to ensure they deliver strong returns even in a lower oil price environment and our North Sea development investments are in line with that strategy.

In early 2014, Cairn received notice from the Income Tax Department of India citing 2012 retrospective legislation and requesting information relating to a group reorganisation in 2006. At the same time, the Income Tax Department restricted Cairn from accessing the value of its remaining ~10% shareholding in Cairn India Limited (CIL), then valued at ~US\$1billion.

The freezing of our asset in India was an unexpected event and measures were swiftly introduced to ensure that the Company remained able to deliver its work programme and long-term strategy in the absence of access to these funds.

First of all, the timetable for bringing in debt financing for our North Sea development activities was accelerated. A Reserve Based Lending bank facility of US\$575m was put in place in July and this currently remains undrawn.

Secondly, the business was re-organised to ensure we had the right size of company for the work programme ahead. The priority was to retain and protect the core technical, commercial and financial competencies which form the foundation of Cairn whilst outsourcing non-core capabilities and reducing costs. The resulting new organisational structure was completed in early 2015 with a 40% reduction in the number of employees and contractors in the business.

Thirdly, we looked to re-balance our portfolio. In September, we announced a farm out agreement to Dyas UK Limited for the sale of a 10% interest in the Catcher development and adjacent acreage in the UK North Sea for a carry of Cairn’s exploration and development costs up to a cap of US\$182m, effective from 1 January 2014. As a result of this transaction, which was successfully completed in January 2015, Cairn reduced forward capital expenditure to the end of 2017 by ~US\$380m and also retained a 20% working interest in the Catcher licence with first oil expected from 2017.

The above measures strengthened our financial position and our ability to create and deliver value through a sustainable, repeatable and self-funding business model.

Outlook

We start 2015 in a strong position to deliver an exciting programme across the portfolio, especially in Senegal, which has the potential to add substantial value beyond the discoveries made to date. We have built a diverse and balanced portfolio and created the financial flexibility to progress our exploration, appraisal and development programmes and ensure ongoing strategic delivery.



Simon Thomson, CEO and Macky Sall, President of Senegal.



Industry overview

Dr Julian Fennema and Erkal Ersoy, CEERP, Heriot-Watt University

How industry context drives Cairn’s strategy

“Globally the largest oil discovery was in Senegal by Cairn Energy.”

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 Management and Languages; School of Life Sciences; and the Energy Academy as well as honorary academics outwith the University.

This industry overview provides an independent view of the industry background against which Cairn operates.

Uneven fragile growth

Global economic recovery, however slow, persisted throughout 2014, but downside risk also left its mark in the overall economic environment.

Amongst the advanced economies, the United States, the United Kingdom and Canada have all experienced growth rates in excess of 2% year on year, but were the select few to buck the trend: the Eurozone and Japan have grown at less than 1%, pulling the OECD average growth rate down to a lacklustre 1.8%<sup>1</sup>.

Within non-OECD countries, China’s economic structural transformation led to a moderation in growth, slowing to 7.4% year on year through 2014, thereby also slowing oil consumption growth. Despite this, China’s imports of oil continued to increase, and the country remained the second-largest consumer of oil after the US. Elsewhere, slower than expected economic growth in, amongst others, Brazil and Russia have restrained oil demand growth, limiting the previous upwards pressure from the emerging economies. Overall, therefore, global demand remained approximately constant as upward movements counteracted downward ones elsewhere – aggregate demand for oil products rose by 0.7 Mb/d to 92.4 Mb/d<sup>2</sup>.

Oil supply outstrips demand

In the presence of this stable demand, the supply side played the pivotal role in price determination within the crude oil market, and both OPEC and non-OPEC sources contributed to a supply expansion of 2.1 Mb/d compared to 2013. The resulting supply-demand imbalance drove the Brent price below \$60 per barrel in December 2014, from over \$100 per barrel at the start of the year.

The main contributor to this supply expansion was the US as its oil production, particularly of LTO<sup>3</sup>, grew by 1.5 Mb/d overall. However, the key story of the oil markets for 2014 was the decision by OPEC to maintain supply instead of reducing their quota of 30 Mb/d crude oil production on 27 November 2014 despite the tumbling oil price and continued expectations of excess supply to the market into 2015. Whilst creating significant short-term pressure within OPEC countries reliant on oil revenues, the longer-term strategy behind this decision is widely held to be one of “survival of the cheapest”, to pressurise capital investment in higher-cost production such as US shale or deep-water so that this supply does not reach the market and erode the OPEC market share<sup>4</sup>.

Strategies and margins under pressure

The shorter-term effect of the falling crude price, evident through 2014, is the squeezing of margins and pressure on cash flows in the sector. The largest of private sector actors, the supermajors, are, with a few exceptions, under pressure to reimpose budget discipline due to very large development projects absorbing available capital. As a result, and as a means to generate cash to return to shareholders, their exploration expenditure is being trimmed back and assets divested allowing them to concentrate on a core set of projects already in the pipeline.

Overall, the exploration spend followed a lower-risk strategy, away from the more speculative frontier<sup>5</sup> activity of recent years to exploration in mature areas, opening new areas of already proven basins. Activity has softened in the vibrant offshore areas in Brazil and East Africa as these plays move into an evaluation and development phase, but elsewhere in Africa significant exploration success was booked in 2014.

“This fall in exploration and appraisal costs is an outcome of supply and demand interaction.”

Whilst, globally, the largest single find was the Pobeda gas discovery in Russia’s Kara Sea, the largest oil discovery was in Senegal by Cairn Energy, with also significant discoveries in West Africa, in Côte d’Ivoire and Gabon. As a result, Sub-Saharan Africa accounted for three-quarters of all commercial reserves discovered in 2014.

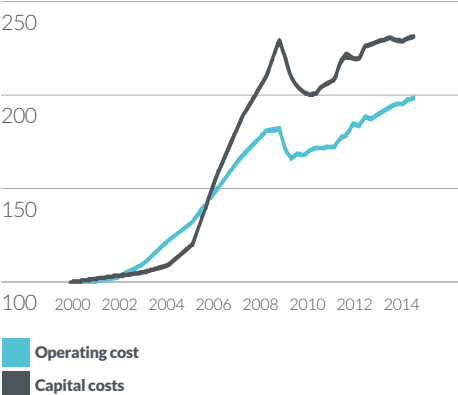
### Return of the megadeal

The sector as a whole is adjusting portfolios to weather the price dip, creating an active but diverse market for corporate and asset deals. The overall M&A market grew 21% from 2013, with \$185 billion of deals announced<sup>6</sup> through 2014 in the upstream sector. This was driven by two trends, the return of the megadeal, for those with available capital<sup>7</sup>, and the return to North America. Deals worth in excess of \$1 billion accounted for 65% of total upstream value and culminated in the announced acquisition of Talisman Energy (Canada) by Repsol (Spain) for \$13bn in what may be the first of a new round of sectorial consolidation driven by a falling oil price<sup>8</sup>.

The North American sector dominated by sheer volume of deals which, whilst generally smaller, accounted for 68% of all deals. Here the US and Canadian actors were retrenching in the buoyant domestic unconventional arena, constructing portfolios of exploration and production assets using the secondary market and, where internationally active, reducing their overseas exposure.

### The price dip

IHS CERA Cost Indices

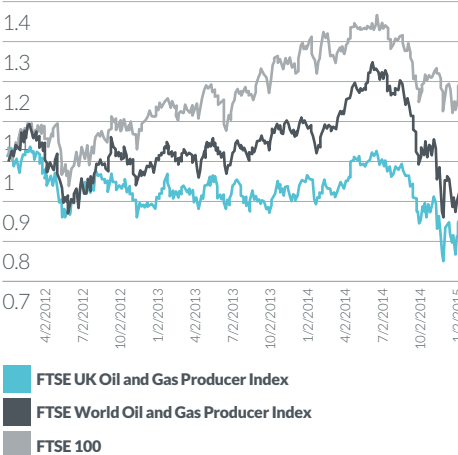


Source: IHS CERA.

Over the last few years the oil and gas sector as a whole underperformed against the stock market, as demonstrated by the graph above. In the short-term, this trend will persist as the current low oil price will benefit oil consumers relative to oil producers, whose output value fell significantly through 2014. Falling crude prices do not spell disaster for all, however: as the significant upward pressure on costs driven by high crude prices recedes, service sector clients with little or no crude production are enjoying lower costs and greater input availability.

The beginnings of this can be observed in the graph above, where the upstream capital cost index is flattening off into the third and fourth quarters of 2014. Upstream operating cost index is likely to follow, but with a lag due to cost frictions and legacy effects. This fall in exploration and appraisal costs is,

Relative Price Performance



once again, an outcome of supply and demand interaction: in the market for deepwater drilling rigs, for example, new supply has arrived at the same time as collapsing demand such that the daily rental rate has halved over 2014 and is expected to remain low through 2015.

There remains considerable uncertainty about how long such a price dip may last, how long it will take for the “cheapest” to remain, but as oil demand strengthens and supply tightens, firms with significant developmental portfolios in 2015 could reap a windfall. They can benefit from reduced costs during the appraisal and development phase, but sell the end product at improved prices as they move into a production standing.

- IMF World Economic Outlook (Update), January 2015.
- IEA Oil Market Report, January 2015.
- Light Tight Oil, oil extracted from impermeable reservoirs, now available for extraction principally due to the developments in the hydraulic fracturing, “fracking”, of reservoirs.
- MEES interview with Ali Naimi, 21 December 2014, [www.mees.com](http://www.mees.com).
- Whilst the meaning, and position, of this frontier is continually changing due to technological and commercial evolution in the sector, this kind of activity is likely to be in remote, and often extreme, geographical locations or in deepwater, or from unconventional sources such as tar sands or shale deposits.
- EY Global Oil and Gas Transactions Review 2014.
- Notably absent after recent years are the National Oil Companies (NOCs), in particular those from China, who have entered a phase of developing their newly-acquired portfolio.
- Consolidation did not occur only in the upstream sector: in the oilfield services sector, the acquisition of Baker Hughes by Halliburton for \$38bn created a new giant from two top-five companies.



Cajun Express drilling rig,  
offshore Senegal.





# Opening a new Atlantic Margin basin – finding oil in Senegal

*In 2014 Cairn and its Joint Venture (JV) partners drilled two wells offshore Senegal discovering oil in both and opening a new basin on the Atlantic Margin. These were the first wells drilled offshore Senegal in 20 years and the first ever deepwater wells.*

Cairn entered the area in March 2013, farming-in to three blocks offshore Senegal held by JV partners FAR Limited and Petrosen (the Senegal national oil company). ConocoPhillips subsequently farmed-in to the blocks three months later.

Cairn, with a 40% interest, operates the licence which covers more than 7,000km<sup>2</sup> and contains a variety of plays, straddling the continental shelf and into the deeper water. Hydrocarbon systems had previously been demonstrated on the Senegal shelf, as in many of the shallow water areas adjacent to Cairn's acreage around the North West Africa Margin. However, these were the first wells drilled in the deeper water off Senegal where Cairn believed there to be extensive source rocks and Cretaceous reservoir systems.

The FAN-1 exploration well, drilled in 1,427m water depth and approximately 100km offshore, encountered high quality light oil in 29 net metres of multiple stacked deepwater fan reservoirs within an extensive oil column, confirming a working hydrocarbon system. Preliminary STOIP estimates range from 250 to 2,500 mmbbls.

SNE-1, the second exploration well to be drilled, was located approximately 24km south east of FAN-1 in 1,100m water depth.

The well, drilled on the palaeo-shelf edge, discovered high quality oil in 36 net metres of high quality shelfal reservoirs of similar age to the oil-bearing sands found in FAN-1. Preliminary P90-P50-P10 contingent resource estimates range from 150 - 330 - 670 mmbbls.

In November 2014 Cairn issued Notices of Discovery for both wells to the Government of Senegal on behalf of the JV. Cairn is currently preparing plans for follow-up activity, which are anticipated to include appraisal drilling starting in 2015, to determine the scale and extent of the discoveries.

Wherever Cairn operates it looks to employ local people and services where possible and where it is safe to do so. Cairn set up an office in the capital, Dakar, and a supply base in its international port and works with local service providers.

Cairn looks to work responsibly with the authorities and other stakeholders to ensure it understands the environment and communities where it operates and to provide assurance that it will operate safely. Prior to commencing operations, a Public Consultation and Disclosure Plan identified stakeholders and guided the way in which they were engaged. An Environment and Social Impact Assessment plan was approved by the regulatory authorities and was successfully implemented. Cairn is pleased to report that all operations to date have been conducted safely, including the drilling of the two wells and the completion of site and environmental surveys.

Cairn looks forward to working closely with the Government of Senegal and its JV partners to realise the full potential from this large acreage position offshore Senegal.



In discussion with  
Simon Thomson, CEO and James Smith, CFO



Operated exploration programme

**James Smith:** 2013/2014 saw us embark upon a focused drilling exploration programme with a series of operated exploration wells. Importantly, these wells were delivered at appropriate equity levels and therefore the right financial exposure for this business.

**Simon Thomson:** This exploration programme was all about play opening wells, in acreage we believe in, and that is exactly what we have achieved in opening a new basin offshore Senegal.

We are delighted with the success to date offshore Senegal. As part of our strategy we have been building and shaping a balanced portfolio with our North Sea development and ultimately production assets on the one side, and exploration on the other side. As you would expect exploration activity in new basins is higher risk and not every well is going to be successful; however, this delivery of exploration success in Senegal is evidence of our strategy working.

Success in Senegal

**Simon Thomson:** Senegal is a great example of Cairn's business model delivering for shareholders. We had a strong technical belief in the potential of the acreage and this belief has been realised with success in both wells drilled to date.

**James Smith:** We have made discoveries in two separate plays, which have the potential to be transformational for Cairn and Senegal. Right now we are focused on working on appraisal and further exploration programmes to fully establish the value in our large acreage position.

**Simon Thomson:** James and I were recently in Senegal and we met with our Joint Venture partners including Petrosen (the national oil company), the Minister of Energy and the President Macky Sall, who is also a geologist. They are incredibly supportive and we all recognise that these discoveries, in the longer term, are potentially transformational for Senegal as a country.

India

**Simon Thomson:** We have a great relationship with India. This is a country where we have spent many years working, where we have discovered, developed and produced oil, delivering significant value both for Cairn shareholders and for India. We are now working closely with the authorities in India to seek a resolution to the tax issue. Our approach has been to focus on continued engagement with the Government of India and to that end we are continuing our programme of targeted, regular meetings with many stakeholders in India. Resolving this issue will continue to be a high priority for us.

**James Smith:** The freezing of our asset in India was an unexpected event and we moved quickly to ensure we remained able to deliver our work programme and longer-term strategy in the absence of those funds. This was principally achieved by accelerating the timetable for bringing in debt financing for our North Sea development activities. We are of course hoping for a resolution in India but the important thing is that the business remains funded through to the point of delivering free cash flow from our North Sea projects.



*“Right now, maximum value for the business and our shareholders is in Senegal, because it has the potential to add substantial value beyond what we have already discovered.”*

## Shaping the organisation

**Simon Thomson:** We pride ourselves on being an established, proficient, safe and fast operator. We have proven ourselves time and time again to be technically, commercially and financially skilled and we are focused on protecting those core competencies.

At the beginning of this year we recognised that we needed to reorganise the business to ensure that Cairn was the right size of company for the work programmes ahead. We were absolutely clear that our priority would be to retain and protect all of those core competencies which means our technical, commercial and financial skills; skills which are the foundation of this business and which have enabled us to achieve success in previous years.

**James Smith:** We have a great technical team, but we also have a great commercial and financial team. It is that combination of high quality competencies and teams which delivers value by marrying technical beliefs with a clear strategy and business model. In addressing the organisational structure we have retained those core technical skills as well as a strong leadership team, whilst delivering a reduction in the central cost base. Following a staff consultation process the reorganisation was completed at the end of 2014, with staff and contractor headcount reduced by approximately 40%.

## Developments

**Simon Thomson:** Our development activities which form the core of a North Sea portfolio of more than 30 licences are a core element of our long-term sustainable business model. They balance our portfolio with exploration on the one side and cash and development activity on the other. From 2017 we anticipate production and free cash flow from these assets with production estimates of around 22,500 barrels of oil equivalent per day net to Cairn.

**James Smith:** The cash flows from this production will be critical to supporting a self funding business model over the medium and long-term. We keep a disciplined focus on projects right across the portfolio which deliver strong returns even in a lower oil price environment and this includes making sure our North Sea development investments are in line with that strategy.

## Outlook

**James Smith:** As we have said before, discipline in the optimal allocation of capital is critical, even more so in the current weaker oil price environment. We will continue to focus on this and on ensuring that we have the right equity exposure across our portfolio. We have demonstrated our abilities as prudent managers of our portfolio throughout the year, including our ability to trade and swap assets particularly within our North Sea portfolio. As a result we start 2015 in a strong position to deliver an exciting programme across the portfolio, especially in Senegal.

**Simon Thomson:** Right now, maximum value for the business and our shareholders is in Senegal, because it has the potential to add substantial value beyond what we have already discovered. So this is where we will be focusing our efforts and we do expect this opportunity to keep us busy for a considerable time to come. However, we have built a diverse, balanced and solid portfolio and we will continue to progress our programmes elsewhere, with particular focus on our core North Sea developments, and to work on our other assets to ensure the entire portfolio remains balanced and in good shape.



Kraken FPSO is under construction in the Keppel boat yard, Singapore.







# North Sea development

*Cairn has built a strong position in the UK and Norway, as part of its North West Europe portfolio, by acquiring exploration, appraisal, development and production assets and participating in licence rounds.*

Cairn has an experienced team dedicated to the UK and Norway with offices in London and Stavanger. More recently Cairn has entered the Barents Sea and is in the process of applying for operatorship in Norway, both of which leverage Cairn's Arctic operational experience and Norwegian presence.

The UK and Norway region represents a critical part of the Group's strategy of having a balanced and sustainable portfolio. The mature basins of the North Sea provide balance to the broader exploration portfolio and will deliver the free cash flow to sustain future exploration. The North Sea is an active market for asset transactions enabling Cairn to continually optimise its portfolio within the region as well as its wider capital allocation.

Kraken and Catcher, two of the largest new projects in the UK North Sea, are the Group's core development projects. They are both under development and will provide free cash flow from 2017 with peak net production to Cairn of ~22,500 boepd. At the peak of production in 2017/2018 it is anticipated that Kraken and Catcher combined could account for around 7% of UK total daily boe production<sup>1</sup>.

1. Based on Oil and Gas UK Activity Survey 2014.

Estimated peak net production  
**~22,500 boepd**

## Catcher

Premier (operator, 50%)  
Cairn 20%, MOL 20%, Dyas 10%

The Catcher field was discovered in 2010 in block 28/9a of the central UK North Sea. Follow-up wells in the block then discovered the Varadero, Burgman, Carnaby and Bonneville fields. There are four adjacent licences to the Catcher licence and, combined, these make up what is known as the Greater Catcher area.

In 2014 a Field Development Plan (FDP) for the development of the Catcher, Varadero and Burgman fields was approved by DECC and 2P reserves were booked. The development will comprise a Floating Production Storage and Offloading (FPSO) facility which is currently under construction in Singapore and will be capable of processing 60,000 bopd.

The development will be located 170km south east of Aberdeen in water depths of ~90m.

Development drilling will start in 2015 with more than 20 wells expected to be drilled over a period of more than four years.

First oil is anticipated in 2017 with net peak production to Cairn of ~10,000 boepd.

## Kraken

EnQuest (operator, 60%)  
Cairn 25%, First Oil 15%

The Kraken field was discovered in 1985 in block 9/2b of the UK North Sea, followed by the Kraken North field in 2013. Combined, these two fields make up the Kraken development. The Joint Venture is continuing to evaluate additional opportunities in the block.

The FDP for the Kraken development was approved by DECC in 2013 and the FPSO vessel, which will be capable of processing 80,000 bopd, is currently under construction in Singapore.

The Kraken field is located ~350km north east of Aberdeen and ~125km east of the Shetland islands in water depths of ~115m.

Development drilling will start in 2015 with 25 wells expected to be drilled over a period of more than four years.

First oil is anticipated in 2017 with net peak production to Cairn of ~12,500 boepd.

## 2014 Key Performance Indicators (KPIs)

Cairn has in place both financial and non-financial Key Performance Indicators (KPIs) which are used to monitor progress in delivering the Group’s strategy.

The 2014 KPIs, which were set out on page 28 of the Annual Report and Accounts 2013, related to delivering a sustainable business, maintaining a balanced portfolio and achieving operational excellence.	The Group’s 2014 KPIs were reflective of the early stage in the value creation cycle, unlike the more traditional KPIs for oil and gas exploration and production companies (such as production or operating cost targets), which the Board currently considers are not relevant as a measure of the Group’s performance.	Good progress has been made across the 2014 KPIs and a brief update on progress is presented in the table below.  The final decision on the overall achievement of the KPIs was made at the Remuneration Committee meeting in December 2014.
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## Maintaining a balanced portfolio

Purpose Grow the reserves and resources base to provide a basis for future growth			KPI Remuneration Committee decision
2014 KPI	Measurement	2014 performance	
Achieve exploration and appraisal success through the discovery of commercial hydrocarbons	<b>Mature Basin:</b> Invest in exploration and appraisal activities in the UK and Norway sectors of the North Sea which will add net 2C resources in excess of 10 mmbbl	The Group successfully discovered potentially commercial hydrocarbons in Senegal through the drilling of the shelf edge well (SNE-1) and the North fan well (FAN1). The SNE-1 well added 120 mmbbls of 2C resources. Further technical evaluation is required to determine the commerciality of the FAN-1 well.	Achieved
	<b>Frontier Basin:</b> Invest in exploration and appraisal activities in Morocco, Senegal and Republic of Ireland which will add net 2C resources in excess of 40 mmbbl	Elsewhere, the Fom Draa and Cap Juby wells in Morocco and the Ensis and Aragon wells in Norway and the UK were unsuccessful at the primary exploration target. It was predetermined that a significant discovery in either of the mature or frontier basins would result in the KPI being achieved.	
Mature high impact exploration prospects ready for drilling in 2015 or 2016	Mature a minimum of six new independent “drill-ready” prospects in each category (mature/frontier basin) which meets the Group’s investment criteria and which could be considered for drilling in 2015 or 2016	Discover more: <i>Operational review</i> P22-27	Partially achieved
		A number of prospects in Senegal, Morocco and Norway were matured to “drill-ready” status for 2015 or 2016. Prospectivity in Mauritania and the Republic of Ireland continues to be assessed. The Group participated in the UK 28th licensing round in 2014, when a “drill-ready” prospect was identified and a firm well commitment bid was made.	
		Discover more: <i>Operational review</i> P22-27	



## Seeking operational excellence

### Purpose

Deliver operational excellence in all 2014 activities and maintain licence to operate

KPI Remuneration  
Committee decision

2014 KPI	Measurement	2014 performance	
<b>Successfully complete operated and non-operated 2014 work programmes</b>	Deliver all operated and non-operated asset projects (technical studies, surveys, seismic and drilling programmes) on schedule and budget (including manpower costs), with full data recovery	Cairn, as Operator, acquired 2D seismic offshore Malta and 3D seismic offshore Republic of Ireland and participated as non-operator in the acquisition of 3D seismic offshore Western Sahara, all of which was successfully completed on time and budget. Two exploration wells were executed on or below budget (Foum Draa offshore Morocco and Ensis in the North Sea). Due to some unscheduled maintenance requirements on the Cajun Express rig, the FAN-1 well offshore Senegal and the Cap Juby well offshore Morocco were over budget and schedule. The Aragon well in the North sea was also over budget.	<b>Partially achieved</b>
		 Discover more: <i>Operational review</i> P22-27	
	Progress North Sea development projects, remaining within 10% of capital guidance and first oil dates scheduled within six months of project sanctioned base case estimates	The Catcher and Kraken development projects are progressing well and remain within 10% of capital guidance. The Catcher project remains on track for first oil in 2017 and the Kraken project remains on track for first oil in 2017 subject to the timely delivery of the FPSO.	<b>Achieved</b>
		 Discover more: <i>Operational review</i> P22-27	
<b>Deliver our activities with a strong focus on not harming people or damaging the environment</b>	Minimise injuries and environmental incidents in 2014 operated activities: <ul style="list-style-type: none"> <li>– Total Recordable Injury Rate (TRIR) target of less than 2.0 TRI/million hours</li> <li>– No oil spills to the environment</li> </ul>	The Total Recordable Injury Rate (TRIR) of 3.88 per million hours remains higher than the target of 2.0 per million hours. This compares well with 5.04 in 2013 and the overall trend of improvement year on year continues. There has been no oil spill to the environment in 2014.	<b>Partially achieved</b>
		 Discover more: <i>Working responsibly</i> P42-57	
<b>Continue to enhance the Group's HSE culture, behaviours and approach</b>	Achieve targets for ten HSE leading performance indicators (LPIs) across the areas of: <ul style="list-style-type: none"> <li>– Knowledge of HSE procedures</li> <li>– Engagement with contractors regarding safety standards</li> <li>– Communication of HSE approach and performance</li> <li>– HSE risk assessment and management</li> </ul>	The 2014 LPIs progressed well. An extensive engagement programme with contractors was completed to raise awareness of the Group's HSE procedures and to deliver key HSE messages through senior management briefings. The HSE risk assessment and management LPI was achieved through enhancements to the travel risk assessment and project risk management processes. A programme to raise awareness and knowledge of the Group's HSE procedures was completed with the delivery of workshops on topics such as corporate responsibility and human rights. HSE communications improved with HSE now a standing agenda item at staff meetings and HSE papers presented at all Board meetings. Some further work is required in embedding and enhancing the HSE cultural framework.	<b>Partially achieved</b>
		 Discover more: <i>Working responsibly</i> P42-57	

## Delivering a sustainable business

### Purpose

Maintain a self funding business plan

KPI Remuneration  
Committee decision

2014 KPI	Measurement	2014 performance	
<b>Retain balance sheet strength</b>	Maintain liquid reserves including undrawn committed banking facilities to meet planned funding commitments plus a cushion at all times	The Group remains funded to deliver its firm exploration and the development programme through to free cash flow from 2017.	<b>Achieved</b>
		 Discover more: <i>Financial review</i> P30-33	

## 2015 Key Performance Indicators (KPIs)

The 2015 Group KPIs in the table below were set by the Board in December 2014 and are based on the Group’s current portfolio, prospects and objectives set out in the 2015 Business Plan.

### Maintaining a balanced portfolio

Purpose		
Grow the reserves and resources base to provide a basis for future growth		
Objective	2015 KPI	Risks to the achievement of KPI
Achieve exploration and appraisal success through discovery or addition of commercial hydrocarbons in 2015	Invest in exploration and appraisal activities which will add net 2C resources in excess of 20 mmbœ	<ul style="list-style-type: none"><li>– Lack of exploration success</li><li>– Reliance on Joint Venture (JV) operators for asset performance</li></ul> <div><div>34</div><div>Discover more: <i>How we manage risk</i> P34-41</div></div>
Mature high impact exploration prospects ready for drilling in 2016 or 2017	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	<ul style="list-style-type: none"><li>– Inability to identify or secure prospective acreage at prices which can generate reasonable returns</li></ul> <div><div>34</div><div>Discover more: <i>How we manage risk</i> P34-41</div></div>
Active portfolio optimisation and acreage protection	Declaration of Commerciality for Sangomar, Sangomar Deep and Rufisque blocks in acceptable timeframe to maximise acreage retention	<ul style="list-style-type: none"><li>– Failure to maximise Senegal acreage position</li></ul> <div><div>34</div><div>Discover more: <i>How we manage risk</i> P34-41</div></div>



On board the Cajun Express drilling rig, offshore Senegal.

## Seeking operational excellence

### Purpose

### Deliver operational excellence in all 2015 activities and maintain licence to operate

Objective	2015 KPI	Risks to the achievement of KPI
Successfully complete operated and non-operated 2015 work programmes	Deliver all operated and non-operated asset projects (technical studies, surveys, seismic and drilling programmes) on schedule and budget (including manpower costs), with full data recovery	<ul style="list-style-type: none"> <li>Operational and project performance</li> <li>Reliance on JV operators for asset performance</li> <li>Staff recruitment and retention</li> </ul>
	Progress North Sea development projects, remaining within 10% of capital guidance and first oil dates scheduled within six months of Final Investment Decision (FID) base case estimates	<ul style="list-style-type: none"> <li>Kraken and Catcher development projects not executed on schedule and budget</li> <li>Reliance on JV operators for asset performance</li> </ul>
	Secure a suitable rig for further exploration and appraisal in Senegal	<ul style="list-style-type: none"> <li>Operational and project performance</li> </ul>
Deliver activities with a focus on the safety of people and the environment	Minimise injuries and environmental incidents in 2015 operated activities: <ul style="list-style-type: none"> <li>TRIR target of less than 2.0 TRIR/million hours</li> <li>No oil spills to the environment</li> </ul>	<ul style="list-style-type: none"> <li>Health, safety, environmental and security incidents</li> </ul>
Continue to enhance the Group's HSE culture, behaviours and approach	Achieve targets for HSE LPs linked to elements of the HSE culture framework	<ul style="list-style-type: none"> <li>Health, safety, environmental and security incidents</li> </ul>

34 Discover more: *How we manage risk*  
P34-41

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P34-41

34 Discover more: *How we manage risk*  
P34-41

## Delivering a sustainable business

### Purpose

### Maintain a self funding business plan

Objective	2015 KPI	Risks to the achievement of KPI
Retain balance sheet strength	Maintain liquid reserves including undrawn committed banking facilities to meet planned funding commitments plus a cushion at all times  Make tangible progress on Cairn India Limited (CIL) shares freeze	<ul style="list-style-type: none"> <li>Restriction on ability to sell CIL shareholding</li> <li>Potential tax liabilities relating to Indian Income Tax Department enquiry</li> <li>Uncertainty in fiscal regimes</li> <li>Operational and project performance</li> <li>Kraken and Catcher development projects not executed on schedule and budget</li> <li>Inability to access internal or external funding</li> </ul>

34 Discover more: *How we manage risk*  
P34-41



# Balanced portfolio of opportunities



*Cairn has built a balanced portfolio of opportunities in a mixture of frontier, emerging and mature basins which offer the opportunity for sustained organic growth and value delivery.*

*Across the portfolio Cairn seeks to acquire significant acreage positions, at appropriate equity levels, in areas we believe have high technical and commercial potential and where, in the case of initial success, we have financial capability to leverage our knowledge and create value. We continually evaluate the entire portfolio to ensure that our equity is at appropriate levels to offer potential growth opportunities.*

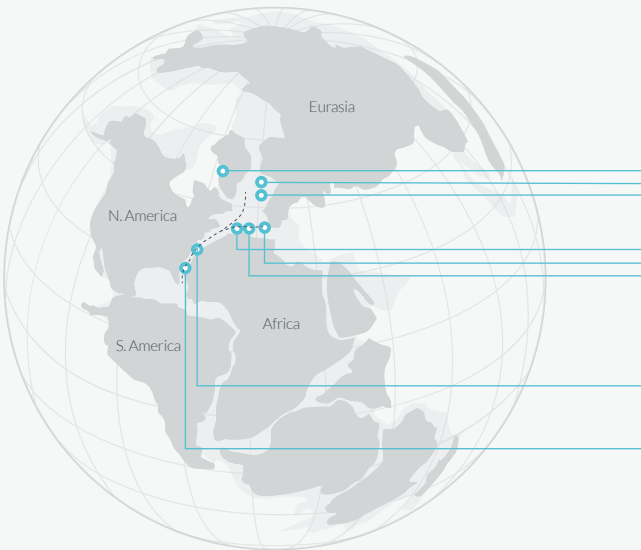
**Richard Heaton**  
Director of Exploration  
9 March 2015

## Where we are focused

The Atlantic Margin, formed together with associated rift basins in the break-up of the Pangaea supercontinent millions of years ago, provides a range of underexplored and mature hydrocarbon basins of Mesozoic and Tertiary age with common geologic themes and promising opportunities for organic growth. Focusing on this area enables the creation of a balanced portfolio, aligning the Company's proven experience in passive margin and rift basin exploration with its operational capability in frontier areas, including Arctic and deepwater capability.

Cairn's mostly operated interests in frontier exploration opportunities lie along the Atlantic Margins offshore North West Africa, Republic of Ireland and Greenland and are balanced by its mainly non-operated exploration and development interests in the more mature and emerging basins in the UK and Norway. Cairn's operated Atlantic Margin exploration drilling programme, which commenced in Morocco in 2013 and continued in Morocco and Senegal throughout 2014, targeted various Mesozoic age passive margin play types at a number of locations.

The success of the programme in the discoveries made by the two wells drilled offshore Senegal has attracted the attention of the industry by opening up a new hydrocarbon basin in the Atlantic Margin. Cairn looks to capitalise on this success in 2015 and 2016 with further exploration and appraisal activity.



**Illustrative geological reconstruction  
of the world ~175 million years ago**

Focused on three regions

Atlantic Margin

Along the underexplored coast of North West Africa, from Senegal to Morocco, Cairn's acreage position has been created in the deeper water areas adjacent to shelf acreage where a number of early wells were drilled during the 1960s and 70s. Many of these wells encountered petroleum in some form, demonstrating the potential for a working hydrocarbon system, but without confirming any commercially viable discoveries. Now, utilising modern 3D seismic data and the drilling capability available through dynamically positioned rigs, Cairn's recent programme and success in Senegal has opened up a new and emerging hydrocarbon basin.

A similar exploration theme encompasses the Company's acreage offshore Republic of Ireland, and Greenland where any future plans will require additional partners.

North West Europe

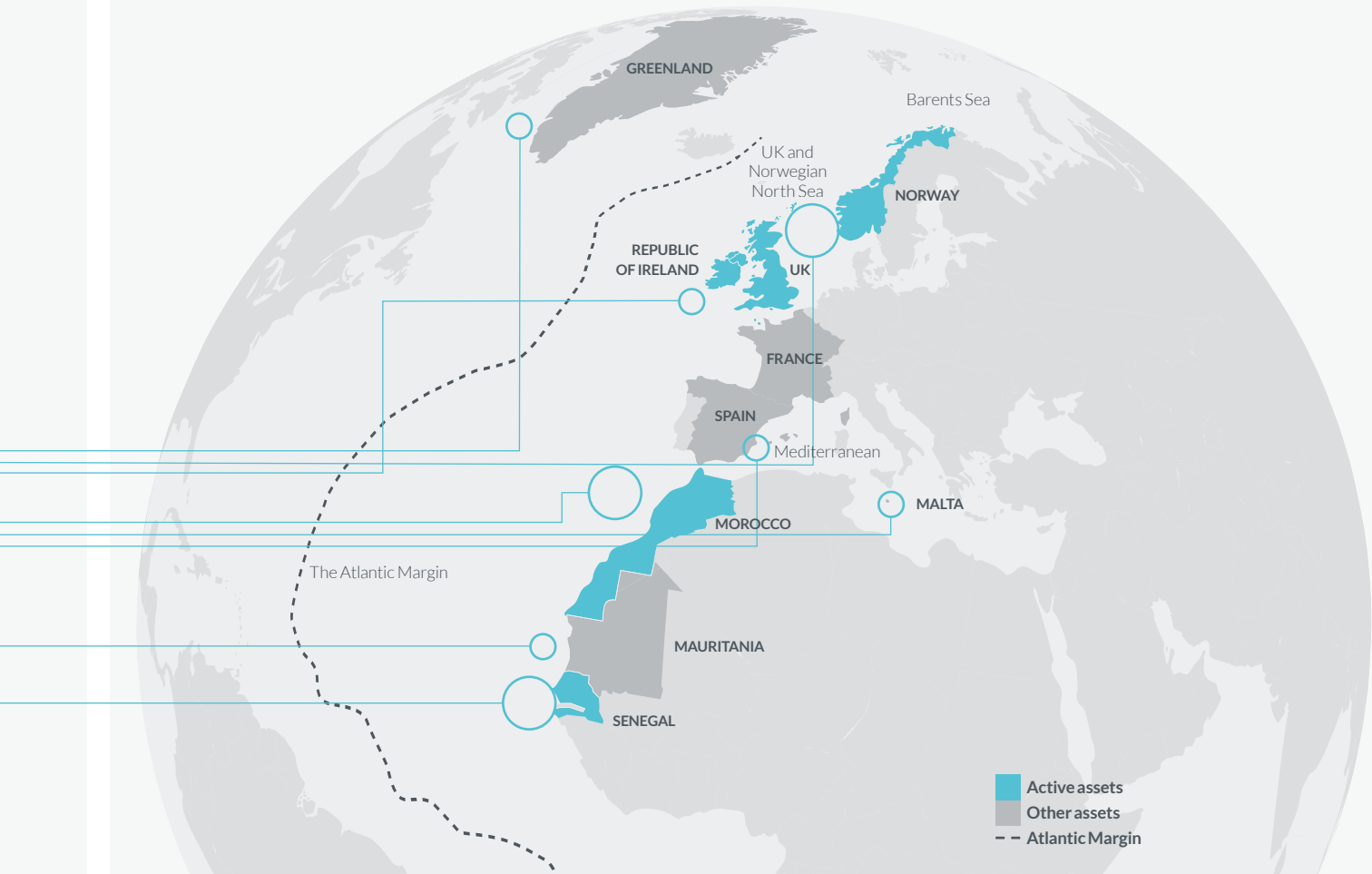
Over the last two years Cairn has built a strong position in the UK and Norway with interests in two major UK North Sea developments, Catcher and Kraken, and a third development, Skarvfjell, in the earlier stage of planning in Norway.

Around these fields Cairn has continued to build an exploration portfolio to leverage its subsurface knowledge and operational synergies to access the maximum commercial value of each area. In parallel, Cairn is applying for operatorship in Norway and has more recently entered the emerging Barents Sea region, where Cairn's Arctic operational expertise can be combined with its geoscience knowledge.

The UK and Norwegian continental shelves offer the potential for a balanced portfolio of opportunities involving a mixture of mature and emerging basins which themselves offer the potential for growth but also benefit from a particularly active and proven market for the efficient trading of assets and associated value creation.

Mediterranean

As part of its longer-term frontier exploration programme, Cairn has also acquired interests in a number of opportunities in the Mediterranean area, most recently completing a seismic survey offshore Malta. The deeper water areas remain underexplored, yet with hydrocarbons demonstrated in a number of plays and modern 3D data starting to unlock new potential, the basin offers a number of opportunities for discovery and attractive fiscal terms.



*“Cairn discovered oil in both wells of its Senegal exploration programme, opening a new hydrocarbon basin on the Atlantic Margin.”*

Overview

### Atlantic Margin

Cairn’s frontier Atlantic Margin exploration strategy is focused along the multiple play types formed from the break-up of the supercontinent Pangaea, with success most recently achieved offshore Senegal.

Countries	
Senegal	1 licence
Morocco	3 licences
Republic of Ireland	3 licences
Greenland	4 licences
Mauritania	1 licence

#### 2014 activity

- 2 operated wells offshore Senegal
- 1 operated well offshore Morocco and 1 non-operated well (completed 2015) offshore Western Sahara
- 3D seismic survey offshore Republic of Ireland

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-- Atlantic Margin

**Senegal**

Cairn discovered oil in both wells of its Senegal exploration programme, opening a new hydrocarbon basin on the Atlantic Margin.

The first exploration well, FAN-1 located in 1,427m water depth and ~100km offshore in the Sangomar Deep block, reached a Target Depth of 4,927m and was targeting multiple stacked deepwater fans. The well encountered a very substantial oil bearing interval that materially upgrades the prospectivity of the block with a proven petroleum system and a number of deep fan and shelf prospects established. Preliminary analysis indicates:

- 29m of net oil-bearing reservoir in Cretaceous sandstones.
- No water contact was encountered in a gross oil bearing interval of more than 500m.
- Distinct oil types ranging from 28° API up to 41° API indicated so far from a number of oil samples recovered to surface.
- Initial gross STOIIIP estimates for FAN-1 range from P90 250 mmbbls, P50 950 mmbbls to P10 2,500 mmbbls and are broadly in line with pre-drill STOIIIP estimates.

The second exploration well, SNE-1, located in 1,100m water depth and ~100km offshore in the Sangomar Offshore block, was targeting the Shelf Edge Prospect. Wire line logging of SNE-1 confirmed hydrocarbons in the Cretaceous clastics objective which is of similar age to oil-bearing sands found approximately 24km away in FAN-1. Initial analysis of the SNE-1 well indicates:

- 95m gross oil bearing column with a gas cap.
- Excellent reservoir sands with net oil pay of 36m.
- Oil of 32° API from samples of gas, oil and water recovered to surface.
- Preliminary estimates of the Contingent Resource range from P90 150 mmbbls, P50 330 mmbbls to P10 670 mmbbls recoverable.

Notices of the two discoveries were submitted to the Senegal Government in November 2014. Following a six month period to plan a future work programme, the JV will submit an evaluation plan in May 2015. Based on early evaluation, the JV currently envisages three firm and three optional wells to begin in 2015.

Cairn has a 40% WI as Operator in three blocks offshore Senegal (Sangomar Deep, Sangomar Offshore and Rufisque); ConocoPhillips has 35% WI, FAR Limited 15% WI and Petrosen, the national oil company of Senegal, 10%. The three blocks cover 7,490km².

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Morocco

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

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

The JM-1 well (Cairn 37.5% WI, Operator) drilled in the Juby Maritime licence to evaluate Upper Jurassic and Middle Jurassic objectives reached a total depth of 3,711m TVDSS and was plugged and abandoned without testing in March 2014. In the Upper Jurassic section, the well confirmed the presence of heavy oil over a gross interval of 110m as originally tested in the 1968 MO-2 well, some 2km from the JM-1 well. Reservoir quality and the oil gravity in the Upper Jurassic across the Cap Juby structure is undergoing further evaluation by JV partners (Office National Des Hydrocarbures et Des Mines “ONHYM” and Genel Energy). Work is also ongoing to correlate the core and log data from JM-1 with other wells on Cap Juby to evaluate the extent of moveable hydrocarbons and to determine whether any further work should be conducted.

The CB-1 well (Cairn 20% WI) commenced drilling in the Cap Boujdour licence offshore Western Sahara in December 2014, targeting the Al Khayr prospect following a 3D seismic survey earlier in the year. It was announced in March 2015 that the CB-1 exploration well encountered hydrocarbons. The well

penetrated 14m of net gas and condensate pay in clastic reservoirs over a gross hydrocarbon bearing interval of approximately 500m. The discovery was non-commercial and the well has been plugged and abandoned. The permit is operated by Kosmos and partnered by ONHYM.

Mauritania

Work continues to mature block C-19 (Cairn 35% WI) offshore Mauritania towards drilling. Interpretation of the proprietary 3D data has been completed, with four drill-ready prospects identified, each with over 400 mmbbls of gross mean prospective resources (Chariot Oil & Gas Operator estimates).

Republic of Ireland

A 900km² 3D seismic survey was completed in Q3 2014 on acreage adjacent to the Spanish Point discovery on Frontier Exploration Licence (FEL) 1/14 (Cairn 38% WI, Operator). A planned appraisal/exploration well on FEL 2/04 offshore West of Republic of Ireland, has been deferred pending discussions with partners and the Government of the Republic of Ireland.

Greenland

Cairn remains encouraged by the opportunity in the Pitu exploration block (Cairn WI 87.5%, Operator), with combined prospects within the 3D area confirming a potential multi-billion barrel of oil equivalent prospective resource. Any future drilling plans would require additional partners in this region.



Rob Jones, Cairn Regional Director – Africa, Mamadou Faye, Petrosen General Manager, Simon Thomson, Cairn CEO and Matt Fox, ConocoPhillips Executive Vice President Exploration and Production (left to right).



Sanco Sword vessel used to acquire 3D seismic data off West coast of Ireland in 2014.

Overview

### Mediterranean

As part of its frontier exploration programme Cairn has interests in the Mediterranean with a seismic survey recently completed offshore Malta.

Countries	
Malta	1 Exploration Study Agreement
Spain	4 licences
France	2 licences

#### 2014 activity

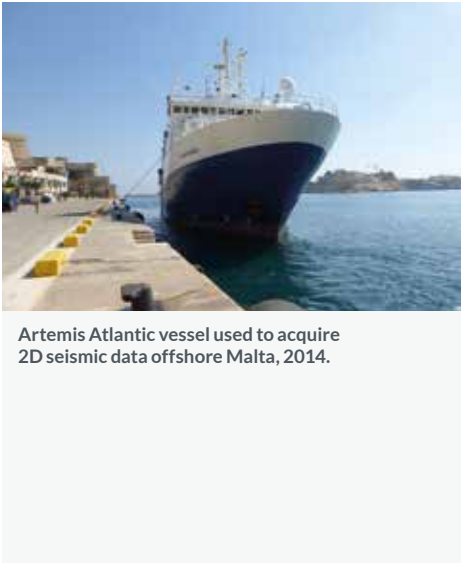
- 2D seismic survey offshore Malta

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**Mediterranean**

As part of our longer term frontier exploration programme, Cairn has acquired interests in a number of opportunities in the Mediterranean area. A 2D seismic survey was completed offshore Malta in April 2014 (Cairn 60% WI, Operator) where the deeper water areas remain underexplored. Hydrocarbons have been demonstrated in a number of plays in the area and with modern seismic data starting to unlock new potential; the basin offers a number of opportunities for discovery. Cairn has also made applications for acreage offshore the Gulf of Lion and the Bay of Biscay in Spain.



Overview

### North West Europe

Over the last two years Cairn has built a strong position in the UK and Norway with interests in two major UK North Sea developments, Catcher and Kraken, and a third development, Skarffjell, in the earlier stage of planning in Norway.

Countries	
UK	20 licences
Norway	14 licences

#### 2014 activity

- 4 non-operated wells in UK and Norwegian North Sea
- Participated in UK 28th Licensing Round and Norwegian 2014 APA Licensing Round
- Entered Barents Sea region
- Applied for Norwegian operatorship

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*“Cairn has built a strong position in the UK and Norway by acquiring exploration, appraisal and development assets and participating in licence rounds.”*

## UK and Norwegian North Sea

Cairn has built a strong position in the UK and Norway by acquiring exploration, appraisal and development assets and participating in licence rounds. The mature basins of the North Sea provide balance to the broader exploration portfolio and will deliver free cash flow to sustain future exploration. The North Sea is an active market for asset transactions enabling Cairn to continually optimise its position within the region as well as its wider capital allocation.

Kraken and Catcher, two of the largest ongoing development projects in the UK North Sea are the Group's core development projects and a third, the Skarvfjell discovery in Norway, is in the early stages of development planning. Kraken and Catcher will provide free cash flow from 2017 with peak net production to Cairn of ~22,500 boepd.

More recently, Cairn entered the emerging Barents Sea and is in the process of applying for operatorship in Norway, leveraging Cairn's Arctic operational experience and Norwegian presence.

## Catcher

The Catcher field (Premier Operator 50%, Cairn 20%, MOL 20%, Dyas 10%) was discovered in 2010 in block 28/9a of the UK Central North Sea. Follow up wells in the block then discovered the Varadero, Burgman, Carnaby and Bonneville fields. These discoveries together with four adjacent licences make up what is known as the Greater Catcher area.

In 2014, a Field Development Plan (FDP) for the development of the Catcher, Varadero and Burgman fields was approved by DECC and 2P reserves were booked. The development will comprise a Floating Production Storage and Offloading (FPSO) facility which is currently under construction in Singapore and will be capable of processing 60,000 boepd.

The development will be located 170km south east of Aberdeen in water depths of ~90m. Development drilling will start in 2015 with more than 20 wells expected to be drilled over a period of more than four years. First oil is anticipated in 2017 with net peak production to Cairn of ~10,000 boepd.

## Kraken

The Kraken field (EnQuest Operator 60%, Cairn 25%, First Oil 15%) was discovered in 1985 in block 9/2b of the UK North Sea, followed by the Kraken North field in 2013. Combined, these two fields make up the Kraken development. The JV is continuing to evaluate additional opportunities in the block.

The FDP for the Kraken development was approved by DECC in 2013 and the FPSO vessel, which will be capable of processing 80,000 boepd, is currently under construction in Singapore. The field is located ~350km north east of Aberdeen and ~125km east of the Shetland Islands in water depths of ~115m. Development drilling will start in 2015 with 25 wells expected to be drilled over more than four years. First oil is anticipated in 2016/17 with net peak production to Cairn of ~12,500 boepd.

## UK & Norway Exploration

In 2014, Cairn continued to build the exploration portfolio in order to leverage our subsurface knowledge and operational synergies and applied for and was awarded interests in both the UK and Norwegian licensing rounds. In Q1 2014, we were awarded interests in all three licences applied for in the Norwegian Awards in Predefined Areas (APA) 2013 Licensing Round and are currently reviewing this acreage, with a view to making drilling decisions in future years. Cairn was also awarded non-operated interests in five licences in the 2014 APA Licensing Round. These licences do not carry firm well commitments and are in locations adjacent to current areas of interest in Norway. In the UK 28th Licensing Round, Cairn was awarded four licences in Q4 2014.

In 2014, the company participated in three non-operated wells:

- Aragon exploration well (Cairn 32.5% WI) licence P1763 in UK North Sea plugged and abandoned in Q4 2014
- Ensis prospect (Cairn 25% WI) PL393B in the Barents Sea plugged and abandoned in Q3 2014
- Atlas prospect (Cairn 20% WI) PL420 in the Skarvfjell area plugged and abandoned in Q4 2014

In 2015, the current programme of non-operated wells in the North Sea is:

- West of Kraken, UK North Sea (EnQuest Operator, Cairn 25% WI) operations are ongoing
- Crossbill, Norwegian North Sea (Wintershall Operator, Cairn 20% WI), operations to commence in Q2



Kraken FPSO under construction.





Cairn's operations  
in Rajasthan,  
North West India.



# Cairn in India

*Working alongside the Government of India and Joint Venture partners, Cairn has been a long-term investor in India for 20 years and its major oil discovery in Rajasthan created the potential to provide more than 30% of India's daily crude production.*

Cairn's successful exploration and development activities have led to long-term job creation in India and the establishment of a legacy asset for the country.

In 2004 Rajasthan represented the largest onshore oil find in India in more than 30 years. Cairn also subsequently discovered and developed interests in Ravva in East India and Cambay Basin in West India. During its involvement in India, Cairn invested approximately US\$5 billion in developing the country's oil and gas resources, making over 40 significant oil and gas discoveries, building 12 offshore platforms, developing four major processing platforms, laying more than 1,000km of pipeline (giving access to 75% of India's refining capacity) and drilling more than 500 wells.

Cairn's investments in India go beyond our exploration and development projects: we have created jobs and worked with local suppliers, added to Rajasthan's GDP growth and invested in communities for local benefit around our operations. For example, the Company, with support from the Government of Rajasthan, set up a partnership with the International Finance Corporation (IFC), the investment arm of the World Bank, to design, fund and implement sustainable socio-economic development programmes in Rajasthan. Key initiatives established included the Enterprise Centre which has now trained more than 6,000 people in areas including construction, handicrafts and English; the Rural Dairy Development Programme which encourages farmers to pool and sell surplus milk; and Health Awareness Initiatives which, through Cairn's Mobile Health Vans, have provided more than 100,000 people with health services.

In 2006, Cairn created Cairn India Limited (CIL) and 100% owned subsidiaries incorporated outside India were transferred to CIL (also a 100% owned company). This reorganisation was submitted to the authorities in India and approved. In 2007, CIL was listed on the Bombay and National Stock Exchanges of India with an independent Board and management team.

Throughout its long history in India, Cairn has been fully compliant and paid all applicable taxes under the legislation in force at the time, including subsequent sales of shares by the Company in CIL.

In January 2014, Cairn received notice from the Income Tax Department of India citing 2012 Retrospective Legislation and requesting information relating to the group reorganisation in 2006. The Income Tax Department provisionally attached the company's remaining 10% shareholding in CIL, then valued at approximately US\$1 billion.

Throughout 2014, Cairn has had a strong focus on resolving the tax issue and has taken measures to protect shareholders' interests.

Financial review

James Smith, Chief Financial Officer

Fully funded to deliver



*Cairn is fully funded to deliver its core development projects through to anticipated sustainable free cash flow generation from 2017.*

**James Smith**  
Chief Financial Officer  
9 March 2015

Overview

The Group secured additional funding of up to US\$575m during the year through a Reserve Based Lending facility. Together with the sale of a 10% interest in Catcher, completed in January 2015, this provides additional financial flexibility for the Group to successfully achieve its strategy of delivering value from discovery and development through disciplined capital allocation across a balanced portfolio.

Exploration assets

During 2014, Cairn successfully completed a four-well frontier exploration programme, focussed on the Atlantic Margin offshore Morocco and Senegal. The first exploration well in the programme, located in the Fom Draa block, completed in January 2014, and the second, in the Juby Maritime block, completed in March 2014. The rig then moved to Senegal where the FAN-1 exploration well and the SNE-1 exploration well completed in September and November 2014 respectively.

Cairn participated in three unsuccessful wells drilled in North West Europe during 2014; two in the North Sea and one in the Barents Sea.

A further appraisal well planned offshore Ireland was deferred as the contracted rig was delayed beyond an acceptable weather window.

Atlantic Margin – Africa

Morocco

During the year, Cairn operated two exploration wells offshore Morocco, both wells were plugged and abandoned after failing to encounter commercial hydrocarbon reservoirs. Unsuccessful exploration costs in 2014 include US\$53m relating to these wells (2013: US\$107m). At 31 December 2014, no material balances remain capitalised in relation to the operations in Morocco (2013: US\$4m).

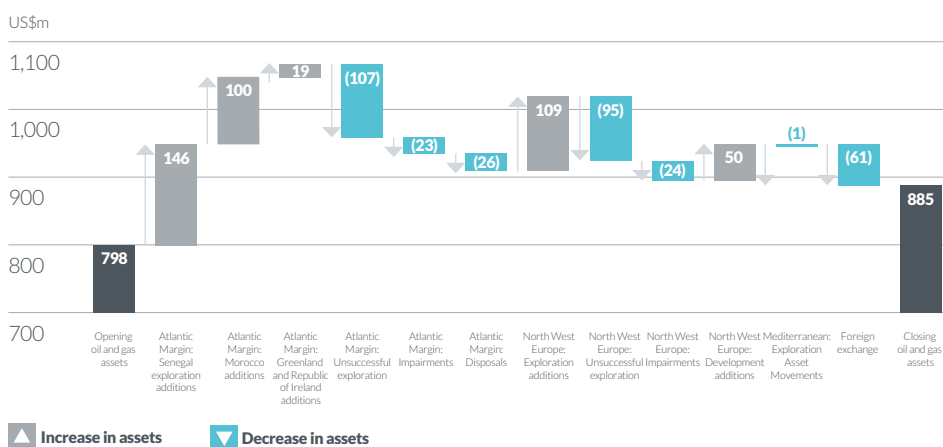
In January 2014, Cairn completed the farm-in to the Cap Boujdour licence in Western Sahara. The CB-1 non-operated exploration well commenced in December 2014, but was confirmed unsuccessful after the balance sheet date.

The total costs incurred on the Cap Boujdour well to 31 December 2014 were US\$47m and are included in unsuccessful exploration costs charged in the year.



“During 2014, Cairn successfully completed a four-well frontier exploration programme, focussed on the Atlantic Margin.”

## 2014 Movements in Oil and Gas assets



### Senegal

Cairn holds a 40% interest in three contiguous blocks offshore Senegal after gaining approval to farm-down 25% to ConocoPhillips early in 2014. Back costs of US\$21m were recovered. Following completion of the Morocco wells, the Cajun Express went on to complete the FAN-1 and SNE-1 exploration wells offshore Senegal. Costs of these two successful wells remain capitalised and are included in the total exploration costs of US\$167m carried in Senegal.

### Atlantic Margin – North Atlantic Greenland

Cairn continues to work to farm-down the Group's interests in Greenland in advance of any further activity and until such a farm-down is concluded, no further exploration activity is planned, an indicator that the asset may be impaired. After testing for impairment in line with Cairn's accounting policy, costs previously capitalised of US\$23m were fully charged to the Income Statement.

### North West Europe

#### UK and Norwegian North Sea

During the year, Cairn drilled two exploration and appraisal wells in the North Sea. Neither the Aragon nor Atlas wells encountered commercial hydrocarbons. Unsuccessful exploration costs of US\$50m were charged to the Income Statement.

The conclusion of Skarvfjell appraisal activities following drilling in 2013 led to an additional charge to the Income Statement. Though the work was technically successful and confirmed the fair value of the asset at the point of acquisition, the appraisal work did not identify any incremental increase in value and therefore was expensed as unsuccessful costs. An additional charge of US\$25m was made to the Income Statement.

Costs remaining capitalised of US\$193m include US\$159m relating to the Skarvfjell discovery and remaining exploration discoveries/prospects in the Catcher area that were not included in the FDP.

### Norwegian Barents Sea

Cairn entered into the Barents Sea region by farming in to the Statoil operated Ensis well, which completed in Q3 2014. The well was unsuccessful and costs of US\$17m were charged to the Income Statement.

## Development assets

### North West Europe

#### UK North Sea

The Catcher area FDP was approved by DECC in June 2014. Costs relating to the fields within the development area of US\$148m were transferred from exploration to development assets.

In September 2014, Cairn entered into a sales agreement with Dyas UK Limited to farm-down a 10% interest in the Catcher development and adjacent acreage, for a carry of US\$182m on future exploration and/or development expenditure and a refund of exploration and development costs incurred from 1 January 2014. Approval for this deal was received subsequent to the year end. Following completion, Cairn retains a 20% working interest.

Costs held in development assets at year end 2014 of US\$468m include the Group's 30% interest in Catcher (including the 10% subsequently sold to Dyas UK Limited) and the Group's 25% interest in the Kraken development. Cairn's 2014 costs relating to Kraken were carried by the operator EnQuest.

## Impairment testing

Given recent declines in oil prices, indicating the possibility of impairment of certain Group assets, Cairn has tested the relevant exploration and development assets for impairment. Goodwill, allocated to the Group's North Sea operating segment, is tested annually for impairment by comparing the net carrying value of the goodwill, the North Sea exploration, appraisal and development assets and the deferred tax assets and liabilities related to those assets to the fair value of the underlying assets in the segment based on recent market transactions or risk-weighted discounted cash flow models.

The Group's base case short-term oil price assumption is based on a three-year forward curve, and thereafter a long-term assumption of US\$90 per barrel is used. With no free cash flow generation anticipated until 2017, the impact of the current low-price environment on the fair value calculations is limited. A comprehensive review of the Group's assumptions has been undertaken and Cairn believes these remain appropriate. Impairment tests resulted in an impairment of North Sea exploration assets of US\$24m and the write-off of remaining costs in Greenland of US\$23m. No impairment arises on the Group's key North Sea development projects or the goodwill associated with the North Sea business.

# Financial review continued

## Available-for-sale financial asset

As at 31 December 2014, Cairn's remaining ~10% holding in Cairn India Limited was valued at US\$703m.

The current restriction on sale of the financial asset does not directly impact its carrying value in the Balance Sheet as the restriction applies only to Cairn and is not a wider market restriction. Dividends declared by CIL of US\$35m during 2014, recognised as finance income in the period are also included within other receivables. A decrease in the CIL share price over the year to a close of INR241 at 31 December 2014, resulted in the recycling of the cumulative deficit on valuation of US\$194m to the Income Statement where it is disclosed as impairment.

## Cash and working capital

Cairn's cash resources at the year end are supported by the US\$575m Reserve Based Lending facility which the Group entered into during 2014. The facility is available to draw down to fund development capex in the Catcher and Kraken projects and in the form of letters of credit or bank guarantees required for Cairn's operational activity. The amount available to fund the projects is determined by standard reserves based lending calculations and by reaching certain project milestones.

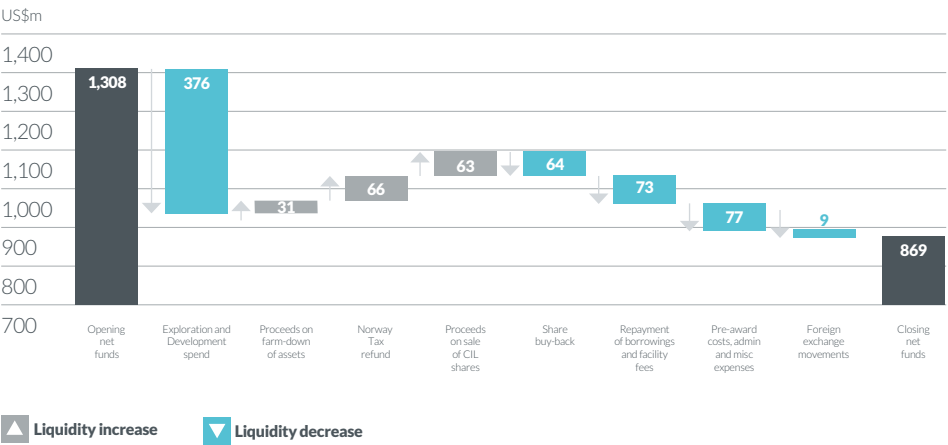
The Group's net funds (cash at bank less bank borrowings) were US\$869m (31 December 2013: US\$1.3bn).

Bank loans in Norway of US\$55m at 31 December 2013 were repaid in full early in 2014 and the facility cancelled.

The US\$575m Reserve-Based Lending Facility was undrawn at the year end. Arrangement and facility fees incurred on entering into the loan agreement are held within prepayments and will be amortised on an effective interest rate basis over the life of the loan, based on drawdown projections. Charges incurred while the facility remains undrawn are charged to the Income Statement.

During the year, Cairn bought back 19m shares for US\$64m.

## 2014 Net funds movements



## Results for the year

With no revenue currently recorded in the Income Statement, the Group reported a loss after tax for the year of US\$381m, analysed as follows:

	2014 US\$m	2013 US\$m
Operational and administrative activities:	Pre-award costs	(55)
	Unsuccessful well costs	(208)
	Administrative expenses and other income/costs	(65)
	Related tax credits	122
		(206)
Finance income	Net finance income	4
Impairments and disposal of investment in CIL:	Impairment	(194)
	Gain on sale	4
	Related net tax credit	41
		(149)
Impairment and loss on sale of oil and gas assets:	Impairment of exploration assets	(47)
	Impairment of goodwill	-
	Gain/(loss) on sale of oil and gas assets	2
	Related tax credits	15
		(30)
Total loss after tax		(381)

*“The Group continues to seek cost-effective entry into new exploration prospects in the Norwegian Barents Sea and the UK and Norwegian North Sea.”*

#### Pre-award costs

The Group continues to seek cost-effective entry into new exploration prospects in the Norwegian Barents Sea and the UK and Norwegian North Sea. Pre-award costs include US\$22m of seismic data acquired in the Barents Sea. Cairn is also active in new UK and Norwegian Licensing Rounds and in the Norwegian 2014 APA Licensing Round, Cairn was awarded non-operated interests in five licences.

#### Operational and administrative expenses

Unsuccessful exploration costs of US\$208m include US\$100m relating to the Morocco Foum Draa, Juby Maritime and Cap Boujdour wells; US\$53m relating to North Sea exploration wells drilled including Aragon and Atlas and US\$17m of costs relating to the Ensis well in the Barents Sea. US\$25m of costs relating to the Skarvfjell appraisal wells drilled in Norway in 2013 were also charged along with US\$13m of other exploration costs.

During 2014, Cairn implemented a Group reorganisation and as a result, US\$6m has been provided for the costs of redundancy and a further charge of US\$2m on associated share-based payments has been recognised. In addition, during 2014, Cairn incurred costs of US\$8m in its efforts to seek resolution of the tax issue in India.

These additional costs contribute to the rise in net administration costs from US\$42m in 2013 to US\$67m for the current year. Controlling administrative cost levels remains a priority for the Group and the measures taken by Cairn should ensure that they remain appropriate for the level and nature of business activity in the medium term.

#### Finance income

Finance income of US\$38m includes US\$35m of dividends declared by CIL which currently remain frozen.

#### Impairment and disposal of available-for-sale financial assets

Prior to the restriction on sale of the Group's investment in CIL in January 2014, the Group sold 0.6% of its holding; recognising a gain on sale of US\$4m. The cumulative deficit in valuation of the investment of US\$194m has been recycled from reserves and is disclosed as impairment.

#### Impairment

Remaining costs of US\$23m associated with the Group's activities in Greenland have been impaired in full as any further activity is subject to a farm-down of Cairn's interests. Impairment tests conducted on North West Europe assets identified an impairment of US\$24m.

#### Principal Risks and Uncertainties

In 2014, Cairn's strategy was to deliver value from discovery and development. There are a number of risks associated with the delivery of the strategy and work programme which the Group actively manage and mitigate.

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

- Lack of exploration success.
- Restriction on ability to sell CIL shareholding.
- Operational and project performance.
- Kraken and Catcher development projects not executed on schedule and budget.



# Cairn has robust risk management processes to manage its business

## Managing business risks

Managing the risks and opportunities is essential to Cairn's long-term success and sustainability. The Group endeavours to pursue investment opportunities which provide the right balance of political, commercial and technical risk and seeks to maintain exposure to these risks at an acceptable level in line with the risk appetite of the organisation.

The Group's risk management framework supports Cairn's approach to business and enhances the chances of safely engaging in successful business opportunities and delivering value to shareholders and other stakeholders.



*“The risks associated with the delivery of the strategy and work programme and the associated mitigation measures and action plans are maintained in a series of risk registers at group, regional, asset, function and project level.”*

## Risk identification and management

Cairn's system for identifying and managing risks is embedded from the top down in its organisational structure, operations and management systems and accords with the risk management guidelines and principles set out in ISO 31000, the International Standard for Risk Management. The Group's risk management structure is set out in the structure to the left.

The Board has overall responsibility for ensuring the Group's risk management and internal control frameworks are appropriate and applied across the organisation. Principal risks are reviewed at each Board meeting and, at least once a year, the Board undertakes a risk workshop to perform a “deep-dive” review of these risks.

The Audit Committee, which is chaired by Iain McLaren, monitors and reviews the scope and effectiveness of the Company's internal control policies and procedures for the identification, assessment and reporting of risks to the Board. The Audit Committee also monitors the output from each Risk Management Committee (RMC) meeting.

The RMC is chaired by the Chief Financial Officer, James Smith, and also includes the Chief Executive, Chief Operating Officer, Exploration Director, Regional Directors and other senior managers. The RMC is responsible for setting the strategic direction for risk management in the Group and aims to facilitate continual improvement of the risk management system. The RMC also considers the principal risks to the business.

The risks associated with the delivery of the strategy and work programme and the associated mitigation measures and action plans are maintained in a series of risk registers at group, regional, asset, function and project level. Assessment of the potential risks plays a fundamental role in the evaluation of each new investment opportunity and the ongoing management of all projects. The risks and mitigating actions from all of these sources are consolidated into the Group risk matrix and presented at the different meetings and committees outlined in the structure to the left.

## Risk appetite

The Group Risk Appetite Statement ensures there is a common understanding between the Board and senior management as to the quantum and type of risk the organisation is willing to seek and tolerate in the pursuit of its strategy and value creation. Cairn's risk appetite, in line with the strategy and business plan, is to operate across the whole value chain of the upstream exploration and production business, allocating capital and resources proportionally to opportunities which are assessed for the likelihood and impact of their risk and reward. Risk appetite and supplementary risk tolerance levels are reviewed annually by the Board and these levels determine the principal parameters for the assessment of risks and opportunities. In 2014, the Board reviewed the tolerance levels across a number of areas, including capital invested, economic thresholds, solvency, health and safety, environmental, political, reputational, and technical. The Board will continue to review key risks to ensure they remain within the boundaries defined by the Group Risk Appetite Statement.

## Responding to the changing risk environment in 2014

As part of steps to seek continual improvement of the risk management process, the following enhancements were made in 2014:

- the Board completed a risk workshop with the objective of identifying key strategic risks to the Group. Risks identified were analysed against the Group Risk Register to ensure there was alignment between the Board's view of risk and the Group identified risks. The workshop was facilitated by Ernst and Young (EY);
- the Group Risk Appetite Statement was reviewed and approved by the Board. Key changes to the statement included the introduction of specific and measurable risk tolerance levels across a number of categories of risk which set out the parameters for acceptable risk taking. These parameters will be applied by senior management in key decision making;
- the Management Team formally conducted a review of the risks, mitigations and actions identified on the Group Risk Register each quarter to ensure ownership for the risks, mitigations and actions is clearly assigned and implementation dates for actions are tracked; and
- risk reporting to the Board was revised to a “dashboard” format to focus attention on key risks, as measured by their probability, materiality, controllability, new or changing nature and position relative to the Group Risk Appetite Statement.

# Principal risks and uncertainties

As the Group continues to focus on creating value and shareholder returns from disciplined capital allocation across a balance of exploration and development assets, the principal risks and uncertainties facing the Group at the end of 2014 were as follows:

## Lack of exploration success

Exploration success is fundamental to the strategy of creating value through the discovery and development of hydrocarbon resources. Consequently, a sustained lack of exploration success may lead to limited or no value creation and a loss of investor confidence in the Group's business model. In 2014, both the Senegal operated wells discovered oil, mitigating this risk to a degree. The Group continues to actively evaluate a number of potential new exploration investment opportunities for 2015 and beyond, which are all subject to extensive external and internal peer review.

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P22-27

## Restriction on ability to sell Cairn India Limited (CIL) shareholding

In January 2014, Cairn received a request from the Indian Income Tax Department to provide information regarding a group reorganisation that took place during the fiscal year ended 31 March 2007 and as a result a restriction was applied to the sale of the Group's CIL shares. The restriction remains in place and the Group continues to cooperate with the Indian Income Tax Department investigation. The continued freeze of the Group's CIL shares could restrict the Group's funding capacity. The Group will take whatever steps are necessary to protect its interests.

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## Operational and project performance

Delivering all operated and non-operated projects in a safe and efficient manner is a key objective for the Group. In 2014, the Morocco and Senegal drilling campaigns experienced delays as a result of unscheduled maintenance requirements on the Cajun Express rig. With safety being the principal concern, the Group ceased drilling until acceptable mitigation plans were implemented. Anticipated in 2015, offshore wells in Senegal, Western Sahara, the UK and Norway will be drilled and the Group will be working with the rig contractors to agree on a safe and efficient execution plan. In addition, the Group will work closely with JV partners to ensure the Kraken and Catcher development projects are delivered safely and efficiently.

22 Discover more: [Operational review](#)  
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## Kraken and Catcher development projects not executed on schedule and budget

The Kraken and Catcher development projects will provide future cash flow to sustain the Group's business plan and are part of the North West Europe portfolio which provides balance to the Group's exploration and appraisal activities in earlier stage hydrocarbon basins. Development projects of this nature can be susceptible to delays and budget increases for a variety of reasons and this may lead to increased costs and delays in future cash flow. To mitigate these risks, the Group works closely with its JV partners to support and/or influence key decisions. The Catcher and Kraken developments in the North Sea are progressing, with first oil targeted for 2017.

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# Principal risks to the Group in 2014/2015

During 2014, we regularly reviewed the risks which we believed could adversely impact our business at the time. The following table provides an overview of the principal risks to the Group at the end of 2014, the potential impacts, the mitigation measures we have in place and the KPIs the risks impact on. The list is not exhaustive or set out in any order of priority and is continually subject to change.



## Strategic risks

Risk description	Impact	Mitigation	2014 movement	2015 KPI objective
<b>Lack of exploration success</b>	<ul style="list-style-type: none"> <li>Loss of investor confidence</li> <li>Limited or no value creation</li> <li>Failure of the balanced portfolio business model</li> </ul>	<ul style="list-style-type: none"> <li>Active programme for high-grading new areas through licence rounds, farm-ins and other transactions</li> <li>Inventory of prospects and leads that offer opportunities with a balance of geological and technical risks</li> <li>Highly competent team applying a thorough review process of prospects and development opportunities and a team of geoscientists with a track record of delivering exploration success</li> <li>Continue to seek out the right personnel who can add value, knowledge and experience to the Group</li> </ul>	<p>This risk decreased in 2014. Key developments included:</p> <ul style="list-style-type: none"> <li>Both Senegal operated wells discovered oil. Work is underway with JV partners to determine follow-up activity which is targeted for Q4 2015</li> <li>One operated well in Morocco and four non-operated wells in North West Europe were drilled, none of which discovered oil</li> </ul>	<ul style="list-style-type: none"> <li>Invest in exploration and appraisal activities which will add net 2C resources in excess of 20 mmboe</li> </ul>
<b>Kraken and Catcher development projects not executed on schedule and budget</b>	<ul style="list-style-type: none"> <li>Increased costs</li> <li>Delay in future cash flow</li> <li>Reduction in debt capacity</li> </ul>	<ul style="list-style-type: none"> <li>Actively engage with all our JV partners early to ensure highly effective working relationships</li> <li>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</li> <li>Work closely with the Kraken and Catcher operators to monitor and review progress with key contracts</li> </ul>	<p>This risk remained at the same level in 2014. Key developments included:</p> <ul style="list-style-type: none"> <li>All major contracts for both projects have been awarded which support the target schedule to first oil in 2017</li> <li>The Group continues to work closely with all JV partners to challenge, apply influence and/or support key decisions</li> </ul>	<ul style="list-style-type: none"> <li>Progress North Sea development projects, remaining within 10% of capital guidance and first oil dates scheduled within six months of Final Investment Decision (FID) base case estimates</li> </ul>
<b>Failure to maximise Senegal acreage position</b>	<ul style="list-style-type: none"> <li>Sub-optimal acreage retention</li> <li>Investment commitments not fully optimised</li> </ul>	<ul style="list-style-type: none"> <li>Actively engage with the Senegalese Government and JV partners to agree the way forward</li> <li>Production Sharing Contract terms allow for a one-year extension to the exploration licence</li> </ul>	<p>This risk has been added in 2014. Key developments included:</p> <ul style="list-style-type: none"> <li>The current Senegal licence requires a Declaration of Commerciality by February 2016 and Cairn has the right to extend for a further year which has been invoked</li> <li>There is a risk that the relatively short timelines for moving to the exploitation permit will restrict the technical review of the acreage and opportunities may not be fully optimised</li> </ul>	<ul style="list-style-type: none"> <li>Declaration of Commerciality for Sangomar, Sangomar Deep and Rufisque blocks in acceptable timeframe to maximise acreage retention</li> </ul>
<b>Inability to identify or secure prospective acreage at a cost which can generate reasonable returns</b>	<ul style="list-style-type: none"> <li>Loss of investor confidence</li> <li>Loss of competitive edge</li> </ul>	<ul style="list-style-type: none"> <li>Exploration Director, with the support of the technical and commercial teams, continues to identify and review a number of prospects</li> <li>Experience and knowledge throughout the organisation in recognising prospective opportunities</li> </ul>	<p>This risk remained at the same level in 2014. Key developments included:</p> <ul style="list-style-type: none"> <li>Cairn successfully farmed-in to opportunities in the North Sea and the Barents Sea</li> <li>A 2D seismic programme offshore Malta was completed and the data is currently being analysed</li> <li>The Group participated in the 2014 Award in Predefined Areas (APA) licensing round in Norway with five licence awards made to Cairn</li> <li>The Group undertook an extensive opportunity screening review which evaluated the technical and commercial prospects of the many opportunities within the Group's existing portfolio. A number of "drill-ready" prospects were identified</li> </ul>	<ul style="list-style-type: none"> <li>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</li> </ul>

Strategic risks (continued)

Risk description	Impact	Mitigation	2014 movement	2015 KPI objective
<b>Sustained low oil price</b>	<ul style="list-style-type: none"><li>– Reduction in future cash flow</li><li>– Value impairment of development projects</li><li>– JV partner capital constraints</li></ul>	<ul style="list-style-type: none"><li>– Sensitivity reports completed to assess robustness of projects and development decisions</li></ul>	<p>This risk has been added in 2014. Key developments included:</p> <ul style="list-style-type: none"><li>– Without current production, lower oil prices do not directly impact on the Group's operating cash-flow. Indirectly, the lower oil price environment may reduce the amount of debt available under the Group's reserve based lending facility. In addition, the Group's JV partners may experience capital constraints leading to a reallocation of capital and a reprioritisation of projects in which the Group has an equity interest</li><li>– A sustained low oil price will continue to drive down industry costs so there is an opportunity for achieving cost efficiencies in the Group's exploration and appraisal projects</li></ul>	<ul style="list-style-type: none"><li>– Maintain liquid reserves including undrawn committed banking facilities to meet planned funding commitments plus a cushion at all times</li></ul>

Health, safety, environment and security risks

Risk description	Impact	Mitigation	2014 movement	2015 KPI objective
<b>Health, safety, environmental and security incidents</b>	<ul style="list-style-type: none"><li>– Serious injury or death</li><li>– Environmental impacts</li><li>– Reputational damage</li><li>– Regulatory penalties and clean-up costs</li></ul>	<ul style="list-style-type: none"><li>– Effectively managing health, safety, security and environmental risk exposure is the first priority for the Board, SLT and MT</li><li>– Corporate Responsibility Management System (CRMS) processes and procedures are embedded throughout the organisation and all potential health, safety, security, environmental and societal impacts are proactively identified, evaluated and treated during project screening processes</li><li>– Process in place for assessing an operator's overall operating and HSE capabilities, including undertaking JV audits to determine the level of oversight required</li><li>– Emergency organisation procedures and equipment are maintained and regularly tested to ensure the Group is able to respond to an emergency quickly, safely and effectively</li><li>– Ebola virus monitoring and management briefing is issued to all staff travelling to impacted countries</li></ul>	<p>This risk remained at the same level in 2014. Key developments include:</p> <ul style="list-style-type: none"><li>– The Group's safety performance improved overall in 2014 despite a Lost Time Injury (LTI) in July</li><li>– Total Recordable Injury Rate (TRIR) of 3.88 per million hours higher than target of 2.0 per million hours. The rate in 2013 was 5.04 per million hours</li><li>– Managing health risks was a key consideration given the heightened health risks in West Africa. A malaria management and awareness programme was implemented in Senegal as well as a programme to manage and monitor the Ebola situation</li></ul>	<ul style="list-style-type: none"><li>– Minimise injuries and environmental incidents in 2015 operated activities</li><li>– Achieve targets for seven HSE leading performance indicators</li></ul>

Operational risks

Risk description	Impact	Mitigation	2014 movement	2015 KPI objective
Operational and project performance	<ul style="list-style-type: none"> <li>Increased well costs</li> <li>Incomplete well programme</li> <li>HSE incident</li> <li>Reputational damage</li> </ul>	<ul style="list-style-type: none"> <li>Comprehensive set of criteria that must be met before contracting and accepting any rig</li> <li>Work very closely with the rig contractors to exert influence and impose our performance expectations</li> <li>Management and influence of drilling contractors to ensure Cairn management systems are fully embedded in operations</li> <li>Positive and regular engagement with JV operators and partners to share knowledge and offer support</li> </ul>	<p>This risk increased in 2014. Key developments include:</p> <ul style="list-style-type: none"> <li>The Cajun Express rig experienced unscheduled maintenance requirements which led to considerable non-productive time over the course of the drilling contract</li> <li>The Group worked very closely with the drilling contractor to establish and implement mitigations, with safety being at the forefront of all considerations, before operations recommenced</li> <li>Cost pressures in the industry have lessened so there is an opportunity for project cost efficiencies going forward</li> </ul>	<ul style="list-style-type: none"> <li>Progress North Sea development projects, remaining within 10% of capital guidance and first oil dates scheduled within six months of FID base case estimates</li> <li>Deliver all operated and non-operated asset projects (technical studies, surveys, seismic and drilling programmes) on schedule and budget (including manpower costs), with full data recovery</li> <li>Secure a suitable rig for further exploration and appraisal in Senegal</li> </ul>
Reliance on JV operators for asset performance	<ul style="list-style-type: none"> <li>Cost/schedule overruns</li> <li>Poor performance of assets</li> <li>HSE performance</li> <li>Delay in first oil from development projects</li> <li>Impact on asset value</li> </ul>	<ul style="list-style-type: none"> <li>Actively engage with all JV partners early to establish good, trusting, working relationships</li> <li>Actively participate in technical meetings to challenge, apply influence and/or support partners to establish a cohesive JV view</li> <li>Application of the Group risk management processes</li> </ul>	<p>This risk remains at the same level as last year. Key developments include:</p> <ul style="list-style-type: none"> <li>The low oil price is impacting on a number of companies throughout the industry and there is the potential for some of the Group's JV partners to reprioritise projects. At the current time, this has not impacted the Group</li> <li>The Group continues to work closely with a number of JV operators in North West Europe and the Atlantic Margin</li> </ul>	<ul style="list-style-type: none"> <li>Progress North Sea development projects, remaining within 10% of capital guidance and first oil dates scheduled within six months of FID base case estimates</li> <li>Deliver all operated and non-operated asset projects (technical studies, surveys, seismic and drilling programmes) on schedule and budget (including manpower costs), with full data recovery</li> </ul>





Financial risks

Risk description	Impact	Mitigation	2014 movement	2015 KPI objective
<b>Restriction on ability to sell CIL shareholding</b>	<ul style="list-style-type: none"><li>- Restriction in the funding capacity of the Group</li></ul>	<ul style="list-style-type: none"><li>- Business plan is fully funded in the absence of CIL stake</li><li>- Continued engagement with the Indian Government</li><li>- Robust legal protection if required</li></ul>	<p>This risk remains at the same level as last year. Key developments include:</p> <ul style="list-style-type: none"><li>- The freeze on the CIL shareholding remains in place</li><li>- The Group continues to cooperate with the Income Tax Department investigation</li><li>- Engagement with Indian Government continues but the tax issue discussions remain unresolved</li><li>- The Group has the option to take legal action to recover the value of the CIL shareholding but this has not been initiated</li></ul>	<ul style="list-style-type: none"><li>- Make tangible progress on CIL shares freeze</li></ul>
<b>Potential tax liabilities relating to Indian Income Tax Department enquiry</b>	<ul style="list-style-type: none"><li>- Restriction in the funding capacity of the Group</li></ul>	<ul style="list-style-type: none"><li>- Business plan is fully funded in the absence of CIL stake</li><li>- Continued engagement with the Indian Government</li><li>- Robust legal protection if required</li></ul>	<p>This risk remains at the same level as last year. Key developments include:</p> <ul style="list-style-type: none"><li>- The freeze on the CIL shareholding remains in place</li><li>- The Group continues to cooperate with the Income Tax Department investigation</li><li>- Engagement with Indian Government continues but the tax issue discussions remain unresolved</li><li>- The Group has the option to take legal action to recover the value of the CIL shareholding but this has not been initiated</li></ul>	<ul style="list-style-type: none"><li>- Make tangible progress on CIL shares freeze</li></ul>
<b>Uncertainty in fiscal regimes</b>	<ul style="list-style-type: none"><li>- Loss of value</li><li>- Uncertain financial outcomes</li></ul>	<ul style="list-style-type: none"><li>- Engage closely with regulators in all jurisdictions where the Group has activities</li><li>- Legal agreements in place to protect interests</li><li>- Seek appropriate legal and tax advice</li></ul>	<p>This risk remains at the same level as last year. Key developments include:</p> <ul style="list-style-type: none"><li>- The Group has assets in a number of different geographies and is potentially exposed to sudden or unplanned changes in tariffs or taxes</li></ul>	<ul style="list-style-type: none"><li>- Maintain liquid reserves including undrawn committed banking facilities to meet planned funding commitments plus a cushion at all times</li></ul>
<b>Inability to access internal or external funding</b>	<ul style="list-style-type: none"><li>- Work programme restricted by reduced capital availability</li></ul>	<ul style="list-style-type: none"><li>- Up to US\$575m Reserve Based Lending bank facility agreement concluded in July 2014</li><li>- Catcher 10% farm-out to Dyas agreed which will reduce capital expenditure by ~US\$380m</li></ul>	<p>This risk has been added in 2014. Key developments include:</p> <ul style="list-style-type: none"><li>- The restriction on Cairn's ability to sell its shareholding in CIL reduced the Group's access to capital</li><li>- Debt facilities were secured to ensure committed work programme was fully funded</li><li>- Cairn farmed-out part of its interest in Catcher and amended longer-term budget plans to ensure the Group was fully funded through to generating free cash flow</li><li>- The fall in the oil price has reduced the market for external funding</li></ul>	<ul style="list-style-type: none"><li>- Maintain liquid reserves including undrawn committed banking facilities to meet planned funding commitments plus a cushion at all times</li></ul>

## Reputational risks

Risk description	Impact	Mitigation	2014 movement	2015 KPI objective
<b>Negative stakeholder reaction to our operations</b>	<ul style="list-style-type: none"> <li>Reputational damage</li> <li>Loss of investor confidence</li> <li>Loss of licence to operate</li> </ul>	<ul style="list-style-type: none"> <li>Comprehensive stakeholder management and communication plans have been developed and executed for all operations</li> <li>Actively monitor steps being taken by regulators and industry through participation in industry bodies such as the International Association of Oil &amp; Gas Producers and Oil &amp; Gas UK</li> </ul>	<p>This risk remains at the same level as last year. Key developments include:</p> <ul style="list-style-type: none"> <li>The Group has assets in a number of different geographies, which has increased the number of stakeholders and, therefore the potential for stakeholder opposition</li> </ul>	<ul style="list-style-type: none"> <li>Minimise injuries and environmental incidents in 2015 operated activities</li> </ul>

## Organisational risks

Risk description	Impact	Mitigation	2014 movement	2015 KPI objective
<b>Staff recruitment and retention</b>	<ul style="list-style-type: none"> <li>Inadequate resource to deliver work programme</li> <li>Loss of key knowledge and experience</li> </ul>	<ul style="list-style-type: none"> <li>The organisational restructure consultation process identified the skills required to deliver the work programme and the Group worked to ensure key people were retained</li> <li>Regional Directors and Departmental Heads agree resource requirements as part of the annual work programme and budget processes</li> <li>As an accredited Investor in People, we support continuous professional development through technical, professional, management and behavioural skills courses as well as mentoring and educational assistance schemes</li> <li>Succession planning is in place for all areas of the business</li> </ul>	<p>This risk was heightened in 2014 as a result of the voluntary redundancy process but has lessened due to current resource availability in the market. Key developments include:</p> <ul style="list-style-type: none"> <li>The Group underwent a reorganisation to ensure the organisation remained appropriate to the future activity levels and work programme</li> <li>Group reorganisation was implemented, following a staff consultation process, to retain core technical skills with a strong leadership team. Total staff and contractor headcount reduced by ~40%</li> <li>The low oil price has led to a number of employee cuts across the industry and therefore, the market for experienced workers is strong</li> <li>The Group is confident that the right people with the right skills have been retained through the process in order to be adequately resourced to successfully deliver the work programme going forward</li> </ul>	<ul style="list-style-type: none"> <li>No specific KPI objective</li> </ul>

# At the heart of our business



Dakar port,  
Senegal.

*Corporate Responsibility remains at the heart of our business to deliver and protect value for all our stakeholders.*

**Simon Thomson**  
Chief Executive  
9 March 2015

Cairn looks to deliver value through discovery and development of hydrocarbons and our challenge is to do so in a safe, secure and environmentally and socially responsible manner.

Corporate Responsibility (CR) is at the heart of our business and is based on our core values of building respect, nurturing relationships and acting responsibly. These are central to delivering our business objectives. We use our CR Management System (CRMS) to help us achieve these objectives and demonstrate transparency to our stakeholders.

We have Business Principles and CR Policies in place which are regularly updated, most recently in September 2014 to reflect changes in our business including our increased focus on risk management and the importance of the role of contractors and our non-operating partners within our business. Our Business Principles and CR policies are available on our website at [www.cairnenergy.com/responsibility](http://www.cairnenergy.com/responsibility).



*“Corporate Responsibility (CR) is at the heart of our business and is based on our core values of building respect, nurturing relationships and acting responsibly.”*

2014

2014 has been a busy year operationally for Cairn with wells completed in Morocco and Senegal and seismic data acquired in Malta and the Republic of Ireland, in addition to our significant non-operated activities.

Engaging with our contractors, who play an important role in the delivery of our business, has been and remains of great importance to us, especially with such a diverse workforce. In our operated activities we rely heavily on our contractors’ performance which we influence directly through day-to-day contact and specific CR engagement programmes. Where we are a non-operating partner, we influence performance through our relationship with the operating company which includes routine meetings and engaging on specific topics where necessary.

I am pleased to report that our safety performance has improved overall in 2014. However it is disappointing to report a Lost Time Incident (LTI) in July when a member of the rig crew on the Cajun Express was injured following a fall whilst carrying out planned preventative maintenance on the drilling top drive system. A thorough accident investigation was completed and corrective measures were taken to avoid recurrence. We continue to strive to eliminate such incidents.

With significant activity during the year in West Africa managing health risks has been important and we successfully implemented a malaria management and awareness programme whilst monitoring and implementing management procedures associated with the developing Ebola situation.

Our significant non-operated portfolio has continued to develop during the year and we play an active role in monitoring and engaging with our partners on associated CR requirements. Our Catcher and Kraken developments in the UK North Sea continue to progress. Kosmos voluntarily conducted the first Social Impact Assessment in the region prior to commencing drilling of the first well in the Cap Boujdour block.

Plans for 2015

In 2015, as operator, we are delighted to be developing an appraisal and exploration programme offshore Senegal, as well as continued participation in non-operated wells in the UK and Norwegian sectors. We are also taking steps to become an approved operator in Norway. The completion of the Cap Boujdour well in early 2015 will also be evaluated to identify the next steps.

We will ensure our CRMS remains fit for purpose in 2015, especially in light of the Group reorganisation completed in 2014. We will continue to set CR objectives each year guided by the most important material issues which take into account our stakeholders’ concerns.

During 2015, we will continue to prioritise the health, safety, security and wellbeing of people while continuing to promote safe behaviours of our contractors. We remain committed to protecting the environment in the areas in which we operate. Good governance will also continue with our commitment to meeting all of our tax obligations in a transparent manner.

We continue to uphold and support the ten principles of the United Nations Global Compact and we remain a Participating Company of the Extractive Industries Transparency Initiative (EITI).

In this way CR remains at the heart of our business to deliver and protect value for all our stakeholders.

The 3Rs

Our Business Principles are based on the core values of the 3Rs

Respect

We act with **respect** for people, their communities, the environment, human rights and the law.

Relationships

We act honestly, transparently and with integrity to develop strong, lasting **relationships** with all our stakeholders.

Responsibility

We behave fairly, ethically and are accountable for our actions. We believe in, and act on, our **responsibility** to care for people, society and the environment.



On board the Cajun Express drilling rig, offshore Senegal.

# Protecting people, the environment and communities

Cairn looks to create, add and realise value for stakeholders, but not at the expense of the safety and well-being of people and the environment.

We manage the risks associated with our business responsibly for all our activities and wherever we operate. This means we aim to behave professionally in our dealings with people and in the environment from the very start of any project or activity.

The oil and gas business is, by nature, long-term and our approach covers every stage of the oil and gas life-cycle and is outlined below.

<div>1.</div> <div>Due Diligence</div> <div>Before making an acquisition or investment, applying for an exploration licence or farming-in to an existing project, Cairn undertakes an extensive screening process which includes assessing whether there are potential health and safety, social, human rights, political, corruption, security or environmental risks and opportunities. The findings from these assessments are used in decision making on whether or not to proceed, and if investment goes ahead, it informs approaches to risk management going forward.</div>	<div>2.</div> <div>Prequalification</div> <div>When we apply for an exploration licence, the necessary documents are submitted to the relevant authorities. Typically this includes information about our legal status, financial capability, technical competence and plans to manage health, safety and environmental risks and contributions to local economic development.</div>	<div>3.</div> <div>Exploration Seismic</div> <div>Once Cairn has been awarded the right to explore in a certain area, we may carry out seismic surveys to develop a picture of geological structures below the surface. This helps identify the likelihood of an area containing hydrocarbons and helps optimise where to drill. Seismic surveys are preceded by an assessment of environmental, social or human rights impacts which are managed through our Project Delivery Process (PDP).</div>	<div>4.</div> <div>Site Survey</div> <div>Before we commence any drilling activity, site surveys are carried out to gain more detailed information on the area where an exploration well may be drilled and to confirm that the selected drilling location is safe and that any sensitive environments can be avoided. The process normally involves taking geological samples from the seabed and carrying out shallow seismic surveys. These activities have low social or environmental impacts and, therefore, usually do not require a separate environmental or social impact assessment.</div>	<div>5.</div> <div>Exploration Drilling</div> <div>Exploration wells are drilled to determine whether hydro-carbons are present. This phase can be accompanied by a step-change in activity and visibility to local people as exploration can involve a drilling rig, supply vessels and helicopters for transporting personnel. Exploration drilling is preceded by various assessments to understand potential health, safety, environmental, social, security and human rights impacts. These assessments identify appropriate steps to reduce impacts, manage risks and assist in operating responsibly. Limited community development programmes may also be put into place at this time depending on the nature of the programme.</div>
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<div>Creating value</div> <div>In 2014 we conducted due diligence on farm-in opportunities including the Mesana blocks in Spain. We farmed-in to the PL420 block and drilling project operated by Statoil in the Norwegian sector of the North Sea. We also farmed-out of UK sector blocks P2040 and P2086, reducing our interests south of Catcher.</div> <div><div>22</div>Discover more: <i>Operational review</i> on P22-27</div>	<div>In 2014 Cairn participated in the recent licensing round in the Barents Sea, Norway.</div> <div><div>22</div>Discover more: <i>Operational review</i> on P22-27</div>	<div>During 2014 Cairn successfully completed seismic surveys offshore the Republic of Ireland and Malta. As non-operator, we also participated in seismic operations offshore Western Sahara. Application for seismic surveys is pending offshore in the Gulf of Valencia.</div> <div><div>22</div>Discover more: <i>Operational review</i> on P22-27</div>	<div>Pre and post drilling surveys were completed for wells offshore Senegal and following drilling offshore Morocco.</div> <div><div>22</div>Discover more: <i>Operational review</i> on P22-27</div>	<div>In 2014 we continued our exploration drilling campaign offshore Morocco, and initiated and completed an exploration drilling campaign offshore Senegal. We were also involved, as non-operator, in exploration drilling in the UK and Norwegian North Sea. Drilling in the Cap Boujdour block, offshore Western Sahara, commenced in December 2014.</div> <div><div>22</div>Discover more: <i>Operational review</i> on P22-27</div>
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Bourbon Topaz, supply vessel offshore Senegal.



On board the Cajun Express drilling rig offshore Senegal.

6.

Appraisal Drilling

If promising amounts of oil and gas are confirmed during the exploration phase, appraisal drilling is then conducted. This establishes the size and characteristics of the discovery and provides technical information to determine if the discovery is commercial and subsequently optimise the method for recovery of the oil and gas. The potential impacts associated with appraisal drilling are comparable to exploration drilling and similar assessments are carried out in advance.

7.

Development

If appraisal wells show technically and commercially viable quantities of oil and gas, a development plan is prepared and submitted to the relevant authorities for approval. This includes a rigorous assessment of all the potential risks and a long-term assessment of environmental and social impacts covering a timeframe of between 10 and 30 years.

The plan will also detail projected benefits to local communities, for example employment and supplier opportunities, as well as proposing how to manage potential impacts such as an influx of workers from outside the local community. At this stage good design is important to remove and mitigate risks to an acceptable level, as well as managing construction and installation in a manner to likewise minimise impacts.

8.

Production

A variety of options are available for the production of oil and gas. During this phase, which can last many decades, regular reviews are made of social and environmental performance to ensure that impacts identified in the assessments are mitigated. Changes in the risks associated with activities are assessed throughout the production period. Safe operations remain an ongoing requirement at this stage, which means personnel are competent and good HSE behaviours are in place, and equipment is properly maintained and operated.

9.

Decommissioning

This phase occurs when hydrocarbons can no longer be extracted safely or economically at the end of any field life-cycle. Decommissioning consists of closing operations in a manner that protects people and the environment to avoid unacceptable legacy issues for local stakeholders and the Company.

Adding value

Due to the delay in refurbishment of the Blackford Dolphin rig, the proposed Spanish Point appraisal well, offshore Republic of Ireland, could not be drilled in 2014 during the safe weather window and was therefore postponed. Preparation for anticipated appraisal drilling in Senegal is underway.

22 Discover more: *Operational review* on P22-27

We are participating as non-operator in two development projects, the Kraken and Catcher fields, in the UK North Sea.

17 Discover more: *North Sea development* on P17

Realising value

We currently have no operated production, but historically had significant production through our Indian business which we subsequently exited, Cairn India Limited (CIL). Our involvement in exploration and latterly production in India brought social and economic development to a number of regions. We anticipate production from our non-operated Catcher and Kraken fields from 2017.

29 Discover more: *Cairn in India* on P29



# Recognising that good people management is key to a high performing organisation

Core to Cairn's business are its people and we understand that our success depends upon the wholehearted support and commitment of our employees. During 2014 we looked very closely at our organisation to ensure we had the right people in place to meet the future activity levels and work programme of the business. This resulted in a reorganisation of the business to ensure forward business objectives could be met. Attracting, developing and retaining the capability required to deliver our business objectives remained a key consideration throughout the year.

## Organisational effectiveness

The Group reorganisation was announced and implemented during 2014. It was important that this process resulted in the retention of core technical skills and a strong leadership team, whilst allowing for certain non-core capabilities to be outsourced.

After the reorganisation was announced to all employees in June 2014, we commenced an extensive collective and individual consultation process with elected employee representatives and all members of staff across the Group. During the consultation process, we were able to minimise the need for compulsory redundancies through the identification and acceptance of voluntary redundancy applications. In total by June 2015, we will have reduced our staff and contractor headcount by around 40% and have recruited fewer external candidates than in previous years. It was critical that throughout this process people were treated with respect, with the needs of the future business in mind, and that the process was conducted transparently. To support those who were displaced, we held a successful career management day which included a number of workshops designed to provide individuals with the skills and knowledge required to make the transition to a new career. The option to accept further formal outplacement support or receive a training allowance to develop new skills was also offered to those leaving to provide essential support at a difficult time. To support all our staff impacted (those staying and those leaving) we held a number of change management workshops to help develop resilience and coping strategies.

## Engagement

Throughout the year, during a period of transition and uncertainty, we continued to focus on engaging our employees with the business, ensuring that our people were informed and engaged in our strategic and business progress.

We achieved this through a variety of different communication mediums including regular company meetings involving our overseas offices, email updates from senior management and teambuilding events. Our Executive Directors also host regular "coffee and chat" sessions with small groups of staff from across the business to facilitate two-way conversations about strategy, operations and the working environment.

To measure engagement levels amongst our people as part of our commitment to understanding how our people feel about working at Cairn, we conducted an internal employee survey in December 2013. The survey demonstrated a good participation rate with 76% of staff responding. The survey identified a number of areas of strength at Cairn including how employees feel about their job and the Company; the perception that Cairn has a positive impact on society; and high levels of satisfaction with the pay and benefits offered at Cairn. The survey also identified a number of areas for development, which we will continue to focus on.

As part of this engagement strategy and our wider commitment to corporate responsibility, we encourage staff to support worthwhile causes and allow all our staff up to three days' paid leave per year to enable them to participate in volunteering

activities. One such teambuilding event during the year was undertaken by our team of Executive Assistants in our Edinburgh headquarters. The "Cairn terriers" set up a market stall event in the office building in support of the children's charity Barnado's, raising over £5,000 in the process. In addition to raising money for a local charity, which is part of our wider corporate charitable giving programme, the event helped to develop team working skills and engagement throughout the business by generating widespread support amongst employees.

## Performance management

Recognising that good people management is key to a high performing organisation, in 2014 we introduced a revised performance management process across the group, designed to be simpler for staff and management, and to connect staff performance to business performance, creating a more cohesive performance measurement process. This enables our staff to monitor their personal progress against the progress of the business, mirroring the objectives of the business, and understanding why and how their objectives are set. In practice, our strategic objectives and Key Performance Indicators (KPIs) provide the starting point for setting business objectives at the highest level of the organisation. These goals are then cascaded to department and individual objectives.

*"I have found the regular monthly one-to-one meetings with my manager a useful routine to adopt. It has helped me to know where I am in relation to achieving my objectives, keeps me focused and ensures that I commit to my own personal development. The new approach to Performance Management at Cairn has further enabled me to clarify what my manager expects of me and to seek feedback on my strengths and areas for development. I now have so much more clarity on my role and responsibilities and how I contribute to the performance of my department."*

Quote from team member



*“The Group reorganisation was announced and implemented in 2014. It was important that this process resulted in the retention of core technical skills and a strong leadership team, whilst allowing for certain non-core capabilities to be outsourced.”*

*“Our new performance management system has helped me to focus on the output of my team members through regular one-to-one conversations about progress. It has further ensured that my team and I have a better understanding about how our objectives fit with the company’s overall business aims.”*

Quote from line manager

The new process was designed following an extensive consultation process across the organisation and in collaboration with a group of internal “People Champions”, and is intended to reinforce our identified high performing behaviours and values which are based on our core business values of respect, relationships and responsibility. Employees are encouraged to actively seek feedback which should be provided in a positive and constructive way. In addition, a number of People Management Accountabilities were introduced, which outline what we expect from all our managers in encouraging, supporting and motivating their teams. The process is supported during the year through regular monthly one-to-one meetings with line management in addition to the year-end annual performance review.

Our new approach to performance management was designed to ensure that:

- our people understand their accountability for delivering personal performance objectives;
- assets, functions, teams and personal performance objectives are connected to business goals;
- key behaviours which underpin high performance and which help us work together in a matrix organisation are clearly communicated and understood; and
- performance management becomes an ongoing process and not a once-a-year event.

Diversity

Diversity is about valuing everyone as an individual: everyone is unique. Diversity can add varied ideas and perspectives to a workplace and helps to develop an open and inclusive working culture. A diverse workforce is important to Cairn and in 2014:

- 49% of Cairn staff were women
- 12% of Cairn staff worked part-time
- 76% of parents returned to work following maternity/adoption/paternity leave
- 14 different nationalities were employed at Cairn
- 2.8% of the workforce had a disability
- Average age at Cairn was 43
- 25% of management roles were held by women
- 14% of PLC Board were women.

In 2014, Cairn continued to roll out equality and diversity training to staff and contractors. The training is designed to further increase awareness of Cairn’s commitment to equality of opportunity, and the behaviours expected of everyone when it comes to treating others with dignity and respect.



Staff in Edinburgh headquarters.

# Twice per year we identify CR priorities to guide our CR activities as the business develops

## How we identify our key CR priorities

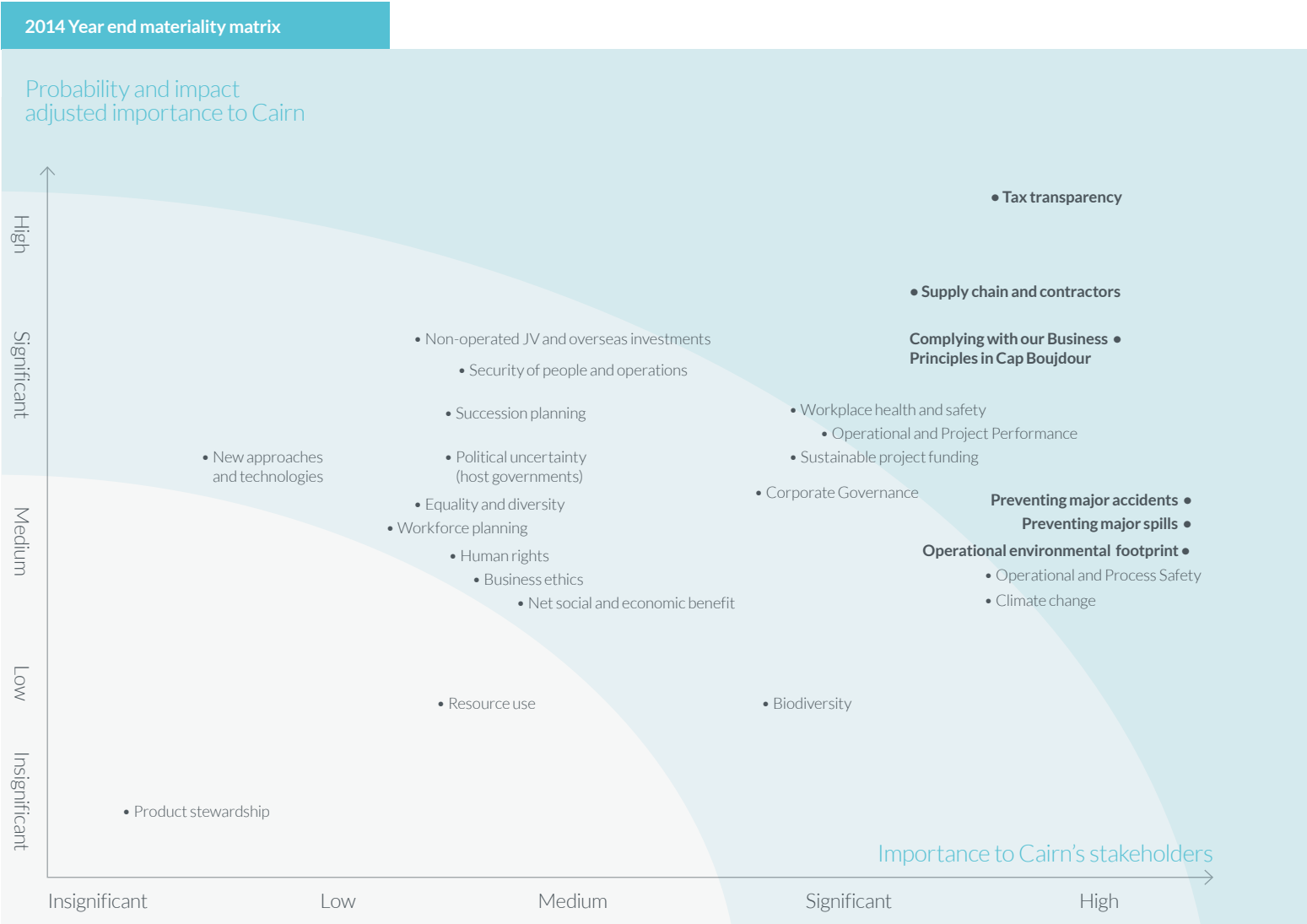
Our CR priorities reflect the topics that matter most to our business and our stakeholders. The process by which we identify these priorities is known as a materiality assessment process. We improved the materiality assessment process in 2014, by introducing a more objective methodology with defined criteria, more closely linked to our business risk management procedure.

These improvements were made in response to recommendations from both an internal CR Management System (CRMS) audit and an external review of our 2013 CR report. The revised process was trialled for the 2014 interim report, then refined and rerun for the 2014 Annual Report.

Our 'CR Materiality Methodology' is based on the AccountAbility APS model (an internationally recognised framework developed by AccountAbility) and helps us conform to the latest Global Reporting Initiative (GRI) sustainability reporting guidelines known as G4, which Cairn adopted in 2014. G4 is superseding the GRI G3.1 guideline against which we have reported since 2011. GRI is a leading organization in the sustainability field.

In 2014 the identification of our CR priorities was carried out during a 'materiality' workshop attended by senior management and facilitated by a third party.

As part of the improved materiality assessment process corporate and operational risks, identified during the business risk management procedure, are grouped into clear CR topics. These topics are then assessed against criteria aligned with the risk management procedure. This gives a rating for 'Probability and Impact Adjusted Importance to Cairn' for each topic.





The topics were then assessed in relation to fixed criteria for ‘Importance to Stakeholders’ and mapped onto a materiality matrix (as shown below) with final broad classifications of ‘high’, ‘medium’ or ‘low’ for each topic. Those receiving a ‘high’ rating are regarded as material in the reporting process and also used to focus attention for objective setting.

Understanding the matrix:

The importance to Cairn is plotted on the vertical axis of the materiality matrix. The importance to stakeholders is plotted on the horizontal axis. The importance to Cairn reflects the probability and impact of a topic in line with our risk assessment criteria. The importance to stakeholders uses a number of criteria with increasing impact. In this way ‘Preventing major accidents’ has a low probability but high impact when using Cairn’s risk criteria, giving a medium rating; however, it is classified as high against the stakeholder concern criteria therefore when plotted in the matrix it is a ‘high’ material issue.

CR priorities

Six material issues

Six material issues were identified to be of ‘high’ importance to both our stakeholders and to Cairn and these are described on the following pages. Further information on how we identify, assess and manage these CR topics as well as the majority of those identified as ‘medium’ is also available on the Cairn website at [www.cairnenergy.com/responsibility](http://www.cairnenergy.com/responsibility).

Supply chain and contractors

Read more on page 50

Preventing major accidents

Read more on page 51

Preventing major spills

Read more on page 52

Operational environmental footprint

Read more on page 54

Tax transparency

Read more on page 55

Complying with our Business Principles in Cap Boujdour

Read more on page 57

CR priorities

# Supply chain and contractors

With up to 78% of the hours worked in connection with Cairn's business contracted out to various parties at times of significant operational activity we place a particular emphasis on selecting the right service providers, communicating expectations, ensuring effective policies and management processes, monitoring performance and sharing lessons learned.

All our contractors are required to work within industry good practice frameworks and they must have clear Health Safety and Environment (HSE) management systems in place to understand risks associated with their activities and implement appropriate measures in a manner to control them. We have a rigorous selection process to assess the suitability of contractors, which includes assessing their ability to conduct operations in line with our Business Principles and Group policies and procedures. In 2014 we revised our Contractor Selection and Management Procedure improving integration of our CR requirements from contractors, as well as refining our tender selection criteria for both drilling rigs and seismic vessels. Following appointment, we link our contractors' HSE or CR systems to our CRMS using a bridging document which lays out responsibilities and clarifies areas of potential uncertainty. This is supplemented by project specific procedures which must be adhered to. For example, in Senegal specialist contractors were used for management of hazardous waste to ensure that good 'Duty of Care' practices were followed and that the treatment and disposal was undertaken at suitable facilities by fit and proper persons.

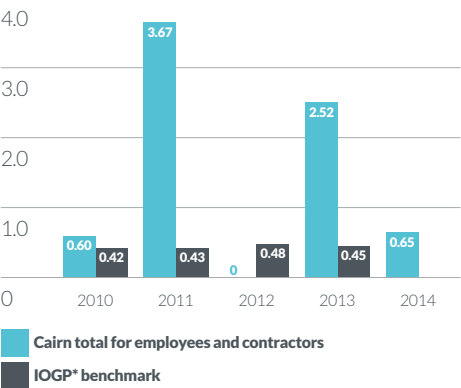
### Lost Time Injury

In 2013 we initiated a Strategic Contractor Engagement Campaign marked by our Chief Executive visiting the Cajun Express rig during operations offshore Morocco in November 2013, following two Lost Time Injuries (LTIs) experienced shortly after drilling commenced that same month. This Campaign was intensified in 2014. All key contractors were engaged by senior personnel on the importance of maintaining HSE and CR standards as the key priority for our 2014 projects offshore Senegal, Republic of Ireland and Malta. A total of 13 major contractors were engaged in this way prior to activities commencing. Senior management continued to visit operational locations with 14 rig visits attended by personnel of Project Manager level or above. These visits served to reinforce our commitment to HSE amongst both our own personnel and our contractors.

Despite our efforts, during 2014 we experienced one LTI on the Cajun Express rig. A member of the rig

crew was injured following a fall whilst carrying out planned preventative maintenance on the drilling top drive system. A detailed accident investigation was completed and corrective measures were taken to avoid recurrence. Overall our Lost Time Injury Frequency (LTIF) and Total Recordable Injury Rate (TRIR) are lower than experienced in 2013.

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



\* IOGP is the International Association of Oil & Gas Producers. We have included overall IOGP benchmark figures (average of onshore and offshore).

As part of our commitment to generate a positive net social and economic benefit we recognise the importance of developing local contractors to support our activities wherever we can. However, sourcing skilled, local contractors in areas where there is not

already a developed oil and gas industry can be difficult. In 2014, contracts were awarded to local supply base logistics providers in Morocco, Senegal and the Republic of Ireland. Particular attention was paid to developing health and safety performance among local contractors through locating experienced HSE advisers at our shore bases in Agadir, Morocco; Dakar, Senegal; and Foynes, Republic of Ireland. These HSE advisers provided, amongst other activities, training, ongoing coaching and supervision, defensive driving courses, and training on waste handling. Specialist heavy lifting training was provided in all locations as these contractors had limited experience of some of the specific equipment used by the industry.

### Anti-Bribery and Corruption

Our Group Code of Business Ethics and Anti-Bribery and Corruption (ABC) System not only guides our own behaviour but also clarifies our expectations of partners and suppliers. Before entering into a business relationship, we undertake a process of information gathering and risk identification, with the option to undertake further third party checks if any concerns do arise. To assist with the risk assessment process, we use various due diligence tools which enable us to identify potential 'red flags' and establish whether potential issues are manageable and if any resulting risks lie within our risk appetite statement. As an example of this, we conducted third party due diligence checks on over 20 suppliers and business partners.

During H1 2014 we updated our procedures to further minimise the risk of bribery and corruption in the supply chain. In Senegal Cairn worked closely with

Case study

Managing waste

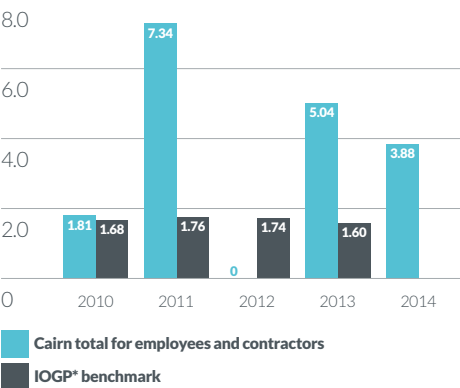
Cairn pays particular attention to the waste management capabilities of our host countries and wherever we operate, we aim to conform to EU based approaches to waste management.

This includes not only the application of a waste management hierarchy (avoid, reuse, recycle, recover, dispose) but also requirements of 'Duty of Care'.

Duty of Care requires prevention of escape of waste; appropriate handling, treatment and disposal; and, handing such waste by 'fit and proper' persons.

In both Senegal and the Republic of Ireland, local contractor capabilities and options for disposal of hazardous wastes are restricted. In the case of the Republic of Ireland, as part of the EU, long established methods are available to meet 'Duty of Care' requirements including treatment in the UK where necessary.

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



\* IOGP is the International Association of Oil & Gas Producers. We have included overall IOGP benchmark figures (average of onshore and offshore).

\*\* 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 ongoing production and other long-term operations.

the business ethics specialist Good Corporation to undertake a detailed risk assessment of the business environment, with a specific focus on potential bribery and corruption risks. The local presence and knowledge of the Good Corporation helped guide and shape our approach to managing the potential risks and implementing mitigations. This included developing a local ABC Management System and preparing training in both English and French.

By contrast, in Senegal such methods are limited especially in relation to wastes generated from the offshore oil and gas industry given this is largely a new industry in the country. Consequently, Cairn conducted a specialist review of waste disposal options in and around Dakar, Senegal and engaged a specialist experienced contractor with both expert knowledge of local capabilities and ability to develop sound Duty of Care programmes for the project.

CR priorities

# Preventing major accidents

The prevention of any accident remains a key focus for Cairn and the wider oil and gas industry and is recognised as a material CR topic for Cairn which requires significant ongoing vigilance and attention. We apply rigorous procedures to identify, assess and manage potential risks and impacts in line with the As Low As Reasonably Practicable (ALARP) principle.

Our drilling operations, both operated and non-operated, are the key focus of our drive to prevent major accidents.

The exploration wells offshore Morocco and Senegal were designed in accordance with the requirements of the Cairn Well Engineering and Construction (WEC) Department and CRMS. These requirements include various well engineering and control barriers applied during well design and operation (see 'Preventing major spills'). All Cairn well designs are assessed by an independent external expert well examiner who verifies that the design complies with defined standards based on UK best practice.

In Senegal, the exploration drilling programme only commenced once the well risk assessment, major accident safety study, and emergency/oil spill response plans had received approval from the Senegalese regulators. An operational readiness audit was also conducted including an independent expert assessment of critical equipment and systems before drilling

commenced. All contingency plans, equipment and trained staff were in place prior to starting the first well. As required under Senegalese legislation the rig and supply base were inspected and authorised by the Senegalese regulator before and during the drilling process.

In respect of our non-operated activities Cairn continued to work closely with EnQuest and Premier Oil on our United Kingdom Continental Shelf (UKCS) development assets, the operators of Kraken and Catcher respectively. This included understanding the HSE risks associated with the projects to ensure robust mitigation plans are implemented throughout the design, construction, commissioning and operational phases. In addition, as in previous years, we continued to fulfil our 'see to' obligations in our Norwegian activities. This is a requirement that non-operating partners must assess HSE arrangements of the block operator prior to approval of activities being given by the Norwegian regulator. This ensures all non-operating parties assure the planned activities being and take responsibility for them. In line with our objective of becoming an operator in the Barents Sea we are furthering our efforts to demonstrate our operational capabilities in both Norway and the UK.

In conjunction with our partners and industry bodies we continue to monitor potential legislation changes in the UK and other EU jurisdictions due to the introduction of the new EU Offshore Safety Directive.





CR priorities

# Preventing major spills

The prevention of major hydrocarbon spills and preparation for response in the unlikely event of a major spill event remain of critical importance to the oil and gas industry and to Cairn and our stakeholders.

During the year we continued to focus on ensuring the integrity of the exploration wells drilled offshore Morocco and Senegal as described in 'Preventing major accidents' and to adopt industry good practice in assessing the risks of oil spills and in oil spill response planning.

To prevent a major accident and oil spill we take a number of steps:

### Design

Our wells are designed and independently assured to a level that exceeds requirements for the expected characteristics of the geological formations to be encountered. We apply our well design standards to ensure the appropriate materials are used and installation methods conform to recognised good industry standards. A qualified external well examiner independently assesses the well design and proposed development methods. This gives us assurance that the well development will meet safety standards. We select drilling fluids to maintain well integrity and also to minimise impact on the environment (see also 'Preventing major accidents').

### Primary well control

We apply a dual barrier approach during drilling activities. This involves control measures designed to maintain fluids in the wellbore, including drilling-hole pressure evaluation and management, kick detection, kick tolerance management, fluid management, cementing practices, blow-out preventer (BOP) system testing and assurance. Testing of a BOP is rigorous and is conducted routinely on a defined schedule to ensure it

remains functional. In the event of unsuccessful tests we make safe the well and cease drilling until resolution of any problem, which can result in substantial lost time and cost. Despite this we do not recommence drilling until completion of work and if necessary specialist support to assure function. We do not compromise in this area.

### Secondary well control

This includes measures to prevent the wellbore fluids escaping from the well, using a BOP. The BOP installed on the wellhead at the seabed is made up of a series of hydraulically operated rams and can be operated in an emergency from the rig or via the backup Remotely Operated Vehicle (ROV) on board the standby vessel which remains with the rig. The BOP is rated for pressures greatly in excess of those expected to be encountered in the exploration well.

### Tertiary well control

These measures provide a third line of defence when formations cannot be controlled by primary and secondary measures and cover well control options such as drilling of a relief well and use of a capping device.

## Case study

# Working with stakeholders on oil spill planning

In Senegal we held an emergency and oil spill management seminar with a variety of stakeholders in late 2013.

This assisted in establishing our 2014 response capability and interfaces with in-country response capability. In addition, a field equipment deployment exercise was conducted in Senegal which used our offshore vessel contractors and shore base personnel.

We shared a video of this exercise with the authorities and local contractors.

During early May 2014, in the Republic of Ireland, Cairn participated in the successful Shannon Estuary Anti-Pollution Team (SEA-PT) oil spill exercise in County Galway. This was helpful in developing our Oil Spill Contingency Plan and in understanding local capabilities. It was well attended and gave us the opportunity to work directly with stakeholders including local council representatives, local environmental experts, the Irish Coast Guard and other civil authorities.



Additionally, in the unlikely event of an oil spill we are able to provide an effective oil spill response. We have applied the latest good practice in all of our recent and future drilling programmes.

- **Planning** – applying the IOGP Joint Industry Project (JIP) new approach to oil spill risk assessment and response planning which includes a structured and detailed analysis of oil spill risk, including: development of potential spill scenarios; likelihood and consequence analysis; detailed modeling; development of a credible response capability; and plans submitted and approved by the authorities in Senegal and in preparation for future drilling in the Republic of Ireland;
- **Surface response capability** – maintaining tiered oil spill response capability including Associate Membership of Oil Spill Response Limited (OSRL) for access to established Tier 3 oil spill response equipment. We also enhanced our Tier 2 capability in Senegal through membership of Western and Central Africa Aerial Surveillance and Dispersant Spraying Services (WACAF). OSRL membership also gave us access to highly experienced consultants who assisted in the development of the oil spill response plans and who could assist in the event of an oil spill;

- **Subsea cap and secure capability** – Cairn maintained access to the Subsea Well Incident System (SWIS) which includes the Capping Stack System (CSS), the Subsea Incident Response Toolkit (SIRT) and the Global Dispersant Stockpile, all of which are managed by OSRL. We ran logistics workshops and continued improving our ability to mobilise and deploy this equipment;
- **Oil Spill Contingency Plans (OSCPs)** – these were developed using latest IOGP practices and approved in Senegal before drilling commenced. We consulted a number of stakeholders including government departments, non-government organisations (NGOs), local response organisations and subject experts for development of our OSCP in preparation for drilling an appraisal well in the Republic of Ireland; and
- **Preparedness** – training and emergency exercises were held at our Edinburgh headquarters and operational sites in Senegal during 2014 and preparations made for the Republic of Ireland. These helped to embed roles and responsibilities and rehearsed application of the oil spill plans and emergency response plans in our field locations.

As shown in the tables below, in 2014 we maintained our record of no oil spills to the environment in the last five years.

Total spills to the environment (number)

	2010	2011	2012	2013	2014
Oil	0	0	0	0	0
Fuel	1	1	0	0	0
Chemical	3	0	1	0	0
Waste	0	0	0	0	0
Other	0	2	0	0	0

Total spills to the environment (barrels)

	2010	2011	2012	2013	2014
Oil	0	0	0	0	0
Fuel	28.30	0.06	0	0	0
Chemical	56.85	0	2.20	0	0
Waste	0	0	0	0	0
Other	0	9.44	0	0	0



Oil spill response exercise, Senegal.

CR priorities

# Operational environmental footprint

In many parts of the world we operate under specific regulatory requirements in order to prevent or minimise any impact of our activities.

However, where regulatory requirements are not in place or are limited, we always carry out an environmental assessment of the local area prior to undertaking any significant operational activity. These assessments allow us to understand how our activities may impact the environment and local activities and how we can avoid or minimise any impact. They also provide important background information.

During 2014 the following environmental assessments were completed:

- **Senegal** – an Environmental and Social Impact Assessment (ESIA) and Environmental and Social Management Plan ahead of our offshore drilling operations;
- **Republic of Ireland** – an Environmental Area Assessment (EAA) in planning for the drilling of an appraisal well. During the planning process it became clear that the refurbishment of the Blackford Dolphin would not complete in time to meet the safe weather window. Consequently the Spanish Point appraisal well was postponed;
- **Republic of Ireland** – submission of an EAA ahead of a 3D seismic campaign conducted offshore in Q3 2014. Approval to proceed was received in July. The survey was conducted successfully and we applied the new ‘Guidance to Manage the Risk to Marine Mammals from Man-made Sound Sources in Irish Waters’; and

- **Malta** – an environmental review in line with Environmental Impact Assessment (EIA) good practices was conducted prior to commencing and completing the 2D seismic campaign offshore in late March/early April. Though not a regulatory requirement the review was used to identify and apply mitigation measures during the seismic acquisition process.

CR plans, which include environmental requirements, and compliance registers are put in place for all our operational programmes and these have been adhered to with no issue of non-conformance or non-compliance during 2014.

## Greenhouse gases

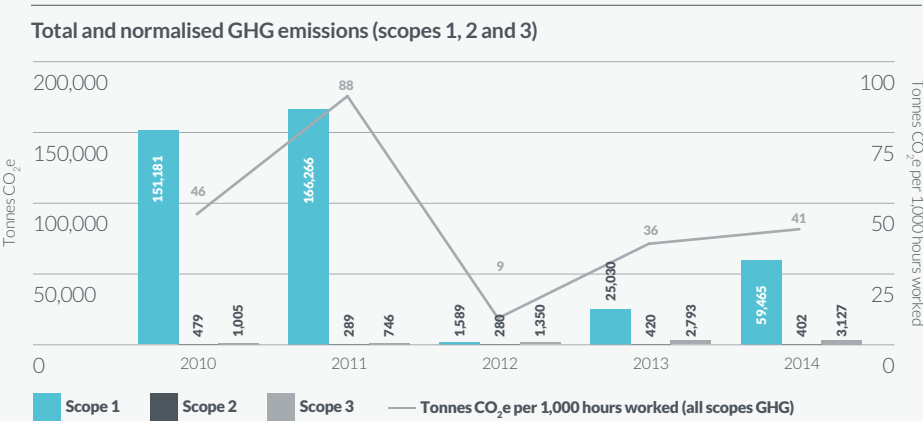
Greenhouse gases (GHGs) form a part of our operational environmental footprint. We monitor and manage the GHGs emitted during our activities and disclose them in accordance with industry requirements and standards. We disclose on an ‘operational control’ basis which means we report emissions from those assets which are operated by us and not from those controlled by our partners. With no operated production facilities, our direct GHG emissions occur primarily from the combustion of fuel on rigs and vessels during the drilling of wells or acquisition of seismic.

The graph below indicates that our GHG emissions over the last five years are heavily dependent on the level of operational activity in any given year. 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. GHG intensity levels in 2014 are slightly higher than in 2013 largely as a consequence of an extended stay on one of the Senegal wells resulting from operational delays. In addition, the figures for Scope 3 GHGs (business travel) have all increased, including historic data, due to changes in calculation factors in line with DEFRA 2014 updates.

## Water, wastewater and waste

Water use in our 2014 activities was not regarded as a significant or material issue due to the nature of our offshore activities and abundance of local supply. Wastewater discharges and waste disposals consisted of typical vessel sanitary discharges and discharge and disposal of drilling wastes. Cairn used water based drilling fluids in the 2014 drill campaigns and these were discharged in line with good industry practice following an exercise to minimise less benign substances. Waste management in Senegal received particular attention in order to ensure a ‘Duty of Care’ was maintained in line with European practice (see Supply chain and contractors).



Notes:

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

1. For calculating Scope 1 (direct) GHG emissions we use emission factors from the API Compendium 2009 and also from EEMS 2008 (UK Environmental and Emissions Monitoring System for the Department of Energy and Climate Change (DECC)).

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

3. In 2014 we updated our methodology for calculating Scope 3 (business travel) emissions in line with DEFRA 2014, including its recommendation to include an uplift for the influence of radiative forcing in air travel emissions. This uplift ensures that the maximum climate impact of an organisations’ travel habits is captured. We have re-baselined our historic data in line with DEFRA 2014. All of our Scope 3 emissions figures have increased considerably because of these updates. (DEFRA 2014 methodology and conversion factors can be found at <http://www.ukconversionfactorscarbonsmart.co.uk/>) For further details about our GHG emissions’ data and calculations, please see our website.



Artemis Atlantic vessel used to acquire 2D seismic data offshore Malta, 2014.

Case study

# Minimising the impact of noise during 3D seismic operations offshore Republic of Ireland and Malta

In 2014 we undertook a 3D seismic survey in the Porcupine Basin, offshore west Republic of Ireland. The survey was conducted in August and September and resulted in the acquisition of nearly 1,000km<sup>2</sup> of 3D seismic data. There is a significant marine mammal presence in the area and as such it was important to minimise the impact of noise generated by seismic air guns on the marine mammal population during the survey.

The Irish National Parks and Wildlife Service provided new guidelines on minimising the impact of man-made noise in 2014 and these, along with the findings of the Environmental Area Assessment (EAA) undertaken by Cairn, formed the basis for our mitigation measures. As with all our seismic operations, Cairn employed two Marine Mammal Observers (MMOs) who worked on board the seismic vessel for the duration of the campaign.

The impact of noise was primarily minimised by using a process called 'soft start', in which we slowly increase the power of acoustic sources over a minimum of 40 minutes, giving marine mammals time to leave the area before

we reach maximum power. Operations would be delayed until any marine mammals sighted are observed to be at a safe distance of 1,000 metres for 60 minutes. Should the air guns be shut down in the hours of darkness, they would not be restarted until daylight which enables the MMOs to carry out a pre-survey watch.

Summary reports on marine mammal observations were sent to the Irish regulator daily and a comprehensive report was compiled detailing the marine mammal interactions and the mitigation measures employed.

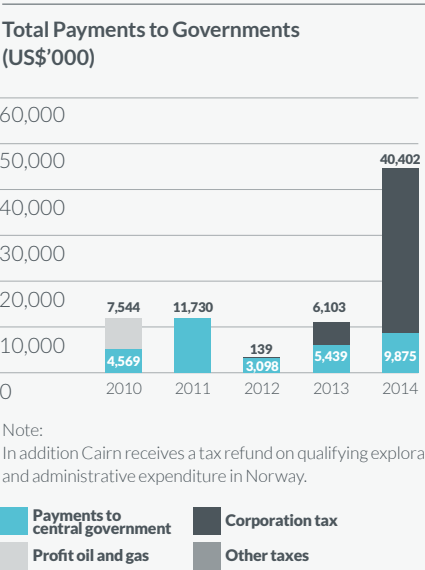
By contrast no specific environmental assessment was required or noise restrictions imposed for shooting seismic offshore Malta. However, in accordance with our internal standards we conducted an environmental review using Environmental Impact Assessment (EIA) practices and ensured that we applied the approach described under the Agreement on the Conservation of Cetaceans of the Black Sea, Mediterranean Sea and Contiguous Atlantic Area (ACCOBAMS).

CR priorities

## Tax transparency

Cairn operates in various different territories with diverse tax obligations and requirements and we are committed to ensuring that in every territory we comply fully with local tax rules and regulations.

We support transparency of tax contributions and other payments to Governments and as such became a Participating Company in the Extractive Industries Transparency Initiative (EITI) in September 2013. As in previous years, we have disclosed our payments to governments as shown below.





Atwood Achiever drillship  
operating CB-1 well.



## Working responsibly continued

### Mapping CR priorities continued

CR priorities

# Complying with our Business Principles in Cap Boujdour

**Cairn has a farm-in agreement with Kosmos Energy for a 20% non-operated interest in the Cap Boujdour exploration block.**

The farm-in builds on Cairn's presence in three countries in Morocco, Senegal and Mauritania.

The CB-1 exploration well commenced operations on the Al Khayr prospect in December 2014 following the successful completion of a 3D seismic survey by Kosmos in the late summer.

Western Sahara has been classified since 1961 as a 'Non-Self-Governing Territory'. Both Morocco and the Saharawi Arab Democratic Republic claim Western Sahara as their sovereign territory. Hydrocarbon exploration offshore of the territory is consistent with international law. Resolution of the territorial status is not required for exploration as the UN 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 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.

*"Both Cairn and the operator, Kosmos, believe that responsible resource exploration and, if successful, development in Western Sahara can occur in parallel with the UN-led discussion on the region's future."*

Responsible resource development can proceed in parallel with the UN-led discussions on the region's future, as long as any such resource development is conducted for the benefit of the people of the territory.

### Applying our Business Principles

Prior to finalising the decision to farm-in to Cap Boujdour Offshore, an extensive due diligence management process was undertaken to fully understand any risks associated with the project.

In late 2013, Kosmos made a joint declaration with the Government of Morocco setting out shared commitments regarding exploration activities and the key principles under which hydrocarbon development would proceed<sup>1</sup>. As part of the ongoing engagement programme, governments and international governance and economic experts have been engaged to contribute to a framework for hydrocarbon development in the region. During 2014 Cairn also participated and supported Kosmos in discussion to address and apply the Joint Declaration of Principles, in particular, in monitoring and promoting human rights.

In 2014, an Environmental Impact Assessment (EIA) was delivered and approved in accordance with Moroccan legal requirements. In addition and in accordance with international best practice, Kosmos also conducted a voluntary social impact assessment (SIA), the first in the region, to present the project to local stakeholders and address concerns. These helped to improve understanding and assist in developing open lines of communication with local communities and will help shape social investment and capacity building programmes going forward.

This Strategic report has been approved by the Board.



**Simon Thomson**  
Chief Executive  
9 March 2015

1. [www.kosmosenergy.com/pdfs/ONHYM-Kosmos-Joint-Declaration-of-Principles-English.pdf](http://www.kosmosenergy.com/pdfs/ONHYM-Kosmos-Joint-Declaration-of-Principles-English.pdf)

Board of Directors



Executive Directors

Non-Executive Directors

**Simon Thomson**  
Chief Executive (50)

**James Smith**  
Chief Financial Officer (38)

**Ian Tyler**  
Non-Executive Chairman (54)

Biography	<p>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 and holds an LLB (Hons) from Aberdeen University and a Diploma in Legal Practice from Glasgow University.</p>	<p>James Smith joined Cairn in March 2014 from Rothschild where he was a director of the energy &amp; power team with 15 years' experience advising E&amp;P companies, oil majors and national oil companies on their M&amp;A transactions and equity and debt market financing. During his investment banking career, James was a long-standing adviser to Cairn on every major transaction and financing from the IPO of Cairn India until he joined the Company. James holds a BA (Hons) from the University of Oxford.</p>	<p>Ian Tyler was chief executive of Balfour Beatty plc from 2005 until March 2013. During this time he took the company from being primarily a UK construction business, to a global infrastructure services business. Ian graduated with a first class degree in Commerce from Birmingham University. He then qualified as a chartered accountant with Arthur Andersen in 1987. Ian subsequently held a number of senior finance and operational positions within listed companies.</p>
Term of Office	<p>Simon was appointed to the Board in November 2006 as Legal and Commercial Director and became Chief Executive in July 2011.</p>	<p>James was appointed to the Board in May 2014 as Chief Financial Officer.</p>	<p>Ian was appointed as an independent non-executive director in June 2013 and became non-executive Chairman in May 2014.</p>
Independent	<p>Not applicable</p>	<p>Not applicable</p>	<p>Yes</p>
External Appointments	<p>Simon is a non-executive director of Graham's The Family Dairy Limited and a member of the advisory Board of the Winning Scotland Foundation.</p>		<p>Ian is non-executive chairman of Al Noor Hospitals Group plc, a non-executive director and chairman of the audit committee of Cable &amp; Wireless Communications plc, a non-executive director of BAE Systems plc and non-executive chairman of Bovis Homes Group Plc.</p>
Committee Membership	<p>Simon chairs the Senior Leadership Team. He is a member of the nomination committee and attends meetings of the remuneration committee by invitation and part of each audit committee meeting by invitation.</p>	<p>James chairs the Risk Management Committee and is a member of the Senior Leadership Team. He is a member of the governance committee and attends meetings of the audit committee by invitation.</p>	<p>Ian chairs the nomination committee and is a member of the audit committee, the governance committee and the remuneration committee.</p>



### Todd Hunt

**Non-Executive Director (62)**

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

Todd was appointed as an independent non-executive director in May 2003. However, given his length of tenure he can no longer technically be considered to be an independent non-executive director in terms of the UK Corporate Governance Code.

No

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

Todd is a member of the remuneration committee, the nomination committee and the governance committee.

### Iain McLaren

**Non-Executive Director (64)**

Iain McLaren has significant experience in the oil and gas sector. He is a chartered accountant and was formerly senior partner for KPMG in Scotland.

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

Yes

Iain is chairman of Investors Capital Trust plc and a non-executive director of Afren plc, Baillie Gifford Shin Nippon plc, Edinburgh Dragon Trust plc and Ecofin Water & Power Opportunities plc. He is also a past president of the Institute of Chartered Accountants of Scotland.

Iain chairs the audit committee and is a member of the nomination committee and the remuneration committee.

### M. Jacqueline Sheppard QC

**Non-Executive Director (59)**

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

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

Yes

Jackie is non-executive chairperson of Emera Inc., a public Canada-based international energy generation, transportation and distribution company. She is also a director of the general partner of Pacific NorthWest LNG LP, which was formed for the purpose of constructing, owning and operating an LNG facility in British Columbia. She is a founder of two upstream oil and gas companies and is the lead director and chair of the audit committee of one of those companies, Black Swan Energy Inc., a Canada-based private equity financed company. Jackie is also the former chairperson of the Research and Development Corporation of Newfoundland and Labrador, a Crown Corporation.

Jackie chairs both the remuneration committee and the governance committee.

### Alexander Berger

**Non-Executive Director (49)**

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

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

Yes

Alexander is chief executive officer of Oranje-Nassau Energie B.V., and a director of Oranje-Nassau Energie UK Limited and Oranje-Nassau Energy Petroleum Limited.

Alexander is a member of the audit committee, the nomination committee and the governance 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 2014 together with the audited consolidated financial statements of the Group and Company for the year. These will be laid before the shareholders at the AGM to be held on Thursday 14 May 2015.

## Results and dividend

The Group made a loss after tax of US\$381.1 million (2013 loss of US\$555.9 million).

The directors do not recommend the payment of a dividend for the year ended 31 December 2014.

Subsequent events that have occurred after the balance sheet date as at 31 December 2014 are included in Section 6 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 1 to 57 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 76 to 97. 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 84. 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 63 to 72 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 58 and 59. The beneficial interests of the directors in the ordinary shares of the Company are shown below:

	As at 31 December 2013	As at 31 December 2014	As at 9 March 2015
Simon Thomson	387,383	457,567	457,567
James Smith*	0	2,688	2,688
Ian Tyler	0	0	0
Todd Hunt	72,012	72,012	72,012
Iain McLaren	7,878	7,878	7,878
Jackie Sheppard	0	7,000	7,000
Alexander Berger	10,979	40,008	40,008

### Former directors

Dr Mike Watts**	1,164,932	–	–
Jann Brown**	295,550	–	–
Sir Bill Gammell**	596,331	–	–
Dr James Buckee**	37,788	–	–

\* James Smith was appointed as an executive director of the Company on 15 May 2014.  
\*\* As set out in the Company's Corporate Governance statement on pages 63 to 72, on 15 May 2014, Dr Mike Watts stood down as the Deputy Chief Executive of the Company, Jann Brown stood down as the Managing Director and Chief Financial Officer of the Company, Dr James Buckee stood down as a non-executive director of the Company and Sir Bill Gammell stood down as the non-executive Chairman of the Company.

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 76 to 97.

None of the directors has a material interest in any contract, other than a service contract, with the Company or any of its subsidiary undertakings. Details of the directors' service contracts are set out in the Directors' Remuneration report on pages 76 to 97.

## Share capital

The issued share capital of the Company is shown in Note 5.1 of the Notes to the Financial Statements. As at 9 March 2015, 576,343,551 ordinary shares of <sup>231</sup>/<sub>169</sub> 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 2014 and 2 March 2015 (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 2014	% Share Capital	As at 2 March 2015	% Share Capital
MFS Investment Management	75,181,585	13.05	79,803,779	13.85
BlackRock	54,755,256	9.50	63,854,899	11.08
Greenlight Capital	32,309,120	5.61	32,305,959	5.61
Schroder Investment Management	29,313,125	5.09	24,146,564	4.19
Franklin Templeton	24,248,713	4.21	26,621,773	4.62
Aviva Investors	21,994,682	3.82	24,098,192	4.18
Hotchkis & Wiley	19,534,233	3.39	26,889,183	4.67
Legal & General Investment Management	17,270,219	3.00	–	–

### 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 1 to 57 of this document, which are deemed to form part of this report by reference.

### Financial instruments

The financial risk management objectives and policies of the Company are detailed in Appendix 2 of the Financial Statements.

### Acquisition of own shares

On 25 October 2013, with its focus on capital discipline, the Company initiated a share buy-back programme with a view to maximising shareholder value and optimising capital allocation. The Board considered that the share buy-back programme would maximise shareholder value by increasing the capital gain per share that would be expected in the event of a successful hydrocarbon discovery and that it would be in the best interests of shareholders generally. Therefore, the Company entered into an irrevocable and non-discretionary agreement with its brokers, Morgan Stanley and Jefferies, to repurchase on the Company's behalf and within certain pre-set parameters up to US\$300m of ordinary shares in the Company for cancellation.

# Directors' report continued

## Acquisition of own shares (continued)

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. In the period from the start of the year to 21 March 2014, 18,887,604 ordinary shares were repurchased and cancelled, which represents 3.28% of the called-up share capital of the Company as at that date and as at 31 December 2014. The nominal value of the shares purchased from the start of the year to 21 March 2014 is US\$427,529 and the aggregate amount of consideration paid by the Company for those shares is US\$63,682,702.

## 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 63 to 72 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.

## 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.

The directors consider the Cairn Energy PLC Annual Report and Accounts 2014, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the Company's performance, business model and strategy.

Each of the directors, whose names and functions are listed in the Board of directors section on pages 58 and 59, confirm that, to the best of their knowledge:

- the Group financial statements, which have been prepared in accordance with IFRSs as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Group and Company; and
- the Strategic report section on pages 1 to 57 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 2014 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 2015

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 Thursday 14 May 2015. 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  
9 March 2015

## Corporate Governance statement

### Dear shareholder

*I would like to assure shareholders that since taking over as non-executive Chairman in May 2014, corporate governance remains a matter of high importance for the Company. Maintaining and promoting high standards of corporate governance is central to my role as Chairman and I firmly believe that this is an essential prerequisite to delivering sustainable business performance.*

At Cairn we operate with integrity at all times, recognising that in doing so the Company will maintain the trust of its many stakeholders.

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

The Board were delighted when, in November 2014, the Company received two awards in respect of its 2013 annual report, winning Best Strategic Report in the FTSE 250 category at the ICSA (Institute of Chartered Secretaries and Administrators) Excellence in Governance Awards and Best Annual Report in the FTSE 250 category at the Investor Relations Society Awards. The Company was also highly commended for its corporate governance reporting in the PwC Building Public Trust awards in December 2014. I would personally like to take this opportunity to thank the team involved in annual reporting at Cairn for their continuous effort in producing such an exemplary standard of reporting.



There have been a number of significant changes to the Cairn Board during 2014:

- Sir Bill Gammell retired as non-executive Chairman and I succeeded him in this role;
- Dr Mike Watts (Deputy Chief Executive) stepped down as an executive director;
- Jann Brown (Managing Director & CFO) stepped down as an executive director;
- James Smith was appointed Chief Financial Officer (CFO); and
- Dr James Buckee retired as a non-executive director.

All of these changes took effect immediately following the Company's Annual General Meeting (AGM) in May 2014 and I am pleased to report that the Board has continued to function efficiently and effectively since those changes. James Smith joined the Company in March 2014 and there was a smooth handover of responsibilities from Jann Brown to James Smith prior to his appointment as CFO in May 2014.

Since standing down as executive directors in May 2014, Dr Mike Watts and Jann Brown continued in senior roles with the Company for a proportion of their one-year notice period with their time dedicated solely to seeking to resolve the tax issue in India. Mike and Jann held no executive director responsibilities during this period. The Board agreed in October 2014 to bring Mike and Jann's notice period to an end and day-to-day responsibility for the Indian tax issue was passed to James Smith at that time.

Following these changes, the Board currently comprises myself as Chairman; two executive directors (the Chief Executive and the CFO); and four non-executive directors, all but one of whom are independent. The Company recognises that as Todd Hunt has served on the Board for more than nine years he can no longer technically be considered to be an independent non-executive director. As such the composition of the Board continues to comply with the provisions of the UK Corporate Governance Code, other than in respect of Mr Hunt's independence. Despite this technical non-compliance with the Code, the Board are however confident that Mr Hunt's judgement remains independent and that he continues to display all of the behaviours expected of our independent non-executive directors (see page 65).

### 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](http://www.frc.org.uk)). Cairn is fully committed to achieving compliance with the principles and provisions set out in the Code.

The Board continually reviews the provisions of the UK Corporate Governance Code and has amended or enhanced the Company's governance framework to ensure that the Company complies with the Code (other than as detailed on page 72). Set out below is a statement of how the Company applied the principles in sections A to E of the UK Corporate Governance Code for the year ended 31 December 2014. This statement reports compliance with the version of the Code published in September 2012. The Company recognises that the UK Corporate Governance Code was amended in September 2014 and intends to report against the revised version of the Code in next year's annual report.

### 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 changes described above, the Board currently comprises the Chairman, two executive directors and four non-executive directors. The current directors' biographies are on pages 58 and 59.

The Company considers the significant refreshment of the Board during 2014 to be positive as it brings new thinking to the Company as well as ensuring that the Board's collective experiences equip it to direct the Company's strategy and meet its business needs as they evolve over time. The Board is also mindful that an appropriate balance between directors who can bring a new perspective and those who provide continuity is essential for a business like Cairn's.



# Corporate Governance statement continued

## The Board (continued)

Diversity is a key element of the Cairn Board, with emphasis placed not only on gender but also on nationality and experience. Following the retirement of Jann Brown as Managing Director & CFO in May 2014 the number of women on the Cairn Board has reduced from two to one. The Board does however continue to demonstrate diversity in the broader sense, with 14% female representation and directors from the Netherlands, the USA and Canada, as well as the UK, bringing gender diversity 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 report of the Nomination Committee on page 68 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.

The Chairman's responsibilities include:

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

The Chairman's other significant commitments out-with the Company are included in his biography on page 58 and there were no changes to these during 2014.

The Chief Executive's responsibilities include:

- managing the Group's business and proposing and developing the Company's strategy and overall commercial objectives in consultation with the Board;
- leading the Senior Leadership Team in implementing the decisions of the Board and its committees;
- ensuring the successful and efficient achievement of the Company's Key Performance Indicators (KPIs) and objectives; and
- providing coherent leadership of the Company in representing the Company to its 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 other executive directors has failed to resolve or for which such contact is inappropriate; and
- to meet with the other non-executive directors without the Chairman present, at least annually, in order to appraise the Chairman's performance.

## Re-election of directors

In accordance with the UK Corporate Governance Code, all of the Company's directors are subject to annual re-election by shareholders. As such, each of the directors will seek re-election at the AGM to be held on 14 May 2015. Full biographical details of the current directors can be found in the Board of Directors section on pages 58 and 59.

## 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. The Company conducted an externally facilitated Board evaluation in 2012 and an internal evaluation in 2013.

The 2013 evaluation resulted in some important recommendations for improving the Board's effectiveness which were set out in last year's corporate governance statement. The majority of these were addressed in Q1 2014 under the leadership

of the previous Chairman and the new Chairman has continued to follow up on these.

This year, given the significant changes to the Board during the review period, it was agreed at the August 2014 Board meeting that an internal rather than external board performance evaluation would once again 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.

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, individual Board members and the Chairman.

Following completion of the questionnaires, the Chairman held a series of one-to-one meetings with each of the directors in December 2014 in order to discuss the answers to the questionnaires. The Chairman's own appraisal was conducted by the senior independent director who did this through a series of one-to-one meetings with the other directors before meeting with the Chairman to present feedback.

The findings of the internal evaluation were then discussed with the Board at the March 2015 Board meeting and a number of action points agreed, including the following:

Key actions	Progress
Strategy: in view of market influences impacting on the sector in which the Company operates, the Board recognises that strategy is a dynamic issue and as such must be kept under regular review.	The Board will conduct an in depth strategy session during 2015 in addition to their regular discussions of strategy at scheduled Board meetings.
Succession planning: it was identified that the Board require a clearer process for fully understanding succession planning beneath Board level, including assessing the strength of executive management, succession planning risks and the organisation structure within which the executive team works.	The Chairman has requested that a session on succession planning be built in to the Board agenda during 2015. The Board recognise that this matter should be a topic in which all directors participate going forward rather than delegated to a Board committee.
Board composition: following the changes to the Board during 2014 the Board have committed to appoint up to two new non-executive directors.	A recruitment process is underway with a number of interviews scheduled for H1 2015.

Following the internal performance evaluation process conducted in 2014, the Board and the Board committees are satisfied that they are operating effectively and that each director has performed well in respect of their roles on the Board and its committees.

As explained above, some improvements have been identified and have already been or will be addressed during 2015. Following the results of the individual performance evaluations, 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 individually reviewed by the remuneration committee against KPIs which are set annually (further details of the KPIs can be found in the KPI section on pages 18 to 21). The bonuses payable to the executive directors under the Company's cash bonus scheme (described further in the Directors' Remuneration Report on pages 76 to 97) are linked directly to the results of these reviews.

## Independence of non-executive directors

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

- provides an objective, robust and consistent challenge to the assumptions, beliefs and views of senior management and the other directors;
- questions intelligently, debates constructively and challenges rigorously and dispassionately;
- acts at all times in the best interests of the Company and its shareholders;
- has a detailed and extensive knowledge of the Company's business and of the market as a whole which provides a solid background 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 does however recognise that, in view of the characteristics of independence set out in the UK Corporate Governance Code, Todd Hunt cannot technically be deemed independent given his length of service.

## Induction and development

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

- **Board**  
Directors' and Company Secretary's contact details; list of Board and committee members and dates of appointment; schedule of matters reserved to the Board; financial delegations of authority; Board papers and minutes of previous meetings; schedule of dates for Board and committee meetings; current directors' education programme.
- **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 Rules and Model Code; Procedures, Systems and Controls for Compliance with the Listing Rules and Disclosure Rules.
- **Organisation**  
Group Structure Chart; latest Annual Report and Accounts.
- **Governance**  
UK Corporate Governance Code; FRC Guidance on Board Effectiveness and Audit Committees; ICSA Guidance on Liability of non-executive directors; 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 to its directors. In 2014, 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 2014, the subjects covered by these seminars included:

- Cairn and the Scottish independence referendum;
- a Board risk workshop facilitated by the Company's internal auditor which included a "deep dive" and discussion of the Company's top risks;
- a corporate governance update;
- a cyber security briefing; and
- asset presentations by senior managers at pre-Board meetings.

These seminars are held prior to Board meetings and are attended by all directors present at such meetings (the Company keeps a record of attendance). 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.

## Information and support

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

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

## Directors' and officers' liability insurance

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

## Conflicts of interest

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

## Matters reserved to the Board and delegation of authority

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

By way of example, some of the matters which the Board considered and approved during 2014 were:

- the Company's strategy, business plan and annual budget;
- the Group KPIs for 2014;
- suspension of the Company's share buy-back programme;
- the Company's 2013 Annual Report and Accounts and 2014 half-year accounts;
- the Company's 2013 Effectiveness of Internal Control Assessment Report;
- the Company's 2014 AGM circular;

# Corporate Governance statement continued

## Matters reserved to the Board and delegation of authority (continued)

- the appropriateness of the Group going concern sign-off for the 2013 full year accounts and 2014 half-year accounts;
- the Company's Risk Appetite Statement;
- the Company's strategy for seeking resolution of the Indian tax issue;
- exploration drilling in Morocco and Senegal;
- approval of Field Development Plan for the Catcher development in the UK North Sea;
- the US\$575 million Reserve Based Lending bank facility agreement;
- strategic entry into the Barents Sea and related planning and resourcing;
- divestment of 10% in the Catcher development and adjacent acreage;
- Kraken development FPSO and detailed engineering; and
- participation in the Norwegian APA 2014 licensing round.

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.

Following changes made to the organisation structure of the Company during 2014 there were also a number of changes made to the senior management committee structure beneath Board level.

The main change has been the creation of a Senior Leadership Team (SLT) which has replaced the Executive Team and which combines input from all senior management. The Executive Team previously comprised the executive directors in office prior to the AGM. The new SLT comprises the Chief Executive, the CFO, the Chief Operating Officer (COO), the Director of Exploration and the Company's Regional Directors. 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:

- formulate strategy for finding, developing and producing oil and gas, to be approved by the Board;
- assess and review (and amend as required) the Business Plan in line with strategy;
- generate, consider and direct acquisitions and disposals; and
- determine the requirement for, objective and authors of, Board papers to ensure timely consideration and approval by the Board.

The members of the SLT also form the RMC, which identifies and reviews key business risks – further information with regard to the role of the RMC is contained in the internal control section of this statement on page 70 and 71.

The Management Team (MT) has continued in existence during 2014 but with a revised mandate to allow it to support the new SLT. The MT currently comprises nine members of the senior management team including the members of the SLT as well as the Deputy Finance Director and three functional managers (Human Resources (HR) Manager, Legal Manager and Health, Safety and Environment (HSE) Manager). The MT continues to be chaired by the COO and 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;
- co-ordinate operations and licence management along with resource allocation and organisational alignment to ensure timely and cost-effective delivery against approved budgets; and
- review and approve other day-to-day business requirements, including Health, Safety, Security and Environment (HSSE) matters.

The previously existing HSE Leadership Team has been disbanded with responsibility for Group level HSE/Corporate Responsibility (CR) leadership being undertaken by the SLT. Day-to-day specific operational HSE/CR issues will be managed by the relevant department managers who in turn report to the MT.

Finally, the Company has also created an Exploration Leadership Team (ELT) which is chaired by the Director of Exploration and currently 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 every two weeks to facilitate alignment, consistency, best practice and team work 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 2014, six scheduled meetings of the Board were held, with all of these meetings taking place over two consecutive days. The Company's Board meetings are held over two days to allow for a pre-Board discussion and Board dinner on the first day followed by the Board and relevant committee meetings on the second day.

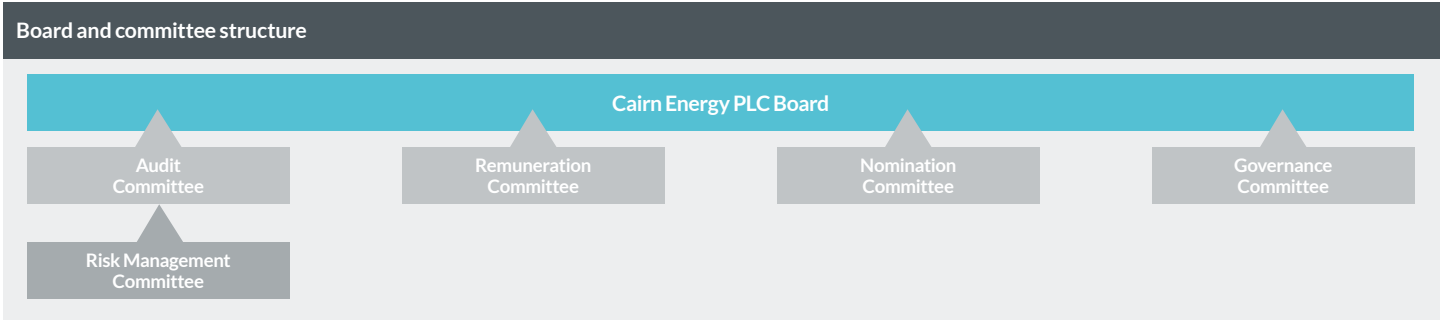
All of the Board meetings during 2014 were held at the Company's registered office in Edinburgh except for one meeting which was held at the Company's office in London. Details of attendance at each of those Board meetings, and at meetings of each of the Board committees, are set out below.

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

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

The formal agenda for each scheduled Board meeting, which regularly includes presentations from senior management, is set by the Chairman in consultation with the Chief Executive and the Company Secretary. Formal minutes of all Board and committee meetings are circulated to all directors prior to the next Board meeting and are considered for approval at that Board meeting. In addition, the members of the Board are in frequent contact between meetings to progress the Group's business.

The non-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 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 remuneration and audit committees) to ensure that non-executive directors can discuss any relevant issues arising from those meetings without executive management being present.



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 2014:

	Board	Audit Committee	Remuneration Committee	Nomination Committee	Governance Committee
Meetings held during 2014	6	5	6	5	4
	Meetings attended	Meetings attended	Meetings attended	Meetings attended	Meetings attended
<b>Executive Directors</b>					
Simon Thomson (Chief Executive)	6	n/a <sup>3</sup>	n/a <sup>3</sup>	n/a	n/a
James Smith (CFO)	6	n/a <sup>4</sup>	n/a	n/a	3
Dr Mike Watts (former Deputy Chief Executive) <sup>5</sup>	2	n/a	n/a	n/a	n/a
Jann Brown (former Managing Director & CFO) <sup>5</sup>	2	n/a <sup>6</sup>	n/a	n/a	2
<b>Non-Executive Directors</b>					
Ian Tyler (Chairman)	6	4	5	3 <sup>7</sup>	2 <sup>7</sup>
Iain McLaren (senior independent director)	6	5	5	4	n/a
Todd Hunt	6	n/a	6	5	4
Alexander Berger	6	5	n/a	5	4
Jackie Sheppard	6	n/a	6	n/a	4
Sir Bill Gammell (former chairman) <sup>8</sup>	2	n/a	n/a	2	1
Dr James Buckee (former director) <sup>9</sup>	2	2	4	n/a	n/a

Notes:

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

- During 2014, 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.
- Where a director was unable to attend meetings of the Board or of Board committees, they reviewed the relevant papers for the meetings and provided their comments to the Board or the Board committees in advance of such meetings.
- Simon Thomson is not a member of the remuneration committee but attends its meetings by invitation. Mr Thomson also attends part of each audit committee meeting by invitation.
- James Smith is not a member of the audit committee but attends its meetings by invitation.
- Dr Mike Watts and Jann Brown stepped down as executive directors on 15 May 2014. The number of meetings they attended are stated up to and including that date.
- Jann Brown was not a member of the audit committee but attended its meetings by invitation prior to stepping down as a director.
- Ian Tyler was appointed a member of the nomination and governance committees on 15 May 2014. The number of meetings he attended is stated from that date.
- Sir Bill Gammell retired as non-executive Chairman on 15 May 2014. The number of meetings he attended is stated up to and including that date.
- Dr James Buckee retired as a non-executive director on 15 May 2014. The number of meetings he attended is stated up to and including that date.

Board committees

The Board has established an audit committee, a remuneration committee, a nomination committee and a governance committee, each of which has formal terms of reference approved by the Board. Copies of the terms of reference are available on the Company’s website.

The terms of reference for each of the Board committees satisfy the requirements of the UK Corporate Governance Code, with the exception of the provision that the Chairman should not be a member of the audit committee. The Board decided in May 2014 that, notwithstanding this provision, it was appropriate for Ian Tyler to remain a member of the audit committee following his appointment as Chairman in order to provide continuity given that Dr James Buckee was retiring from the committee at that time. This has also allowed the committee to continue to benefit from Mr Tyler’s extensive financial experience.

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.

Set out below are reports from each of the Board committees, with the exception of the audit committee report which, in line with best practice, is presented as a separate report (on pages 73 to 75) rather than including this in the corporate governance statement. The remuneration committee section on page 68 covers only the composition and role of the committee, with full details of the Company’s policies on remuneration, service contracts and compensation payments given in the separate Directors’ Remuneration Report on pages 76 to 97, which has been prepared in accordance with the Directors’ Remuneration Reporting Regulations introduced in 2013.



Remuneration Committee Report



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

- **Jackie Sheppard (Chair);**
- Todd Hunt;
- Iain McLaren;
- Ian Tyler; and
- Dr James Buckee (retired as a director and member of the committee on 15 May 2014).

The remuneration committee met six times during 2014. The Chief Executive of the Company 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 forum.

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

Nomination Committee Report



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

- **Ian Tyler (appointed Chair with effect from 15 May 2014);**
- Iain McLaren;
- Todd Hunt;
- Alexander Berger;
- Simon Thomson; and
- Sir Bill Gammell (stepped down as chair and member of the committee on 15 May 2014);

The nomination committee met five times in 2014. The Chairman and three of the Company’s 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.

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

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

One of the main recommendations of the 2013 Board evaluation was to consider the composition of the Board in light of the changes to the Board during the year. The committee has commenced a recruitment process with a view to appointing up to two new non-executive directors during 2015 and has instructed external recruitment consultants Ridgeway Partners to assist with this.

## Diversity

The nomination committee very much takes into account the benefits of diversity on the Board, including gender. As a result of Jann Brown stepping down as an executive director of the Company, the number of women on the Board has reduced from two to one during 2014. The Board does however remain diverse in terms of the range of 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.

Cairn aspires to diversify its Board further as part of its succession planning policy. In seeking to achieve this aspiration the Company will not appoint an individual to the Board unless they are the best candidate for the role, whether male or female.

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

## Succession planning

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

The Board and the nomination committee have regularly discussed and reviewed Board composition and succession planning throughout 2014 and this will continue in 2015 in view of the Board changes which have taken effect during the year and the proposed appointment of up to two new non-executive directors.

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

## Governance Committee Report



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

- **Jackie Sheppard (Chair);**
- Todd Hunt;
- Alexander Berger;
- Ian Tyler (appointed a member of the committee with effect from 15 May 2014);
- James Smith (appointed a member of the committee with effect from 15 May 2014);
- Sir Bill Gammell (stepped down as a member of the committee on 15 May 2014); and
- Jann Brown (stepped down as a member of the committee on 15 May 2014).

The governance committee met four times in 2014 and is comprised of a majority of non-executive directors. In addition, to ensure continuing executive input on governance matters, the CFO was appointed a member of the committee on 15 May 2014.

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. 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.

# Corporate Governance statement continued

## Relations with shareholders (continued)

A list of the Company's major shareholders can be found in the Directors' Report on page 60. Following his appointment as Chairman in May 2014, Ian Tyler held introductory meetings with a number of the Company's major shareholders at which a broad range of matters were discussed.

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

## Annual General Meeting (AGM)

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

It is policy to involve shareholders fully in the affairs of the Company and to give them the opportunity at the AGM to ask questions about the Company's activities and prospects. Details of resolutions to be proposed at the AGM on 14 May 2015 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 DTR 7.2.6 (directors' interests in shares; appointment and replacement of directors; powers of the directors; restrictions on voting rights and rights regarding control of the Company) in the Directors' Report.

## Going concern

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

## Internal control

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

The framework has been in place for the 2014 financial year and up to the date of approval of the annual report and accounts. The Board has carried out a review of the effectiveness of the system of internal controls during 2014 and will ensure that a similar review is performed in 2015. In so doing, the Board took into account the assurance provided by the Chief Executive in respect of the effectiveness of the system of internal control within the Company. The Board is accordingly satisfied that effective controls are in place and that risks have been mitigated to a tolerable level across the Group in 2014.

The Company is subject to a variety of risks which derive from the nature of the oil and gas exploration and production business and some of which relate to the countries in which it conducts its activities (see pages 34 to 41 of this Annual Report and Accounts for more information on risks).

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 2014 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 2014 to the following key controls, business processes and procedures:

- a Standard Operating Manual of core business processes has been developed which outlines "the Cairn way" for executing key processes. The Manual will be rolled out across the Group in Q1 2015;
- the Company's Project Delivery Process was refreshed and rolled out to the business;
- the suite of policies and procedures which form the Group's Corporate Responsibility Management System were developed or refreshed to reflect current best practice or Group policy;
- our Business Continuity Plan has been updated to reflect current business impacts and recovery strategies. A test of the Business Continuity Plan was completed in March 2014 with positive results; and
- an extensive "lessons-learned" project was executed which reviewed our drilling campaigns and identified areas for enhancement which are being implemented in future planning.

The following describes the key elements of the framework and the processes used by the Board during 2014 to review the effectiveness of the system and the approach to be taken in 2015.

## 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 with various partners on both an operated and non-operated basis. Supporting the strategy is a matrix organisation, where the assets are the principal focus, tasked with delivering objectives for their particular asset with functional departments providing support to the assets in delivering their objectives.

Following organisational changes which were implemented during 2014 the executive directors are supported by the new 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 66. 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.

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

The Company's Business Risk Management System (BRMS) defines the processes through which Cairn seeks to systematically identify, analyse, assess, treat and monitor the business risks faced by the Company. The BRMS also identifies the risk management organisational structure through which business risks are managed and regularly reviewed at operating, asset, country and Company levels. The BRMS was updated in 2014 to cover enhancements to the process over the last few years and to reflect organisational changes.

Following the retirement of Jann Brown as Managing Director & CFO in May 2014, James Smith, CFO, took over the role of Chair of the RMC. The RMC currently 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 to manage and facilitate the assessment and treatment of business risks that may affect the Company's ability to deliver its strategy.

The RMC, which met four times during 2014, continues to focus on ensuring the risk framework and strategies embedded in the organisation are fit for purpose. To supplement the role of the RMC, business risks, together with the mitigating measures and responsibilities, are identified and managed at an asset, country, regional and departmental level. Local level risk registers are used to capture, assess, monitor and review risks before principal risks are consolidated into the Company's Group risk register, which is regularly reviewed by the SLT, RMC and MT to ensure that the business understands the key risks it faces and that there is an embedded risk management approach in place across the Company.

Enhancements to our approach to risk management during 2014 included the following:

- the Group Risk Appetite statement was reviewed in light of changes to the business over the last year to ensure it was still aligned with the business strategy. A series of risk tolerance levels across a number of categories were identified and agreed with the Board and senior management.
- the Company's internal auditor facilitated a Board risk identification workshop. The purpose of the workshop was to utilise the collective knowledge of the Board to consider, in line with the strategy going forward, the principal risks to the achievement of the strategy objectives. An analysis against the Group Risk Register was then performed to ensure alignment.

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 2014 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 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. Cairn's internal control and assurance framework document was reviewed by external specialists in 2013 and an updated framework document was finalised and rolled out across the business in Q4 2013.

During 2014, the directors reviewed the effectiveness of the Company's system of financial and non-financial controls, including operational and compliance controls, risk management and high-level internal control arrangements. The Directors derived assurance from the following internal and external controls during 2014:

- 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.



# Corporate Governance statement continued

## Compliance with the UK Corporate Governance Code

Throughout 2014, the Company complied with the provisions of the UK Corporate Governance Code published in 2012, except in the following areas:

Provision of the UK Corporate Governance Code	Company position	Explanation
B.1.1 – the Board should state its reasons if it determines that a director is independent notwithstanding the existence of relationships or circumstances which may appear relevant to its determination, including if the director has served on the Board for more than nine years from the date of their first election.	Todd Hunt has served on the Board for more than nine years since his initial appointment to the Board in May 2003.	The Company accepts that Mr Hunt is not independent in terms of his length of service but the Board is of the view that he is independent in all other respects and has therefore agreed that he should continue as a non-executive director for the time being in order to retain his valuable technical skills and experience. The Company recognises that Mr Hunt continues to sit on certain Board committees and as such the composition of those committees do not fully satisfy the Code provisions in relation to the number of independent non-executive directors on each of those committees.
C.3.1. – In smaller companies the company chairman may be a member of, but not chair, the audit committee in addition to the independent non-executive directors, provided he or she was considered independent on appointment.	The Chairman is a member of, but does not chair, the audit committee.	The Company's recognises that the Code recommends that, except in smaller companies, the Chairman should not be a member of the audit committee. Ian Tyler was not appointed Chairman of the committee until May 2014 and as such the Company complied with this provision prior to the 2014 AGM. Following the 2014 AGM, in view of Dr James Buckee's retirement from the audit committee and Ian Tyler's considerable financial experience, the Company considers it appropriate that Mr Tyler continues to be a member of the audit committee.

## Audit Committee report

### Dear shareholder

*Throughout 2014, our activities continued to focus on the integrity of the financial reporting of the Group and the appropriateness of internal controls. We continue to evolve our activities and our reporting to you in light of guidance from regulators and emerging best practice. In the current year, we have enhanced our reporting on our assessment of the effectiveness of the external audit process.*

During the year under review, I served as Chair of the audit committee alongside three of my fellow non-executive directors, all of whom are considered by the Board to be independent.

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

- Ian Tyler;
- Alexander Berger; and
- Dr James Buckee (retired as a director and member of the committee on 15 May 2014).



### Responsibilities

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

These include:

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

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

### Main activities of the committee during the year

The audit committee met five times in 2014, with meetings arranged around the key external reporting dates. Meetings in January and March focused on the 2013 year-end external audit process (reported in the 2013 Annual Report), in June and August on half-year reporting; and a December meeting on planning for the 2014 year-end cycle and external audit process.

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, approving the annual internal audit plan, tracking the progress of internal audits and reviewing their output and recommendations. Other business covered by the committee includes the approval of corporate assumptions and re-approval of the Group's policy on non-audit services and the Group's Whistleblowing Policy. Subsequent to the year-end a further meeting was held in March 2015 to conclude on the 2014 audit and significant issues.

At our request, the Finance Director and senior members of the Finance Department attended each of these meetings. Other relevant people from the business are also invited to attend certain meetings to give us the necessary insight into their own areas of business, for example in relation to the reporting of oil and gas reserves. In addition, these meetings were attended by both internal and external auditors.

The external auditors receive copies of all relevant audit committee papers and minutes of all audit committee meetings. In addition, I regularly meet with the external audit partner to discuss matters relevant to the Group.

# Audit Committee report continued

## 2014 year-end and significant accounting issues

### Key accounting issue

Recurring issues		Non-recurring issues		
Impairment testing on oil and gas assets – corporate assumptions.	Impairment testing on goodwill – components of Cash Generating Unit (“CGU”) and consistency with asset impairment tests	Cairn India Limited tax issue	Sale of 10% interest in Catcher	Recognition of deferred tax assets

### Background

With the fall in oil prices through Q4 of 2014, the noted that the Group’s exploration and appraisal assets would be tested for impairment.	Goodwill is tested annually for impairment on 31 December, regardless of whether indicators exist or not. Goodwill is tested against the carrying value of assets and liabilities in the North Sea CGU.	Cairn is subject to enquiries regarding certain group reorganisation transactions carried out in 2006, as a result of the retrospective tax legislation introduced in 2012 and is therefore currently restricted from selling its shares in CIL and CIL are restricted from remitting dividends to Cairn, (see page 29).	In September 2014, Cairn announced the sale of a 10% working interest in Catcher. The deal completed in January 2015.	The approval of the Catcher FDP in June confirms the eligibility to certain tax allowances and creates additional UK tax trading losses.
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### Audit Committee action

The audit committee review the group corporate assumption’s proposed by management. The committee discussed and agreed the use of short-term and long-term assumptions and challenged management on the appropriateness of these assumptions. This included a review of the benchmarking exercise that management had performed and the guidance offered by the external auditors.	The inclusion of assets and liabilities in the CGU both in determining the carrying value of the unit and its recoverable amount is closely monitored by the audit committee. Specifically, we challenged management on the inclusion of deferred tax assets and liabilities in the CGU and the consistency of this approach with impairment tests conducted on the individual assets within the CGU.	The audit committee discussed with the Company’s tax and legal advisers and management whether the Company should make any tax provision in relation to the transactions subject to Indian Income Tax Department enquiries. In addition the audit committee discussed with management and the auditors the accounting implications of the restriction (in the context of the IFRS definition of a restriction on sale) to satisfy ourselves that the restriction did not lead to an impairment of the financial asset and related dividend income nor did it require a provision for tax to be recognised in the financial statements.	The sale of our 10% interest in Catcher had several impacts in the financial statements. The valuation of Catcher implied in the sale was used as its fair value for the purposes of impairment test. The audit committee challenged management on the appropriateness of this fair value given changing market conditions. We also considered whether the share of the asset to be sold should be classified as held-for-sale at the Balance Sheet date.	The approval of the FDP triggered the recognition of eligible field allowances and tax losses in the Group’s deferred tax calculations. The audit committee challenged management, ensuring that the deferred tax assets recognised were reflective of their probable future benefit to the Group.
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### Audit Committee conclusions

The audit committee concluded that the use of a short-term oil price assumption based on the forward curve was appropriate. After challenge, the audit committee also determined that the Group’s long-term price assumption should remain unchanged.	After reviewing the impairment tests prepared by management and the assumptions around deferred taxation and after taking account of the views of the Group’s auditors, the audit committee approved management’s proposals on the impairment test CGU.	The Audit Committee agreed with the recommendations of management and the Group’s advisers and the opinion of the auditors that there was no requirement to make a tax provision in respect of the transactions subject to Income Tax Department of India enquiries and the restriction on sale does not lead to an impairment of the asset or a tax provision.	After challenge of both management and auditors we agreed that it was appropriate to base the fair value of Catcher on the sale and were satisfied that the disclosures made in the financial statements were appropriate. Following guidance from our auditors, the 10% interest is not disclosed as held-for-sale.	We were satisfied that after challenging management the increase in the deferred tax asset was reasonable.
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### Further details in Financial Statements

See Section 2.	See section 2.5	See section 3.1	See sections 2.1 and 2.3	See section 4.6
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## Going Concern

At each reporting date management consider the factors relevant to support a statement of going concern (see Corporate Governance section on page 70). The audit committee review and challenge management’s conclusions so that we may, in turn, provide comfort to the Board that management’s assessment has been considered and challenged where appropriate.

Given the ongoing restriction on the sale of the shareholding in Cairn India Limited and the committed levels of expenditure on exploration and development projects, the audit committee carefully reviewed management’s going concern conclusion based on the Group’s latest net cash position and the forecast spend in the period ending 31 March 2016. This confirmed that the Group is fully funded to meet its work programme and firm commitments. The audit committee subsequently recommended to the Board that the Group continues to use the going concern basis in preparing its financial statements.

## 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 decided to comply 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 2014 year-end audit therefore represents the second year of PwC’s tenure as Group auditor.

## Assessment of external audit process

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

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 page 98).	The Committee agreed with the level of materiality set by the auditors.
A review of the Audit Quality Inspection (AQI) Report 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.
A review of the management letter produced by the auditors and the weighting given to points raised indicating the understanding of the auditor of matters of significance to the Group.	The management letter was discussed at the August Audit Committee meeting, with the Committee noting the actions taken by management. The Committee were encouraged by the points that were raised by the Auditors and the wider impact that they have on the business.
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 2014 was presented to the Audit Committee in June 2014 and is summarised in the Independent Auditor's Report on page 98.
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 have been reported to the Audit Committee.

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 presented. The final audit report was presented to the audit committee in March 2015. After thorough discussion the committee agreed with the conclusions that the auditors had reached noting the significant areas of judgement.

## Auditor independence and provision of non-audit services

We have a long established policy in relation to the supply of non-audit services by the external auditors. The Group will engage an external adviser to provide non-audit services on the basis of the skills and experience required for the work, where benefit will be derived as a result of the third party's knowledge of the Group and cost. These advisers may include the Group's external auditors, under a restricted set of circumstances, 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 2014. No changes were made to the existing policy, full details of which can be found on the Group's website.

During the year, PwC provided other services including accounting advice in relation to the tax dispute in India, advice in relation to contracts tax in Republic of Ireland and providing a working capital report on a shareholder circular.

A full breakdown of remuneration paid to the Group's external auditor in respect of both audit and non-audit work is provided in Appendix 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 70), 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 the audit plan.

## Whistleblowing and Related Policies

The Group updated its Whistleblowing Policy during 2012 and the new policy was reviewed by the audit committee and subsequently rolled out across the organisation. The committee is satisfied that arrangements are in place for the proportionate and independent investigation of possible improprieties in respect of financial reporting and other matters and for appropriate follow-up action. The Whistleblowing Policy was reviewed by the committee in December 2014 and re-approved with no changes considered necessary.

The Group has in place a comprehensive Anti-Bribery and Corruption Management System and Code of Business Ethics and training has been provided to all staff in relation to these. As Cairn enters new countries, further monitoring is undertaken and training is continued. Further information regarding these policies can be found on the Group's website.



Iain McLaren

Chair of the Audit Committee  
9 March 2015



# Directors' Remuneration report

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



Dear shareholder

As the Chair of Cairn's remuneration committee (the "remuneration committee" or the "committee"), I am pleased to present our Directors' Remuneration Report for 2014.

Last year was the first time that shareholders were asked to vote separately on both our "Directors' Remuneration Policy" and "Annual Report on Remuneration" and the committee was encouraged by the strong support for both resolutions shown by the Company's members.

The overall executive remuneration framework that was approved at last year's AGM was intended to operate for the remainder of 2014 and the following two financial years. It was subsequently applied throughout 2014 and the committee continues to believe that it remains fit for purpose for 2015. As a consequence, shareholders are not being asked to approve a new Directors' Remuneration Policy at the 2015 AGM. However, for ease of reference the substantive provisions of the approved policy are repeated in Part 2 of this report. Part 3, which contains our Annual Report on Remuneration, then goes on to explain how these provisions were actually applied in 2014 and how they will be operated in 2015. The Annual Report on Remuneration will be subject to an advisory vote at the forthcoming AGM.

### Summary of 2014 business context and key remuneration decisions

The work of the committee in 2014 was conducted against a backdrop of a year in which the Company fulfilled its objective of operating with a focus on safety, building a business with appropriate exposure to material frontier and mature basin exploration whilst maintaining a strong balance sheet with financial flexibility.

Its key decisions relating to remuneration in 2014 are described in more detail in the Annual Report on Remuneration contained on pages 85 to 97 and can be summarised as follows:

- **Base salary increases**  
Each of the individuals that were executive directors of the Company as at 1 January 2014 (being Simon Thomson, Jann Brown and Dr Mike Watts) received an increase to base salary of 2.5% with effect from that date. This was consistent with the level of standard annual salary increase awarded to other employees at that time.
- **Board changes – departure of Jann Brown and Dr Mike Watts**  
On 15 May 2014, Jann Brown, Managing Director & CFO, and Dr Mike Watts, Deputy CEO, stood down as executive directors of the Company. Both individuals agreed to work a portion of their notice periods, principally in order to help seek a resolution of the tax issue in India, and subsequently ceased employment on 17 October 2014. It was agreed that, during the time they remained as employees of the Group following cessation of directorship:
  - a reduction of £75,000 would be applied to both individuals' base salaries; and

- they would continue to participate in the Company's annual bonus scheme, with any awards made for 2014 being pro-rated to the date of leaving employment.

Following the cessation of their employment on 17 October 2014, no additional payments were made to either individual in lieu of the salary (or pension or other benefits) to which they would have been entitled had they worked the remainder of their notice periods.

Finally, the committee concluded that Jann Brown and Dr Mike Watts should both be treated as "good leavers" for the purposes of the Company's Long Term Incentive Plan (or "LTIP") with the result that their outstanding awards under that scheme will continue to vest on their original terms, subject to application of the performance conditions at the end of the normal performance period and a time pro-rating reduction.

Further details of the pay arrangements that have been applied to the above individuals following the cessation of their directorships can be found throughout the Annual Report on Remuneration.

- **Board changes – recruitment of James Smith**

James Smith joined the Company on 3 March 2014 and became CFO on 15 May 2014. His annual base salary was set at £350,000 and the remaining elements of his remuneration package on appointment were consistent with the policy approved by shareholders at the 2014 AGM. As a consequence, during the year he participated in both the existing LTIP and annual bonus scheme (with awards under the latter arrangement being pro-rated by reference to the part of the period that he was employed by the Company).

In connection with his recruitment, and as previously announced on 10 April 2014, James Smith was also granted an award of £200,000 in order to compensate him for bonus forfeited from his previous employment due to his resignation to join Cairn. 50% of this award was paid in cash on commencement of employment with the remaining 50% being delivered in the form of an award of shares that was released after the completion of 12 months' service. The aggregate value of this award made to James Smith was less than the amount of bonus foregone and the deferral period imposed on the share element was comparable to the time horizon applicable to his forfeited entitlements.

Additional information in relation to James Smith's pay arrangements and recruitment "buy-out" award is set out pages 86 and 87 of the Annual Report on Remuneration.

- **Annual bonus**

During the early part of the year, the committee carried out an interim review of the 2014 annual bonus scheme in order to determine whether any variations were required to reflect the exceptional circumstances surrounding the Indian tax issue that had arisen after the original structure had been agreed. The conclusion reached was that the committee should use its discretionary powers under the Company's approved Directors' Remuneration Policy to alter the weightings ascribed to a number of the Group KPIs in order to increase the relative importance of balance sheet strength.

The committee was also required to consider whether the cessation of directorship by Jann Brown and Dr Mike Watts necessitated the making of any variation to the terms of their participation in the bonus scheme over the remainder of the period of their employment with the Company. The committee decided that, in order to better reflect their revised roles, the weightings used to calculate their 2014 bonuses should be amended to 50% Group KPIs and 50% individual

performance, with the latter category being assessed by reference to specific measures relating to the Indian tax issue.

The committee is firmly of the view that the amended weightings described above (full details of which are set out in page 89 of the Annual Report on Remuneration) were entirely necessary in order to ensure that the 2014 KPIs, and therefore management activity, were appropriately aligned with the revised priorities of the business that arose as a result of the occurrence of these unforeseen material events at the beginning of the year. For the avoidance of doubt, the committee is also of the opinion that these in-year variations to the 2014 bonus scheme did not make it less demanding for any individual than when it was originally set.

Based on an assessment of the extent to which the relevant targets were achieved during 2014, and taking into account any pro-rating requirements, payments made under the annual bonus scheme to individuals who served as executive directors during the year (as a percentage of salary paid during the year) were: 78.5% in the case of Simon Thomson; 79.15% for James Smith; and 76.75% for both Jann Brown and Dr Mike Watts. Further details of the way in which these awards were determined are set out on pages 89 to 91 of the Annual Report on Remuneration.

#### – Long Term Incentive Plan (LTIP)

The performance period applicable to the LTIP awards granted in 2011 came to an end during 2014. However, the performance conditions that required to be satisfied in order for these awards to vest were not achieved, with the result that no shares were released to participants and the awards lapsed.

### Applying the policy for 2015

The ways in which the Company's remuneration policy will be applied in 2015 are set out in detail on page 97 in the Annual Report on Remuneration. In particular, salaries for the executive directors in post at the beginning of the year were increased by 1.5% on 1 January 2015 in line with the standard annual increase awarded to other employees in the Group. The Group KPI measures used for the annual bonus scheme (and their respective weightings) have been reformulated for 2015 in order to appropriately reflect the Company's strategic goals for the period. In addition, and in order to ensure consistency with the approach first adopted for the Chief Executive in 2014, the proportion of the CFO's bonus opportunity for the year that will be determined by reference to these Group KPIs has been increased to 100% (from the 90% level that applied in 2014). No material changes have been made to the manner in which the LTIP will operate in 2015, although the members of the Total Shareholder Return international oil and gas comparator group will be slightly changed to take account of delistings and the need to ensure there are sufficient companies.

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

We welcome questions and feedback from all parties on both the content and style of this report and hope that shareholders are supportive of the resolution to approve our Annual Report on Remuneration that is to be proposed at the AGM on 14 May 2015.



**M. Jacqueline Sheppard QC**  
Remuneration Committee Chair  
9 March 2015

## Part 2 – Directors' Remuneration Policy

### Introduction

At the AGM held on 15 May 2014, shareholders overwhelmingly approved a new Directors' Remuneration Policy for the Company. This policy, which specifies the various pay structures operated by the Company 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, became effective immediately on receipt of such approval and was applied by the committee during 2014. This policy will be operative throughout 2015.

Although not required by the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (the "Regulations"), the substantive terms of the above Directors' Remuneration Policy are repeated in this Part 2 for ease of reference. However, any details that were specific to 2014 or earlier years (including, for example, any disclosures relating to named directors and the illustrative remuneration scenarios set out on page 83) have, where applicable, been updated to reflect the current position. The policy as originally approved by shareholders can be found on pages 82 to 89 of the 2013 Annual Report and Accounts, a copy of which is available on the Company's website.

### Purpose and role of the remuneration committee

The remuneration committee determines and agrees with the Board the overall remuneration policy for the executive directors and the Group's PDMRs (Persons Discharging Managerial Responsibilities). Within the terms of this agreed policy, the committee is also responsible for:

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

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

Cairn's remuneration committee operates within written terms of reference agreed by the Board. These are reviewed periodically to ensure that the committee remains up-to-date with best practices appropriate to Cairn, its strategy and the business 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 functions, it takes into account the views and opinions of all the relevant stakeholders in the business. During 2014, Ian Tyler met with a selection of the Company's larger institutional investors following his appointment as Chairman in order to listen to their views on a range of issues relating to the business, including its remuneration structures and practices.

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 including employee engagement surveys.

# Directors' Remuneration report continued

## Part 2 – Directors' Remuneration Policy (continued)

### Overview of current remuneration policy

Cairn's current policy on executive directors' remuneration, which became effective on 15 May 2014 and which is set out below, is to ensure that it appropriately incentivises individuals to achieve the Group's strategic objectives to create, realise and add value for its shareholders, whilst offering a competitive package against the market.

A description of each of the elements 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 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.	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.	Company cars up to a value of £70,000 (or, as an alternative, an annual car allowance of up to £8,771) may be provided. Other benefits will be in line with the market.	None

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



# Directors' Remuneration report continued

## Part 2 – Directors' Remuneration Policy (continued)

### Policy Table – elements of directors' remuneration package (continued)

Remuneration element	Purpose and link to strategy	Operation	Opportunity	Framework for assessing performance
<b>Long Term Incentive Plan (or LTIP)</b>	Incentivises executive directors to deliver superior levels of long-term performance for the benefit of shareholders, thereby aligning the interests of the directors with those of the Company's investors.	Cairn currently operates one LTIP that was approved by shareholders in 2009.	Normal maximum % of salary: 300%.	Vesting of all awards granted under the LTIP to date is determined by comparing the growth in Total Shareholder Return ("TSR") of Cairn over a performance period of three years from grant with the TSR of a comparator group of international oil and gas companies that is selected by the committee prior to each grant, with 20% vesting at median, 100% at upper decile and on a straight line sliding scale in between.  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 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.  Although the committee's intention is that the above condition will be applied to LTIP awards granted in 2015, 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.
		Awards of conditional shares and/or nil-cost options are made annually with vesting dependent on achievement of performance conditions chosen by the committee. Performance is measured over a three-year period.	Exceptional circumstances maximum % of salary: 400%.	
		On vesting of an award, only 50% of the shares to which the holder has become entitled are released/become exercisable immediately, with the remaining 50% normally being released/becoming exercisable after a further period of one year.		
		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.		

Remuneration element	Purpose and link to strategy	Operation	Opportunity	Framework for assessing performance
<b>Share Incentive Plan (or SIP)</b>	Encourages a broad range of employees to become long-term shareholders.	<p>The Company established an HM Revenue and Customs approved share incentive plan in April 2010. It allows the Company to provide eligible employees, including the executive directors, with some or all of the following benefits:</p> <ul style="list-style-type: none"> <li>– partnership shares acquired using deductions from salary;</li> <li>– matching shares awarded to those employees who purchase partnership shares on the basis of a ratio specified by the Company; and</li> <li>– free shares.</li> </ul> <p>Matching and free shares awarded under the SIP must normally be held in the plan for a specified period.</p>	<p>Participation limits are those set by the UK tax authorities from time to time. These limits are currently as follows:</p> <ul style="list-style-type: none"> <li>– Partnership shares: up to £1,800 per tax year can be deducted from salary.</li> <li>– Matching shares: up to two matching shares for every one partnership share purchased.</li> <li>– Free shares: up to £3,600 worth in each tax year.</li> </ul>	None
<b>Pension</b>	Rewards sustained contribution.	<p>The Company operates a defined contribution group personal pension plan in the UK. The scheme is non-contributory and all UK permanent employees, including the executive directors, are eligible to participate.</p> <p>The Company contributes a specified percentage of basic annual salary for senior employees, including executive directors.</p> <p>Where an executive director has an individual personal pension plan (or overseas equivalent), the Company pays its contribution to that arrangement.</p> <p>If an executive director's pension arrangements are fully funded or applicable statutory limits are reached, an amount equal to the Company's contribution (or the balance thereof) is paid in the form of additional salary.</p>	Company contributes 15% of basic salary on behalf of executive directors or pays them an equivalent amount of additional salary.	None

# Directors' Remuneration report continued

## Part 2 – Directors' Remuneration Policy (continued)

### Policy Table – elements of directors' remuneration package (continued)

Remuneration element	Purpose and link to strategy	Operation	Opportunity	Framework for assessing performance
<b>Non-executive directors' fees</b>	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.	Company's Articles of Association place a limit on the aggregate annual level of non-executive directors' and Chairman's fees (currently £900,000).	None
<b>Chairman's fees</b>	Helps recruit and retain the relevant individual.  Reflects time commitment.	The Chairman's fee is considered annually and is determined in light of market practice, the time commitment and responsibilities associated with the role and other relevant factors.	Company's Articles of Association place a limit on the aggregate annual level of non-executive directors' and Chairman's fees (currently £900,000).	None

Notes:

1. A description of how the Company intends to implement the policy set out in this table during the financial year to 31 December 2015 is provided on page 97.

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 LTIP is limited to the executive directors and certain selected senior managers. Other employees are eligible to participate in the Company's share option schemes, details of which are provided on pages 129 and 130.
- Under the Company's defined contribution pension scheme, the Company contribution for less senior employees is 10% of basic annual salary.
- A lower level of maximum annual bonus opportunity applies to employees other than the executive directors and certain PDMRs.
- Benefits offered to other employees generally comprise permanent health insurance, private health insurance, death-in-service benefit and gym and fitness allowance.

In general, these differences arise from the development of remuneration arrangements that are market competitive for the various categories of individuals. They also reflect the fact that, in the case of the executive directors and PDMRs, a greater emphasis is placed on variable pay.

3. The TSR performance conditions applicable to the LTIP (further details of which are provided on page 91) were selected by the remuneration committee on the basis that they improve shareholder alignment and are consistent with the Company's objective of delivering superior levels of long-term value to shareholders. Under the terms of these performance conditions, the committee can specify the basis on which TSR for any company is calculated and has the discretion to make adjustments to this methodology to take account of exceptional circumstances, including share capital variations. Where any company becomes unsuitable as a member of the comparator group as a result of, for example, a change of control or delisting, the committee has the discretion to treat that company in such manner as it deems appropriate (including replacing it with another organisation).

4. Where a nil-cost option award under the LTIP becomes exercisable, it will generally remain so until the tenth anniversary of the date on which it was granted.

5. The choice of the performance metrics applicable to the annual bonus scheme reflect the committee's belief that any incentive compensation should be tied to appropriately challenging measures of both the overall performance of the Company against its strategic KPIs and (where appropriate) those areas of the business that the relevant individual can directly influence.

6. The legislation applicable to the SIP does not allow performance conditions to be applied in relation to partnership or matching shares and, given that the SIP is an "all-employee" arrangement, the Company has decided that it is not appropriate to apply performance conditions to free shares awarded under it.

7. As highlighted on page 95, the Company has a share ownership policy which requires the executive directors to build up and maintain a target holding equal to 100% of base salary. Until such a holding is achieved, an executive director is obliged to retain shares with a value equal to 50% of the net-of-tax gain arising from any vesting or exercise under the Company's share incentive plans. Details of the extent to which the current executive directors had complied with this policy as at 31 December 2014 are set out on page 95.

### Committee discretions

The committee will operate the annual bonus scheme, LTIP and SIP according to their respective rules and the policy described in this Part 2 of the report. The committee, consistent with market practice, retains discretion over a number of areas relating to the operation and administration of these arrangements. These include (but are not limited to) the following:

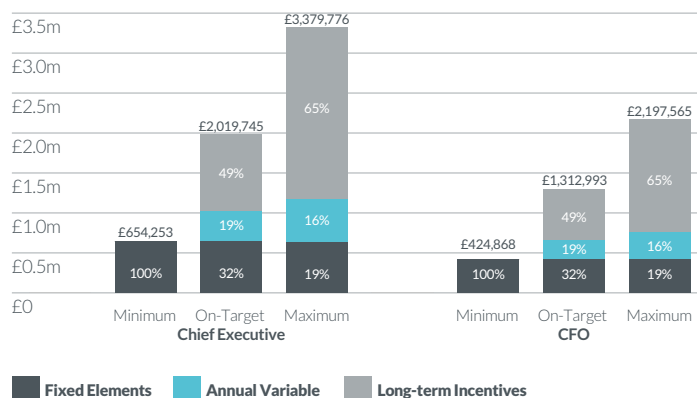
- who participates in the plans;
- the timing of grant of award and/or payment;
- the size of an award and/or a payment;
- discretion relating to the measurement of performance in the event of a change of control or reconstruction;
- the weightings, metrics and targets for the annual bonus plan;
- the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

### Legacy awards

Outstanding share incentive awards that remain unvested/unexercised as detailed on page 93 of the Annual Report on Remuneration remain eligible to vest/be exercised based on their original award terms.

## Remuneration scenarios relating to the above policy

Cairn's pay policy seeks to ensure that the overall package of the executive directors is generally weighted more towards variable pay and, within such variable pay element, that greater emphasis is placed on the delivery of long-term performance through the award of long-term incentives. In the chart below, we show the make-up of remuneration of the current executive directors in 2015 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 2015 irrespective of performance levels, namely base salary (at current rates), benefits (using the annualised details set out in the 2014 single-figure table provided on page 87) and pension (calculated by applying the percentage entitlement set out in the policy table against latest confirmed salary).
- The "on-target" scenario seeks to illustrate the remuneration the executive directors would receive if performance was in line with expectation. In addition to the fixed elements summarised above, it assumes a specified level of payout/vesting under the annual bonus scheme and LTIP. Given that neither of these incentive arrangements explicitly stipulate an "on-target" amount, the assumed levels for this scenario have been calculated by reference to the approximate average annual payouts/vestings for all executive directors over the five years up to and including 2014, being a payout of 70% of salary under the annual bonus scheme and a 60% vesting of LTIP awards originally granted over shares worth 300% of salary.
- The "maximum" columns demonstrate total remuneration levels in circumstances where the variable elements pay out in full (i.e. annual bonus payment of 100% of salary and 133% vesting of LTIP awards originally granted over shares worth 300% of salary).
- For the purposes of valuing the LTIP awards, any post-grant share price movements have been ignored.
- The executive directors are entitled to participate in the SIP on the same basis as other employees. The value that may be received under this arrangement is subject to legislative limits and, for simplicity, has been excluded from the above chart.

## Recruitment policy

### Base salaries

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

### Benefits

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

### Variable pay

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

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

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

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

### Non-executive directors

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



# Directors' Remuneration report continued

## Executive directors' service contracts

The current executive directors' service contracts contain the key terms shown in the table below:

Provision	Detailed terms
Remuneration	<ul style="list-style-type: none"><li>– Salary, pension and benefits.</li><li>– Company car or cash allowance.</li><li>– Permanent health insurance.</li><li>– Private health insurance for director and dependants.</li><li>– Death-in-service benefits.</li><li>– 30 days' paid annual leave.</li><li>– Participation in annual bonus plan, subject to plan rules.</li><li>– Participation in LTIP and SIP, subject to plan rules.</li></ul>
Notice period <sup>1</sup>	– 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.

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

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

On a change of control of the Company resulting in the termination of 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 new CFO, 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.

## Executive director board appointments with other companies

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

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

## Non-executive directors' letters of appointment

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

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

The non-executive directors' letters of appointment are available for inspection, on request, at the Company's registered office.

## 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 2014 and explains how Cairn's approved Directors' Remuneration Policy that is described on pages 77 to 84 was implemented during that period. It also summarises how that policy will be applied in 2015.

In accordance with the Regulations, this part of the report will be subject to an advisory vote at the forthcoming AGM on 14 May 2015.

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 2014

#### Members of the remuneration committee

The members of the remuneration committee during the year (all of whom are independent non-executive directors) were as follows:

- M. Jacqueline Sheppard QC (Chair of the committee);
- Dr James Buckee (retired as a non-executive director and member of the committee on 15 May 2014);
- Todd Hunt;
- Iain McLaren; and
- Ian Tyler.

The non-executive directors who served on the committee had no personal financial interest (other than as shareholders) in the matters decided, no potential conflicts of interest from cross-directorships and no day-to-day involvement in running the business. Biographical information on the committee members is shown on pages 58 and 59 and details of attendance at the committee's meetings during 2014 are shown on page 67.

#### Internal assistance provided to the committee

The Chief Executive is not a member of the remuneration committee but may attend its meetings by invitation and is consulted in respect of certain of its proposals. Similarly, the CFO is not a member of the committee but may occasionally be invited to attend parts of its meetings to address specific matters. Neither the Chief Executive nor the CFO is consulted or involved in any discussions in respect of their own remuneration. During the year, the committee also received material assistance and advice on remuneration policy from the 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 2014	Fees for committee assistance in 2014 <sup>1</sup>	Other services provided to the Company during 2014
<b>New Bridge Street<sup>2</sup></b>	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.	<b>£85,128</b>	None
<b>Slaughter and May</b>	Appointed by the committee to provide advice in relation to executive directors' service contracts and other matters relating to their remuneration arrangements. Also assisted with the preparation of the Directors' Remuneration Report.	<b>£5,790</b>	None
<b>Ernst &amp; Young LLP</b>	Carried out an independent verification of the Company's achievement against performance conditions applicable to the Company's LTIP and share option schemes. However, they provided no advice to the committee.	<b>n/a</b>	Internal auditors of the Company throughout the year.
<b>Shepherd and Wedderburn LLP</b>	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.	<b>£30,715</b>	General legal services to the Group throughout the year.

#### Notes:

1. The bases for charging the fees set out in the above table were agreed by the committee at or around the time the particular services were provided and, in general, reflected the time spent by the adviser in question on the relevant matter.
2. "New Bridge Street" is a trading name of Aon Hewitt Limited, part of Aon plc – they are a member of the Remuneration Consultants Group and their work is governed by the Code of Conduct in relation to executive remuneration consulting in the UK.
3. The committee reviews the performance and independence of all its advisers on an annual basis.

# Directors' Remuneration report continued

## Part 3 – Annual Report on Remuneration (continued)

### Operation of the remuneration committee during 2014 (continued)

#### 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" & "Discretionary"	% of votes cast	Number of votes "Against"	% of votes cast	Total number of votes cast	Number of votes "Withheld" <sup>1</sup>
To approve the 2013 Directors' Remuneration report	15 May 2014	384,329,738	99.30%	2,692,844	0.70%	387,022,582	1,031,354
To approve a 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 took steps, wherever practicable, to understand the concerns of investors who did not support the resolutions.

### Board changes during 2014

#### Leaving arrangements – Dr Mike Watts and Jann Brown

Dr Mike Watts, Deputy CEO, and Jann Brown, Managing Director & CFO, stood down as executive directors on 15 May 2014. Both individuals agreed to work a portion of their 12 month notice period, principally in order to help seek a resolution of the tax issue in India, and subsequently ceased employment on 17 October 2014.

Following their retirement as directors, their annual salaries were reduced by £75,000 to £400,600 (in the case of Dr Mike Watts) and to £362,675 (in the case of Jann Brown). On the subsequent cessation of their employment, no additional payments were made in lieu of the salary (or pension or other benefits) to which these individuals would have been entitled had they worked the remainder of their notice periods.

Both individuals continued to participate in the annual bonus scheme for 2014 and details of their payments for the year under that arrangement (which were pro-rated to the date of cessation of employment) are set out on page 87.

Finally, the committee determined that, for a number of reasons (including the particular circumstances surrounding both individuals' departure and the significant contribution that they had made to the Group over a very considerable period), it was appropriate to treat Dr Mike Watts and Jann Brown as "good leavers" for the purposes of the LTIP. As a result, their outstanding awards did not lapse and will continue to vest at the end of the original performance period but only if, and to the extent that, the applicable performance conditions are satisfied. The number of ordinary shares that vest will also be subject to a time pro-rating reduction to reflect their early cessation of employment.

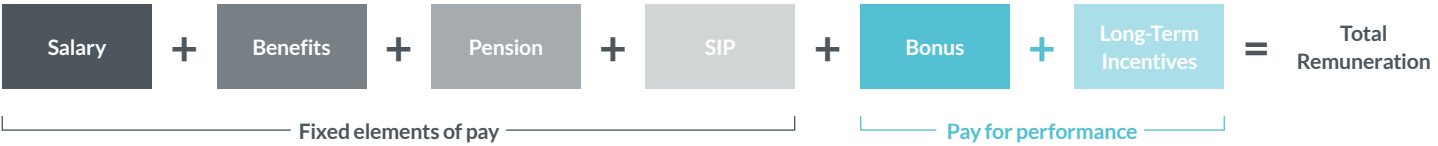
#### Recruitment of James Smith

James Smith, CFO, joined the Company on 3 March 2014 and became an executive director on 15 May 2014. Details of his remuneration package for the year (which is consistent with the policy approved by shareholders at the 2014 AGM) are provided throughout this Annual Report on Remuneration.

As previously announced on 10 April 2014, the committee agreed that, in connection with his recruitment, James Smith would be granted an award of £200,000 in order to compensate him for bonus forfeited from his previous employment due to his resignation to join Cairn. 50% of this award was paid in cash on commencement of employment with the remaining 50% being delivered in the form of an award of shares that was released after 12 months' continuous service with the Group. The aggregate value of this award made to James Smith was less than the amount of bonus foregone and the deferral period imposed on the share element was comparable to the time horizon applicable to his forfeited entitlements.

### Single total figure table for 2014 (audited)

The tables below set out the remuneration received by executive directors and non-executive directors during the year in the following categories.



## Executive directors

	Financial year	Fixed elements of pay						Pay for performance			Total remuneration
		Salary and fees	Benefits <sup>1</sup>	Pension <sup>2</sup>	SIP <sup>3</sup>	Award on recruitment <sup>4</sup>	Fixed element subtotal	Bonus <sup>5</sup>	Long-term incentives <sup>6</sup>	Performance element subtotal	
Current directors											
Simon Thomson	2014	£538,125	£26,126	£80,719	£5,997	–	£650,967	£422,458	–	£422,458	£1,073,425
	2013	£525,000	£22,269	£78,750	£5,996	–	£632,015	£330,750	–	£330,750	£962,765
James Smith <sup>4&amp;8</sup>	2014	£291,667	£21,000	£43,750	£2,998	£200,000	£552,023	£229,969	–	£229,969	£781,992
	2013	–	–	–	–	–	–	–	–	–	–
Former directors											
Jann Brown <sup>7,8&amp;9</sup>	2014	£333,144	£19,279	£47,461	£2,998	–	£402,882	£244,158	–	£244,158	£647,040
	2013	£427,000	£22,688	£64,050	£5,996	–	£519,734	£264,740	–	£264,740	£784,474
Dr Mike Watts <sup>7,8&amp;9</sup>	2014	£349,633	£10,817	£51,982	£2,998	–	£415,430	£267,444	–	£267,444	£682,874
	2013	£464,000	£11,497	£69,600	£5,996	–	£551,093	£285,360	–	£285,360	£836,453

## Notes:

- Taxable benefits available to the executive directors during 2014 were a company car/car allowance, private health insurance, death-in-service benefit, relocation expenses (in the case of James Smith) and, in the case of all of the executive directors who served during the year other than Dr Mike Watts, a gym and fitness allowance. This package of taxable benefits was unchanged from 2013.
- Additional disclosures relating to the pension provision for the executive directors during 2014 are set out on page 89.
- 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 2014 are set out on pages 94 and 95.
- James Smith became an employee of the Company on 3 March 2014 and was appointed as a director with effect from 15 May 2014. His "Award on recruitment" was made up of: a cash award of £100,000 that was paid on the commencement of his employment with the Group; and a conditional award of 55,096 ordinary shares at a price of 181.5 pence per share, both by way of compensation for the loss of bonus from his previous employer. Further information in relation to these matters is provided on page 86.
- This column shows the amount of bonus paid or payable in respect of the year in question after the operation of any applicable time pro-rating reduction. Further information in relation to the annual bonus scheme for 2014 is provided on pages 89 to 91.
- 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 2014 are provided on pages 91 to 94.
- Both Jann Brown and Dr Mike Watts stood down as executive directors on 15 May 2014 but thereafter continued as employees of the Group until 17 October 2014.
- The Regulations only require the above table to show remuneration paid to an individual at a time when he or she is a director of the Company. However, it has been decided that, in order to be as transparent as possible, it should disclose all sums paid to each of James Smith, Jann Brown and Dr Mike Watts during 2014, including those paid at a time when they were employees of the Group but not directors.
- For 2014, the salary figures for Jann Brown and Dr Mike Watts include accrued holiday pay of £16,739 and £3,082 respectively that was paid on termination of employment.
- Following the end of the year to 31 December 2014, 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

	Financial year	Fixed elements of pay				Pay for performance			Total remuneration
		Salary and fees <sup>1</sup>	Benefits	Pension <sup>2</sup>	Fixed element subtotal	Bonus <sup>2</sup>	Long-term incentives <sup>2</sup>	Performance element subtotal	
Current directors									
Ian Tyler <sup>3</sup>	2014	£127,675	–	–	£127,675	–	–	–	£127,675
	2013	£36,277	–	–	£36,277	–	–	–	£36,277
Todd Hunt	2014	£73,800	–	–	£73,800	–	–	–	£73,800
	2013	£72,000	–	–	£72,000	–	–	–	£72,000
Iain McLaren	2014	£83,800	–	–	£83,800	–	–	–	£83,800
	2013	£82,000	–	–	£82,000	–	–	–	£82,000
Alexander Berger	2014	£73,800	–	–	£73,800	–	–	–	£73,800
	2013	£72,000	–	–	£72,000	–	–	–	£72,000
M. Jacqueline Sheppard QC	2014	£83,800	–	–	£83,800	–	–	–	£83,800
	2013	£82,000	–	–	£82,000	–	–	–	£82,000
Former directors									
Sir Bill Gammell <sup>4</sup>	2014	£90,712	–	–	£90,712	–	–	–	£90,712
	2013	£236,000	–	–	£236,000	–	–	–	£236,000
Dr James Buckee <sup>4</sup>	2014	£27,675	–	–	£27,675	–	–	–	£27,675
	2013	£72,000	–	–	£72,000	–	–	–	£72,000

## Notes:

- The annual fee for each of the non-executive directors (other than the Chairman) for 2014 was £73,800. 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.
- 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.
- Ian Tyler, who had previously served as a non-executive director, was appointed Chairman on 15 May 2014. The annual rate of fees payable to him in this new role was £160,000.
- Both Sir Bill Gammell and Dr James Buckee retired as directors on 15 May 2014 and their respective fees for 2014 reflect the period from the start of the year to that date.



# Directors' Remuneration report continued

## Part 3 – Annual Report on Remuneration (continued)

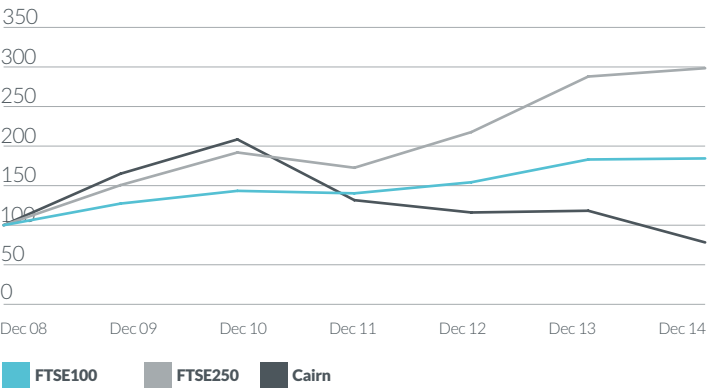
### TSR performance graph and further information on Chief Executive pay

#### Introduction

The following chart demonstrates the growth in value of a £100 investment in the Company and an investment of the same amount in both the FTSE 250 Index and the FTSE 100 Index over the last six years. These comparisons have been chosen on the basis that Cairn was a constituent member of the FTSE 250 Index for the whole of 2014 but has also previously been a constituent member of the FTSE 100 Index.

The table beneath the graph illustrates the movements in the total remuneration of the Company's Chief Executive during the same six-year period.

#### Performance graph – comparison of six-year cumulative TSR on an investment of £100



#### Total remuneration of Chief Executive during the same six-year period

Financial year	Chief Executive	Total remuneration of Chief Executive <sup>1</sup>	Annual variable element award rates for Chief Executive (as % of max. opportunity)	Long term incentive vesting rates for Chief Executive (as % of original award level)
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 <sup>2</sup>	Simon Thomson	£3,405,719	82%	121%
2011	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 87.

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).

#### 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 2014 remuneration package, the percentage change from 2013 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	2.5%	17.3%	27.7%
All Group employees	3.0%	23.0%	27.9%

## Executive directors' base salaries during 2014

Based on a review carried out in December 2013, the following salary increases for executive directors became effective on 1 January 2014:

### 2014 Annual salary details

	Job title	Annual salary as at 31 December 2013	Annual salary as at 1 January 2014 (or on appointment, if later)	% increase with effect from 1 January 2014
<b>Current directors</b>				
Simon Thomson	Chief Executive	£525,000	<b>£538,125</b>	2.5%
James Smith	CFO	n/a	<b>£350,000</b>	n/a
<b>Former directors</b>				
Jann Brown <sup>1</sup>	Managing Director & CFO	£427,000	<b>£437,675</b>	2.5%
Dr Mike Watts <sup>1</sup>	Deputy Chief Executive	£464,000	<b>£475,600</b>	2.5%

Notes:

- Both Jann Brown and Dr Mike Watts stood down as executive directors with effect from 15 May 2014 but subsequently remained as employees of the Group until 17 October 2014. With effect from the date of cessation of directorship, their respective base salaries were reduced by £75,000 from the level noted in the above table.

The increases shown in the above table for each of Simon Thomson, Jann Brown and Dr Mike Watts were consistent with the level of standard annual salary increase awarded to other employees on 1 January 2014.

## Executive directors' pension provision during 2014 (audited)

As highlighted in the Directors' Remuneration Policy described on pages 77 to 84, 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.

On joining the Company, James Smith became a member of the Company scheme and, during the remainder of the year, received a Company contribution of 15% of his basic salary.

Both Simon Thomson and Jann Brown have an individual personal pension plan. During 2014, Jann Brown received a contribution from the Company equal to 15% of her salary for the period that she was employed by the Group. Simon Thomson also received a contribution of 15% of his salary into his personal plan for the first 3 months of the year, at which point the arrangement reached the applicable statutory limit. Thereafter, he received an amount equivalent to 15% of his basic salary for the remaining portion of the year in the form of additional salary.

During the year, Dr Mike Watts received an amount equivalent to 15% of his annual basic salary in the form of additional salary, as his pension arrangements are fully funded.

Details of the actual amounts of pension contributions/additional salary that were paid to current and former executive directors during 2014 are set out in the "pension" column of the single total figure table on page 87.

## Annual bonus – 2014 structure and outcome (audited)

During 2014, 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 2014 was 100% of annual salary (as at date of award).

For all participants, as in prior years, bonus awards were based on individual and/or Company performance measures. Individual performance was measured through the Company's performance management system and Company performance conditions were based on annually defined KPIs.

The following paragraphs highlight, for each individual who served as an executive director during the year, the allocation of their bonus opportunity between Group KPI and individual performance conditions. Taking into account commercial sensitivities around disclosure, a summary of the relevant targets, ascribed weightings and achievement levels is also set out below.

### 2014 annual cash bonus scheme – allocation between Group KPIs and individual performance conditions

	Allocation of maximum bonus opportunity (as % of salary) between:	
	Group KPIs	Individual performance
<b>Current directors</b>		
Simon Thomson	100%	0%
James Smith	90%	10%
<b>Former directors</b>		
Jann Brown <sup>1</sup>	50%	50%
Dr Mike Watts <sup>1</sup>	50%	50%

Notes:

- In connection with the cessation of Jann Brown's and Dr Mike Watts' directorships on 15 May 2014, the committee determined that, in order to better reflect their revised roles in the business going forward, the weightings used to calculate their 2014 bonuses should be amended to 50% Group KPIs and 50% individual performance, with the latter category being assessed by reference to specific measures relating to the Indian tax issue.

# Directors' Remuneration report continued

## Part 3 – Annual Report on Remuneration (continued)

### Annual bonus – 2014 structure and outcome (audited) (continued)

#### 2014 annual cash bonus scheme – Group KPI performance conditions and achievement levels

Measures and weightings			Performance achieved in 2014	
Performance measures	Performance targets	Weighting (as % of allocated proportion of maximum opportunity)	Bonus awarded (as % of allocated proportion of maximum opportunity)	Summary of achievement
Exploration and appraisal success	Discovery of commercial hydrocarbons <sup>2</sup>	35% <sup>3</sup>	35%	Two oil discoveries offshore Senegal with the FAN-1 and SNE-1 exploration wells; target volumes of commercial hydrocarbons exceeded
Active portfolio optimisation	Prospect generation; acquire value accretive nearer term production assets; secure partners in higher cost frontier acreage	15%	3%	Seven new prospects matured out of a target of twelve; unsuccessful in achieving other two targets during 2014
Balance sheet	Retain balance sheet strength; minimum target liquid reserves up to 2017	15% <sup>3</sup>	13.5%	Debt financing concluded; divestment of 10% interest in Catcher to Dyas completed after year end
Licence to operate	Maintain licence to operate by achieving targets for several leading HSE performance indicators	15%	13%	Good performance against almost all the leading targets, both leading and lagging indicators (versus OGP industry standards)
Demonstrate operational excellence	Timely and cost effective delivery of operated and non-operated asset projects; progress development projects on schedule and within budget	20%	14%	Timely delivery of the majority of operated and non-operated asset projects, particularly seismic projects; some delays in exploration drilling due to rig inefficiency and non-productive time; Catcher and Kraken development projects on track
Totals		100%	78.5%	

Notes:

- 1. Further disclosures in relation to the above Group KPIs, including details of the way in which they were measured and assessed, are set out in the 2014 Key Performance Indicators (KPIs) section on pages 18 to 21.
- 2. This KPI was assessed on (i) evidence of commercial discoveries based on 2C resources; plus (ii) the net volumes versus the 50 mmboe target; and (iii) the finding efficiency expressed in US\$/boe.
- 3. As explained in the Annual Statement set out on pages 76 and 77, the committee carried out an interim review in May 2014 of the above annual bonus scheme in order to determine whether any variations were required to reflect the exceptional circumstances surrounding the Indian tax issue that had arisen after the original structure had been agreed. The conclusion reached was that, as provided for by the Directors' Remuneration Policy, the committee should vary the weightings ascribed to the "Exploration and appraisal success" and "Balance sheet" measures, with the former being moved from 45% to 35% and the latter being changed from 5% to 15%.

#### 2014 annual cash bonus scheme – individual performance conditions and achievement levels

With the exception of the Chief Executive, each individual who served as an executive director during the year was given a number of different personal objectives tailored to their role and the needs of the business for the year. In summary, these objectives related to various matters associated with the Indian tax issue and, in the case of James Smith, also included the negotiation of certain debt facilities, a strategic review of funding and identified actions connected to the management of the finance department.

The achievements against the above objectives were carefully considered by the committee following which it awarded each of the relevant individuals between 8.5% and 37.5% of salary, as set out on page 91.

## 2014 annual cash bonus scheme – actual payments awarded

	Award (as % of salary) based on achievement against performance measures relating to:		Bonus actually paid (i.e. after application of any time pro-rating adjustment)
	Group KPIs	Individual performance	
Current directors			
Simon Thomson	78.5%	–	£422,458
James Smith	70.65%	8.5%	£229,969 <sup>1</sup>
Former directors			
Jann Brown	39.25%	37.5%	£244,158 <sup>1</sup>
Dr Mike Watts	39.25%	37.5%	£267,444 <sup>1</sup>

Note:

1. The 2014 bonus awarded to each of these individuals was pro-rated by reference to the proportion of the year that he/she was employed by the Company.

The remuneration committee considered that the above award levels were appropriately reflective of overall performance during the year.

## Long-term incentives during 2014

### Introduction

During the year to 31 December 2014, the executive directors participated in the Company's LTIP, which was originally approved by shareholders at the AGM held on 19 May 2009.

The LTIP enables selected senior individuals to be granted conditional awards or nil-cost options over ordinary shares, the vesting of which is normally dependent on both continued employment with the Group and the extent to which pre-determined performance conditions are met over a specified period of three years.

In the case of all awards under the LTIP (including those granted during 2011, 2012, 2013 and 2014), the performance conditions involve a comparison of the TSR of the Company over a three-year performance period (commencing on the date of grant of the relevant award) with the TSR of a share in each company in a comparator group. At the end of this period, each company in the comparator group is listed in order of TSR performance to produce a "ranking table". The vesting of awards then takes place as follows:

Ranking of Company against the comparator group	Percentage of ordinary shares comprised in award that vest
Below median	0%
Median	20%
Upper decile (i.e. top 10%)	100%
Between median and upper decile	20%–100% on a straight line basis

A list of the companies comprised in the comparator groups applicable to all LTIP awards that were outstanding during 2014 is set out on page 94.

In order to ensure that the LTIP encourages and rewards exceptional performance in terms of delivering increased growth and shareholder value, the performance conditions attaching to awards also provide that, where the TSR of the Company produces a ranking at or above the upper decile level in the appropriate comparator group, a participant will then be given the opportunity to increase the percentage of his/her award that vests through the application of a "multiplier" that is linked to the TSR actually achieved over the performance period. The way in which this multiplier operates is as follows:

Multiplier applied to determine the number of ordinary shares that actually vest	TSR of the Company over the performance period
1	50% or less
1.33	100% or more
1–1.33 on a straight line basis	Between 50% and 100%

However, notwithstanding the performance of the Company against the above targets, no part of any award will vest unless the remuneration committee is satisfied that there has been an overall satisfactory and sustained improvement in the performance of the Company as a whole over the performance period. In addition, and as noted in the Directors' Remuneration Policy, awards granted in 2012 and later years are subject to clawback provisions which may be operated by the committee where, in the period of three years from the end of the applicable performance period, it becomes aware of either a material misstatement of the Company's financial results or an error in the calculation of performance metrics.

On any vesting of an award under the LTIP, only 50% of the ordinary shares to which the holder has become entitled are released/become exercisable immediately, with the remaining 50% normally being released/becoming exercisable after a further period of one year.



# Directors' Remuneration report continued

## Part 3 – Annual Report on Remuneration (continued)

### Long-term incentives during 2014 (continued)

#### LTIP – awards granted during 2014 (audited)

On 19 March 2014, the following awards under the LTIP were granted to directors:

Type of award	Basis of award granted	Share price at date of grant	No. of shares over which award originally granted	% of shares over which award originally granted that vest at threshold	Face value (£,000) of ....		Vesting determined by performance over	
					...shares over which award originally granted <sup>3</sup>	...max. no. of shares to vest if all performance measures met <sup>4</sup>		
Current directors								
Simon Thomson	Nil-cost option	3 x salary of £538,125	£1.682	959,794	20%	£1,614	£2,147	3 years until 18 March 2017
James Smith	Nil-cost option	3 x salary of £350,000	£1.682	624,256	20%	£1,050	£1,396	
Former directors								
Jann Brown <sup>5</sup>	Nil-cost option	3 x salary of £437,675	£1.682	780,633	20%	£1,313	£1,746	3 years until 18 March 2017
Dr Mike Watts <sup>5</sup>	Nil-cost option	3 x salary of £475,600	£1.682	848,275	20%	£1,427	£1,898	

- Notes:
1. Details of the performance conditions applicable to the awards granted in 2014 are provided on page 91.
  2. No price is payable by participants for their shares on the exercise of a nil-cost option granted under the LTIP.
  3. The values shown in this column have been calculated by multiplying the "number of shares over which the award was originally granted" by the "share price at date of grant" (being, for these purposes, the closing mid-market price of a share in the Company on the day immediately preceding the date of its grant).
  4. The values shown in this column have been calculated by multiplying the "number of shares over which the award was originally granted" by 133% (being the vesting percentage that would apply on full satisfaction of all performance conditions to which the awards are subject – see page 91) and multiplying the result by the "share price at date of grant" (being, for these purposes, the closing mid-market price of a share in the Company on the day immediately preceding the date of its grant).
  5. As explained on page 86 of this report, both Jann Brown and Dr Mike Watts have been categorised as "good leavers" for the purposes of the LTIP rules with the result that their awards will continue to vest at the same time and in substantially the same manner (subject to time pro-rating) as those held by all other participants.

#### LTIP – awards vesting during the year (audited)

On 16 June 2014, the three-year performance period applicable to the awards granted under the LTIP on 17 June 2011 to various participants (including the executive directors) came to an end. Thereafter, the remuneration committee assessed the relevant performance conditions. The results of this assessment can be summarised as follows:

Performance measure	% of award subject to measure	Performance achieved 2011–2014	% of award vested
Relative TSR performance against a comparator group of 17 companies with the opportunity for additional multiplier of up to 1.33 to be applied for upper decile performance.	100%	Cairn's TSR over the period ranked below the median company in the comparator group.	0%

- Notes:
1. Further details of the performance conditions that applied to the above awards are set out on page 91.
  2. At various points in the period 17 June 2011 to 16 June 2014, the committee was required to determine the treatment of those comparator group companies that were the subject of takeover transactions. No other discretions were exercised by the remuneration committee during or after the relevant performance period.
  3. The calculations used to inform the committee's determinations in relation to the above awards were independently verified by Ernst & Young LLP.

### LTIP – other awards held by executive directors during the year

For the sake of completeness, and in order to allow comparisons to be made with the awards granted under the LTIP during 2014, set out below are details of the other entitlements under the plan that were held by current and former executive directors during the year:

							Face value (£,000) of ....		
	Date of grant	Type of award <sup>2</sup>	Basis of award granted	Share price at date of grant	No. of shares over which award originally granted	% of shares over which award originally granted that vest at threshold	...shares over which award originally granted <sup>3</sup>	...max. no. of shares to vest if all performance measures met <sup>4</sup>	Vesting determined by performance over three years until...
Current directors									
Simon Thomson	14 June 2012	Nil-cost option	3 x salary of £494,000	£2.887	513,335	20%	£1,482	£1,971	13 June 2015
	20 March 2013	Nil-cost option	3 x salary of £525,000	£2.784	565,732	20%	£1,575	£2,095	19 March 2016
James Smith	–	–	–	–	–	–	–	–	–
Former directors									
Jann Brown <sup>5</sup>	14 June 2012	Nil-cost option	3 x salary of £416,000	£2.887	432,282	20%	£1,248	£1,660	13 June 2015
	20 March 2013	Nil-cost option	3 x salary of £427,000	£2.784	460,129	20%	£1,281	£1,704	19 March 2016
Dr Mike Watts <sup>5</sup>	14 June 2012	Nil-cost option	3 x salary of £452,000	£2.887	469,691	20%	£1,356	£1,803	13 June 2015
	20 March 2013	Nil-cost option	3 x salary of £464,000	£2.784	500,000	20%	£1,392	£1,851	19 March 2016

#### Notes:

- Further details of the performance conditions that apply to these awards are set out on page 91.
- The awards shown in the above table that were granted in 2012 were originally made in the form of conditional shares. However, to provide flexibility to participants, they have been converted into nil-cost options.
- The values shown in this column have been calculated by multiplying the relevant "number of shares over which the award was originally granted" by the appropriate "share price at date of grant" (being, for these purposes, the closing mid-market price of a share in the Company on the day immediately preceding the date of its grant).
- The values shown in this column have been calculated by multiplying the relevant "number of shares over which the award was originally granted" by 133% (being the vesting percentage that would apply on full satisfaction of all performance conditions to which the awards are subject – see page 91) and multiplying the result by the appropriate "share price at date of grant" (being, for these purposes, the closing mid-market price of a share in the Company on the day immediately preceding the date of its grant).
- As explained on page 86 of this report, both Jann Brown and Dr Mike Watts have been categorised as "good leavers" for the purposes of the LTIP rules with the result that their awards will continue to vest at the same time and in substantially the same manner (subject to time pro-rating) as those held by all other participants.

# Directors' Remuneration report continued

## Part 3 – Annual Report on Remuneration (continued)

### Long-term incentives during 2014 (continued)

#### Comparator group companies applicable to LTIP awards

The table below provides details of the comparator groups applicable to each tranche of awards granted under the LTIP that were outstanding during 2014.

Company	Comparator group applicable to LTIP awards granted on...			
	17 June 2011	14 June 2012	20 March 2013	19 March 2014
Afren PLC	✓	✓	✓	✓
BG Group PLC	✓	✓	✓	✓
Bharat Petroleum Corporation Limited	✓			
DNO ASA	✓	✓	✓	✓
EnQuest PLC	✓	✓	✓	✓
EOG Resources, Inc	✓			
Faroe Petroleum PLC		✓	✓	✓
Genel Energy PLC		✓	✓	✓
JKX Oil & Gas PLC	✓	✓	✓	✓
Lundin Petroleum AB		✓	✓	✓
Melrose Resources PLC*	✓			
Newfield Exploration Company	✓			
Niko Resources Limited		✓	✓	✓
Noble Energy, Inc	✓			
Oil and Natural Gas Corporation Limited	✓			
Ophir Energy PLC		✓	✓	✓
Petroceltic International PLC		✓	✓	✓
Premier Oil PLC	✓	✓	✓	✓
Rockhopper Exploration PLC		✓	✓	✓
Salamander Energy PLC	✓	✓	✓	✓
Santos Limited	✓	✓	✓	✓
SOCO International PLC		✓	✓	✓
Talisman Energy, Inc	✓	✓	✓	✓
Tullow Oil PLC	✓	✓	✓	✓
Woodside Petroleum Limited	✓			

\* Denotes company that has delisted during the applicable performance period.

### Participation of executive directors in all-employee share schemes during 2014

#### 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 2014/2015, the Company awarded two matching shares for every one partnership share purchased and intends to continue using this award ratio for the tax year 2015/2016.
- “Free shares” – employees can be given up to £3,600 worth of ordinary shares free in each tax year. On 8 April 2014, an award of free shares was made to employees, including to a number of 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 2014

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 2014	Free shares awarded on 8 April 2014 at a price of £1.676 per share	Partnership shares awarded on...		Matching shares awarded on...		Total SIP shares held at 31 December 2014 (or date of cessation of employment, if earlier)
			...6 May 2014 at a price of £1.851 per share	...5 December 2014 at a price of £1.673 per share	...6 May 2014 at a price of £1.851 per share	...5 December 2014 at a price of £1.673 per share	
<b>Current directors</b>							
Simon Thomson	6,761	1,789	810	–	1,620	–	10,980
James Smith	–	– <sup>1</sup>	–	896	–	1,792	2,688
<b>Former directors</b>							
Jann Brown	6,761	1,789	–	–	–	–	8,550
Dr Mike Watts	6,761	1,789	–	–	–	–	8,550

Notes:

- Although James Smith was an employee of the Company on the date these free shares were awarded, he had not by that time satisfied the qualifying employment requirements for SIP participation.

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 60.

### Shareholding guidelines for directors (audited)

The committee believes that a significant level of shareholding by the executive directors strengthens the alignment of their interests with those of shareholders. Accordingly, a formal share ownership policy is in place under which the executive directors are required to build up and maintain a target holding equal to 100% of base salary. The policy also provides that, until such a holding is achieved, an executive director is obliged to retain shares with a value equal to 50% of the net-of-tax gain arising from any vesting or exercise under the Company's share incentive plans.

The following table discloses the beneficial interest of each director in the ordinary shares of the Company as at 31 December 2014 (or date of cessation of directorship, if earlier). 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.

	Ordinary shares	Ordinary shares held in the SIP <sup>2</sup>	Total holding of ordinary shares	Value of holding as a % of salary on 1 January 2015 <sup>3</sup>	Ordinary shares subject to outstanding unvested awards under the LTIP <sup>4</sup>	Ordinary shares subject to other unvested awards <sup>5</sup>	Total interest in ordinary shares
<b>Executive directors</b>							
Simon Thomson	446,587	10,980	457,567	141%	2,038,861	–	2,496,428
James Smith	0	2,688	2,688	1%	624,256	55,096	682,040
<b>Non-executive directors</b>							
Ian Tyler	0	–	0	–	–	–	0
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
<b>Former directors</b>							
Sir Bill Gammell	656,131	–	656,131	–	–	–	656,131
Dr James Buckee	37,788	–	37,788	–	–	–	37,788
Jann Brown	305,279	8,550	313,829	–	1,673,044	–	1,986,873
Dr Mike Watts	1,224,136	8,550	1,232,686	–	1,817,966	–	3,050,652
	<b>2,796,819</b>	<b>30,768</b>	<b>2,827,587</b>		<b>6,154,127</b>	<b>55,096</b>	<b>9,036,810</b>

Notes:

- Details of the Company's share ownership policy for executive directors are set out above.
- 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.
- Share price used is the average share price over the period of 90 days ending on 1 January 2015.
- This column shows all unvested and outstanding awards under the LTIP that were held by the director concerned as at 31 December 2014 (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 91.
- As explained on page 86, in connection with his recruitment, James Smith was granted a conditional award of 55,096 ordinary shares, the vesting of which was subject to continued employment until the first anniversary of the date he joined the Group. This condition was satisfied on 3 March 2015 and the relevant shares were released to him shortly thereafter.



# Directors' Remuneration report continued

## Part 3 – Annual Report on Remuneration (continued)

### Dilution of share capital pursuant to share plans during 2014

In any ten-year rolling period, the number of ordinary shares which may be issued in connection with the Company's discretionary share plans cannot exceed 5% of the Company's issued ordinary share capital.

In addition, in any ten-year rolling period, the number of ordinary shares which may be issued in connection with all of the Company's employee share schemes (whether discretionary or otherwise) cannot exceed 10% of the Company's issued ordinary share capital.

For the purposes of operating both the above limits, the number of shares issued prior to 6 February 2012 in connection with options and awards is adjusted to reflect the share capital consolidation which became effective on that date.

It should also be noted that all shares acquired by or awarded to participants under the SIP are existing ordinary shares purchased in the market. As a result, the SIP does not involve the issue of new shares or the transfer of treasury shares.

### Board appointments with other companies during 2014

Certain of the Company's current executive directors serve as non-executive directors on the boards of other companies and are permitted to retain any associated fees. Details of the positions held during 2014 and the fees that were payable are as follows:

Position held		Fees received for the year to 31 December 2014 (or date of cessation of employment with the Group, if earlier)
<b>Current directors</b>		
Simon Thomson	Non-executive director, Graham's The Family Dairy Limited	<b>£35,000</b>

### 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 2013 and 2014.

	Financial Year 2013	Financial Year 2014	% change
Employee costs (US\$m)	41.5	<b>51.3</b>	23.6%
Distributions (US\$m) <sup>1</sup>	36.6	<b>64.3</b>	75.7%

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 2015

The following table provides details of how the Company intends to implement the key elements of the Directors' Remuneration Policy described on pages 77 to 84 during the year to 31 December 2015.

Remuneration element	Implementation during 2015
<b>Base salary</b>	Both of the executive directors received a 1.5% increase in base salary on 1 January 2015 – 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 2015 are as follows: <ul style="list-style-type: none"> <li>– Simon Thomson, Chief Executive – £546,197; and</li> <li>– James Smith, CFO – £355,250.</li> </ul>
<b>Benefits</b>	Executive directors will continue to receive the same benefits as in 2014.
<b>Annual bonus</b>	<p>In accordance with the requirements of the policy, executive directors will be eligible to receive a bonus of up to 100% of base salary depending on the extent to which specified measures are satisfied over the year.</p> <p>All of the Chief Executive's and CFO's 2015 bonus opportunity will be based on the demanding Group KPIs described below (with details of the weightings specified in brackets):</p> <ul style="list-style-type: none"> <li>– exploration and appraisal success (25%);</li> <li>– active portfolio optimisation (25%);</li> <li>– retain balance sheet strength (20%);</li> <li>– maintain licence to operate (15%); and</li> <li>– operational excellence (15%).</li> </ul> <p>The specific targets to be used for the purposes of the 2015 bonus scheme are commercially sensitive and have not, therefore, been set out in detail above. However, appropriate disclosures in relation to the 2015 bonus scheme will be included in next year's Annual Report on Remuneration.</p>
<b>LTIP</b>	It is intended that, during 2015, the executive directors will be granted LTIP awards over shares worth 300% of salary (being the same level as was awarded in 2014). The performance conditions that will determine the vesting of these grants will be those that applied to last year's awards (full details of which are set out on page 91 of the Annual Report on Remuneration) except that the Total Shareholder Return comparator group will exclude Talisman Energy Inc, Salamander Energy PLC, JKX Oil & Gas PLC and Niko Resources Limited and include Kosmos Energy Limited, Nostrum Oil & Gas PLC, Dragon Oil PLC and Det Norske Oljeselskap ASA.
<b>SIP</b>	Executive directors will be given the opportunity to participate in the SIP on the same terms as apply to all other eligible employees in the arrangement.
<b>Pension</b>	The Company will continue to contribute 15% of basic salary on behalf of executive directors or pay them an equivalent amount of additional salary.
<b>Non-executive directors' fees</b>	The annual non-executive director fee for 2015 has been increased from £73,800 to £74,900. The additional annual fee for chairing the audit and/or remuneration committees is unchanged at £10,000.
<b>Chairman's fees</b>	The annual Chairman's fee for 2015 has been retained at £160,000.

By order of the Board

**M. Jacqueline Sheppard QC**

Chair of the remuneration committee

9 March 2015

# 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 parent company financial statements (the "financial statements") give a true and fair view of the state of the group's and of the parent company's affairs as at 31 December 2014 and of the group's loss and the group's and the parent company's cash flows for the year then ended;
- the group financial statements have been properly prepared in accordance with International Financial Reporting Standards ("IFRSs") as adopted by the European Union;
- the parent company financial statements have been properly prepared in accordance with International Financial Reporting Standards ("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

Cairn Energy PLC's financial statements comprise:

- the Group Balance Sheet and the Company Balance Sheet as at 31 December 2014;
- the Group Income Statement and the Group Statement of Comprehensive Income for the year then ended;
- the Group Statement of Cash Flows and the Company Statement of Cash Flows for the year then ended;
- the Group Statement of Changes in Equity and the Company 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.

The financial reporting framework that has been applied in the preparation of the financial statements is applicable law and IFRSs as adopted by the European Union and, as regards the parent company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

### Our audit approach

The context for our audit is set by Cairn Energy PLC's ("Cairn") major activities in 2014, together with the significant fall in world oil prices in Quarter 4. In the year, Cairn has progressed to development stage their interest in the Catcher North Sea field; raised finance for this and the other development project, Kraken; and completed a 4 well exploration drilling programme offshore North West Africa, which resulted in oil discoveries on 2 wells offshore Senegal. Away from core operations, Cairn's main focus has been dealing with enquiries from the Indian Tax Authorities relating to a group reconstruction undertaken prior to the IPO of Cairn India in 2007, which has also resulted in a restriction on the ability to sell the remaining 10% holding in Cairn India.



### Overview

- Overall group materiality was \$30.2m which represents 1% of group total assets.
- Group audit scoping was performed based on total assets held within each of the 63 individual components in the group and addressed over 94% of group total assets.
- Impairment of exploration/development assets and goodwill.
- Impact of tax enquiry in relation to Cairn India Limited on tax provisions.
- Going concern.
- Other tax judgements.

### Materiality

The scope of our audit is 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 and to evaluate the effect of misstatements, both individually and on the financial statements as a whole.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

Overall group materiality	\$30.2m (2013: \$36.0m).
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 \$1.5m (2013: \$1.8m) as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

### 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 accounting processes and controls, and the industry in which the group operates.

For operating purposes, the group is structured around 3 key segments: Atlantic Margin (North Atlantic & North West Africa), the Mediterranean and North West Europe. During 2014, North West Europe has seen the most significant development activity, with the main exploration activity being undertaken in North West Africa.

For accounting purposes, the group is structured into 63 reporting units or components. Our group scoping was based on total assets, consistent with our approach to materiality, and identified 10 components which required an audit of their complete financial information. A further 7 components were subject to specified procedures at a financial statement line item (FSLI) level to obtain sufficient coverage. The majority of the finance function is in Edinburgh, other than North West Europe which is primarily accounted for in Norway. Our PwC Norway audit team performed the audit work on the North West Europe components and all other audit work was performed by our UK audit team. The UK team attended audit planning and clearance meetings in Norway, as well as being directly involved in the scoping and review of the work performed by PwC Norway.

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	How our audit addressed the area of focus
<b>Risk of impairment of exploration/development assets and goodwill</b>	
Exploration assets of \$417.0m relate to costs incurred where there is expected future activity but no approved development plan. Development assets of \$467.8m reflect spend to date on Catcher and Kraken. Both of these asset categories only require an impairment review if an impairment trigger is identified.	We tested management’s impairment review of goodwill, capitalised exploration and capitalised development costs.  We reviewed management’s assessment of impairment triggers and did not identify any further triggers which had not been considered by management.
The goodwill balance of \$145.1m arose on the acquisitions of Agora and Nautical in 2012. As required by IAS 36, an annual impairment review is performed on this balance.	Specific work that we performed over the impairment review included:
Due to the nature of Cairn’s industry, indicators of impairment include: <ul style="list-style-type: none"><li>– unsuccessful exploration such as experienced in Fom Draa, Juby Maritime and Skarfjell during the year;</li><li>– the recent significant decrease seen in global oil prices;</li><li>– changes to exploration plans;</li><li>– changes to reserves estimates; and</li><li>– consolidated net assets being more than \$1.5bn greater than the market capitalisation of the group.</li></ul>	<ul style="list-style-type: none"><li>– comparing the assumptions used within the impairment review model to approved budgets and business plans and other evidence of future intentions for individual exploration properties, which we found to be consistent;</li><li>– comparing reserves and production profiles and matching capital and operating expenditure forecasts to group approved values or operator estimates, which we found to be consistent;</li><li>– benchmarking of key assumptions including commodity price and discount rate and inflation against our own internal data which we found to be in line;</li><li>– performing 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. We calculated the degree to which the long-term oil price assumption would need to reduce further before an impairment arises on these assets and considered the likelihood of this arising in isolation from other changes in assumptions; and</li><li>– challenged management on the inclusion of all appropriate assets and liabilities in the cash-generating units 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 all relevant balances had been included.</li></ul>
When an impairment review is triggered, within the impairment review calculations there are significant judgements in relation to assumptions such as: <ul style="list-style-type: none"><li>– long-term oil price ;</li><li>– reserve estimates;</li><li>– production profiles;</li><li>– cost profiles and escalation applied; and</li><li>– discount rates.</li></ul>	
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 whether there are any impairment triggers or impairments.	None of the items noted above resulted in a change to the impairment charge recorded by management
Refer to Notes 2.1, 2.2 and 2.4 to the financial statements.	



# Independent auditors’ report to the members of Cairn Energy PLC continued

Area of focus	How our audit addressed the area of focus
<b>Potential impact on tax provisions of tax enquiry in relation to Cairn India Limited</b>	
<p>We focused on this area because 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.</p> <p>Although there have been developments over the course of 2014, no conclusion has been reached by the Indian tax authorities in relation to this enquiry and therefore 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.</p> <p>Refer to Note 6.2 to the financial statements.</p>	<p>In assessing the potential impact of the request for information by the Indian tax authorities we:</p> <ul style="list-style-type: none"><li>– read the correspondence received by the Group from the Indian tax authorities;</li><li>– understood the group reconstruction under review, and the potential basis for any claim, including the relevant legislation and other precedent;</li><li>– discussed with management the advice and action they had taken with regards to the enquiry and reviewed any associated documents;</li><li>– discussed certain aspects of the matter directly with the group's legal advisers; and</li><li>– sought advice from our own tax experts.</li></ul> <p>We concluded that the position adopted in the financial statements was reasonable based on the work we performed, in particular:</p> <ul style="list-style-type: none"><li>– management's view that no provision for tax should be made at this time;</li><li>– the adequacy of the disclosure in the Annual Report; and</li><li>– the impact of the restriction on sale of Cairn India shares on the future funding requirements for the Group.</li></ul> <p>We also considered whether this ongoing enquiry would have any impact on the carrying value of the investment in Cairn India Limited of \$702.6m. 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.</p>
<b>Going concern</b>	
<p>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.</p> <p>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.</p> <p>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.</p> <p>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 exploration and appraisal wells in North West Europe and North West Africa over the next 12-18 months which will be funded from existing cash resources.</p>	<p>In assessing the appropriateness of the going concern assumption used in preparing the financial statements, we:</p> <ul style="list-style-type: none"><li>– reviewed the cash flow requirements of the Group over the next 18 months based on budgets and forecasts;</li><li>– understood what forecast expenditure is committed and what could be considered discretionary;</li><li>– considered the liquidity of existing assets on the balance sheet, including the Cairn India investment;</li><li>– reviewed the terms associated with the debt agreement and the amount of the facility available for drawdown; and</li><li>– considered potential downside/upside scenarios and the resultant impact on available funds</li></ul> <p>Our conclusion on going concern is below.</p>
<b>Other tax judgements</b>	
<p>We focused on this area because Cairn operates in a complex tax environment comprising a number of jurisdictions with specific tax rules relating to oil and gas activities. The rules which have the most significant impact on the results are in relation to North Sea field allowances and UK reinvestment relief. As a result, management have to make significant judgements regarding current and deferred tax positions.</p> <p>Refer to Note 4.6 to the financial statements.</p>	<p>Our assessment of the tax judgements was made on the basis of:</p> <ul style="list-style-type: none"><li>– our tax knowledge from similar circumstances and past experience;</li><li>– our understanding of the Group and the relevant transactions;</li><li>– reviewing correspondence with tax authorities and/or evidence from similar precedent; and</li><li>– our professional judgement.</li></ul> <p>Specifically, in relation to corporate and deferred tax positions we:</p> <ul style="list-style-type: none"><li>– considered the information available in relation to the Group's open tax positions and assessed the associated level of provisioning. We found that management had appropriately included the relevant information and calculated the provision accordingly;</li><li>– assessed management's consideration of the impact of the Group's future plans and current legislation specifically related to oil and gas on the recognition of deferred tax and found it to be reasonable. In particular, we assessed the treatment of field allowances relating to Catcher and Kraken awarded at the time of Field Development Plan approval and found it to be in line with industry practice; and</li><li>– we assessed the basis on which deferred tax assets recognised are expected to be recovered and agreed with management's assessment.</li></ul>

Going concern

Under the Listing Rules we are required to review the directors’ statement, set out on page 70, in relation to going concern. We have nothing to report having performed our review.

As noted in the directors’ statement, the directors have concluded that it is appropriate to prepare the financial statements using the going concern basis of accounting. The going concern basis presumes that the group and parent company have adequate resources to remain in operation, and that the directors intend they will 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 parent company’s ability to continue as a going concern.

Other required reporting

Consistency of other information

Companies Act 2006 opinions

In our opinion:

- the information given in the Strategic report and the Directors’ report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the information given in the Corporate Governance statement set out on pages 63 to 72 with respect to internal control and risk management systems and about share capital structures is consistent with the financial statements.

ISAs (UK & Ireland) reporting

Under ISAs (UK & Ireland) we are required to report to you if, in our opinion:

<div><div>- Information in the Annual Report is:<ul style="list-style-type: none"><li>- materially inconsistent with the information in the audited financial statements; or</li><li>- apparently materially incorrect based on, or materially inconsistent with, our knowledge of the group and parent company acquired in the course of performing our audit; or</li><li>- otherwise misleading.</li></ul></div></div>	We have no exceptions to report arising from this responsibility.
<div><div>- the statement given by the directors on page 72, 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 parent company’s performance, business model and strategy is materially inconsistent with our knowledge of the group and parent company acquired in the course of performing our audit.</div></div>	We have no exceptions to report arising from this responsibility.
<div><div>- the section of the Annual Report on page 73, 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.</div></div>	We have no exceptions to report arising from this responsibility.

Adequacy of accounting records and information and explanations received

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements and the part of the Directors’ Remuneration Report to be audited are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

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 Companies Act 2006 we are required to report to you if, in our opinion, a corporate governance statement has not been prepared by the parent company. We have no exceptions to report arising from this responsibility.

Under the Listing Rules we are required to review the part of the Corporate Governance Statement relating to the parent company’s compliance with 10 provisions of the UK Corporate Governance Code. We have nothing to report having performed our review.

# Independent auditors' report to the members of Cairn Energy PLC continued

## 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 62, 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 parent company's circumstances and have been consistently applied and adequately disclosed;
- the reasonableness of significant accounting estimates made by the directors; and
- the overall presentation of the financial statements.

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 and Accounts (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.



### Michael Timar (Senior Statutory Auditor)

for and on behalf of PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
Glasgow  
9 March 2015

- (a) 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.
- (b) Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

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# Group Income Statement

## For the year ended 31 December 2014

	Section	2014 US\$m	2013 US\$m
<b>Continuing operations</b>			
Pre-award costs	4.2	(54.8)	(23.5)
Unsuccessful exploration costs	2.1	(208.4)	(213.1)
Net operating expenses	4.3	(64.5)	(42.2)
Impairment of intangible exploration/appraisal assets	2.1	(46.9)	(251.4)
Gain/(loss) on disposal of oil and gas assets	2.2	2.3	(24.7)
Impairment of goodwill	2.4	-	(324.2)
<b>Operating loss</b>		<b>(372.3)</b>	(879.1)
Gain on disposal of available-for-sale financial assets	3.1	3.9	-
Impairment of available-for-sale financial assets	3.1	(194.3)	(267.5)
Finance income	4.4	38.3	50.6
Finance costs	4.5	(34.7)	(2.9)
<b>Loss before taxation from continuing operations</b>		<b>(559.1)</b>	(1,098.9)
<b>Taxation</b>			
Tax credit	4.6a	178.0	543.0
<b>Loss for the year attributable to equity holders of the parent</b>		<b>(381.1)</b>	(555.9)
<b>Loss per ordinary share – basic (cents)</b>	4.7	<b>(66.51)</b>	(93.24)
<b>Loss per ordinary share – diluted (cents)</b>	4.7	<b>(66.51)</b>	(93.24)

# Group Statement of Comprehensive Income

## For the year ended 31 December 2014

	Section	2014 US\$m	2013 US\$m
<b>Loss for the year</b>		<b>(381.1)</b>	(555.9)
<b>Other comprehensive income – items that may be recycled to profit or loss</b>			
Deficit on valuation of financial assets	3.1	(261.1)	(110.8)
Deferred tax credit on valuation of financial assets	4.6a	56.6	48.8
Valuation movement recycled to Income Statement	3.1	189.2	267.5
Deferred tax charge on valuation movement recycled to Income Statement	4.6a	(40.9)	(74.5)
Currency translation differences		(58.8)	7.6
<b>Other comprehensive income for the year</b>		<b>(115.0)</b>	138.6
<b>Total comprehensive income for the year attributable to equity holders of the parent</b>		<b>(496.1)</b>	(417.3)



# Group Balance Sheet

## As at 31 December 2014

	Section	2014 US\$m	2013 US\$m
<b>Non-current assets</b>			
Intangible exploration/appraisal assets	2.1	417.0	498.6
Property, plant & equipment – development/producing assets	2.2	467.8	299.9
Intangible assets – goodwill	2.4	145.1	163.4
Other property, plant & equipment and intangible assets		5.5	6.0
Available-for-sale financial assets	3.1	702.6	1,027.6
Deferred tax assets	4.6c	106.2	58.7
		<b>1,844.2</b>	<b>2,054.2</b>
<b>Current assets</b>			
Income tax asset	3.3	60.3	81.3
Inventory		5.0	10.0
Other receivables	3.4	238.6	152.3
Cash and cash equivalents	3.2	869.3	1,308.3
		<b>1,173.2</b>	<b>1,551.9</b>
<b>Total assets</b>		<b>3,017.4</b>	<b>3,606.1</b>
<b>Current liabilities</b>			
Trade and other payables	3.5	278.2	201.0
Provisions		11.6	11.4
Loans and borrowings	3.2	–	55.3
		<b>289.8</b>	<b>267.7</b>
<b>Non-current liabilities</b>			
Deferred tax liabilities	4.6c	61.7	148.0
Provisions		2.8	2.6
		<b>64.5</b>	<b>150.6</b>
<b>Total liabilities</b>		<b>354.3</b>	<b>418.3</b>
<b>Net assets</b>		<b>2,663.1</b>	<b>3,187.8</b>
<b>Equity attributable to equity holders of the parent</b>			
Called-up share capital	5.1	12.4	12.8
Share premium	5.1	487.0	486.9
Shares held by ESOP/SIP Trusts	5.1	(26.7)	(28.0)
Foreign currency translation	5.1	(82.7)	(23.9)
Capital reserves – non-distributable	5.1	40.8	40.4
Merger reserve	5.1	255.9	255.9
Available-for-sale reserve	5.1	–	56.2
Retained earnings		1,976.4	2,387.5
<b>Total equity</b>		<b>2,663.1</b>	<b>3,187.8</b>

The financial statements on pages 104 to 142 were approved by the Board of Directors on 9 March 2015 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 2014

	Section	2014 US\$m	2013 US\$m
<b>Cash flows from operating activities</b>			
Loss before taxation		(559.1)	(1,098.9)
Unsuccessful exploration costs		208.4	213.1
Depreciation and amortisation		3.3	4.5
Share-based payments charge		21.4	14.0
Impairment of intangible exploration/appraisal assets		46.9	251.4
(Gain)/loss on sale of oil and gas assets		(2.3)	24.7
Gain on disposal of available-for-sale financial assets		(3.9)	–
Inventory disposal/write down		8.4	–
Impairment of goodwill		–	324.2
Impairment of available-for-sale financial assets		194.3	267.5
Finance income		(38.3)	(50.6)
Finance costs		34.7	2.9
Interest paid		(0.5)	(2.9)
Income tax received		66.0	59.9
Foreign exchange differences		8.8	1.3
Other receivables movement		4.3	(6.4)
Trade and other payables movement		(4.6)	34.5
Provisions movement		2.9	–
<b>Net cash (used in)/from operating activities</b>		<b>(9.3)</b>	<b>39.2</b>
<b>Cash flows from investing activities</b>			
Expenditure on intangible exploration/appraisal assets		(336.0)	(386.6)
Expenditure on property, plant & equipment – development/producing assets		(39.8)	(31.4)
Proceeds on disposal of intangible exploration/appraisal assets		31.4	7.1
Proceeds on disposal of property, plant & equipment – development/producing assets		–	72.7
Purchase of inventory		(4.5)	(10.3)
Proceeds from disposal of inventory		0.6	–
Purchase of other property, plant & equipment and intangible assets		(3.2)	(4.4)
Proceeds from disposal of available-for-sale financial assets		62.6	–
Movement in funds on bank deposits		0.2	2.0
Dividend received		–	40.5
Interest received		3.1	3.8
<b>Net cash used in investing activities</b>		<b>(285.6)</b>	<b>(306.6)</b>
<b>Cash flows from financing activities</b>			
Cost of shares purchased		(64.3)	(36.6)
Facility and arrangement fees		(19.2)	–
Proceeds from exercise of share options		0.3	–
Proceeds of borrowings		–	32.5
Repayment of borrowings		(53.4)	–
<b>Net cash flows used in financing activities</b>		<b>(136.6)</b>	<b>(4.1)</b>
Net decrease in cash and cash equivalents		(431.5)	(271.5)
Opening cash and cash equivalents at beginning of year		1,308.3	1,586.6
Exchange losses on cash and cash equivalents		(7.5)	(6.8)
<b>Closing cash and cash equivalents</b>	3.2	<b>869.3</b>	<b>1,308.3</b>

## Group Statement of Changes in Equity

### For the year ended 31 December 2014

	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 2013	499.9	(28.7)	(31.5)	296.1	(74.8)	2,980.7	<b>3,641.7</b>
Loss for the year	–	–	–	–	–	(555.9)	<b>(555.9)</b>
Deficit on valuation of financial assets	–	–	–	–	(110.8)	–	<b>(110.8)</b>
Deferred tax credit on valuation of financial assets	–	–	–	–	48.8	–	<b>48.8</b>
Valuation movement recycled to Income Statement	–	–	–	–	267.5	–	<b>267.5</b>
Deferred tax charge on valuation movement recycled to Income Statement	–	–	–	–	(74.5)	–	<b>(74.5)</b>
Currency translation differences	–	–	7.6	–	–	–	<b>7.6</b>
Total comprehensive income for the year	–	–	7.6	–	131.0	(555.9)	<b>(417.3)</b>
Share buy-back	(0.2)	–	–	0.2	–	(50.6)	<b>(50.6)</b>
Share-based payments	–	–	–	–	–	14.0	<b>14.0</b>
Cost of shares vesting	–	0.7	–	–	–	(0.7)	<b>–</b>
At 31 December 2013	499.7	(28.0)	(23.9)	296.3	56.2	2,387.5	<b>3,187.8</b>
Loss for the year	–	–	–	–	–	(381.1)	<b>(381.1)</b>
Deficit on valuation of financial assets	–	–	–	–	(261.1)	–	<b>(261.1)</b>
Deferred tax credit on valuation of financial assets	–	–	–	–	56.6	–	<b>56.6</b>
Valuation movement recycled to Income Statement	–	–	–	–	189.2	–	<b>189.2</b>
Deferred tax charge on valuation movement recycled to Income Statement	–	–	–	–	(40.9)	–	<b>(40.9)</b>
Currency translation differences	–	–	(58.8)	–	–	–	<b>(58.8)</b>
Total comprehensive income for the year	–	–	(58.8)	–	(56.2)	(381.1)	<b>(496.1)</b>
Share buy-back	(0.4)	–	–	0.4	–	(50.3)	<b>(50.3)</b>
Share-based payments	–	–	–	–	–	21.4	<b>21.4</b>
Exercise of employee share options	0.1	0.2	–	–	–	–	<b>0.3</b>
Cost of shares vesting	–	1.1	–	–	–	(1.1)	<b>–</b>
At 31 December 2014	<b>499.4</b>	<b>(26.7)</b>	<b>(82.7)</b>	<b>296.7</b>	<b>–</b>	<b>1,976.4</b>	<b>2,663.1</b>

## Section 1 – Basis of Preparation

This section contains the Group's significant accounting policies that relate to the financial statements as a whole. Significant accounting policies specific to one note are included with that note. Accounting policies relating to non-material items are not included in these financial statements.

This section also includes new EU endorsed accounting standards, amendments and interpretations and their expected impact, if any, on the performance of the Group.

### 1.1 Significant Accounting Policies

#### a) Basis of preparation

The consolidated financial statements of Cairn Energy PLC ('Cairn' or 'the Group') for the year ended 31 December 2014 were authorised for issue in accordance with a resolution of the directors on 9 March 2015. Cairn is a limited company incorporated and domiciled in the United Kingdom whose shares are publicly traded. The registered office is located at 50 Lothian Road, Edinburgh, Scotland, EH3 9BY.

Cairn prepares its financial statements on a historical cost basis, unless accounting standards require an alternate measurement basis. Where there are assets and liabilities calculated on a different basis, this fact is disclosed either in the relevant accounting policy or in the notes to the financial statements. The financial statements comply with the Companies Act 2006.

The Group's financial statements are prepared on a going concern basis.

#### b) Accounting standards

Cairn prepares its financial statements in accordance with applicable International Financial Reporting Standards ('IFRS'), issued by the International Accounting Standards Board ('IASB') as adopted by the EU. The Group's financial statements are also consistent with IFRS as issued by the International Accounting Standards Board ('IASB') as they apply to accounting periods ended 31 December 2014.

Effective 1 January 2014, Cairn has adopted the following standards:

- IFRS 10 'Consolidated Financial Statements'
- IFRS 11 'Joint Arrangements'
- IFRS 12 'Disclosure of interests in Other Entities'
- IAS 27 (amendment) 'Separate Financial Statements'
- IAS 28 (amendment) 'Investments in Associates and Joint Ventures'

Adopting IFRS 11 has the most significance as the Group's material interests in oil and gas exploration and development licences are managed through joint arrangements with fellow partners.

Previously, the Group's interests in these arrangements were classified as jointly controlled assets and disclosed as joint venture balances in the notes to the appropriate financial statement line item. Following implementation of IFRS 11, the Group's joint arrangements are all now classified as joint operations and the disclosures in the financial statements amended accordingly. There was no impact on the results for the year as a result of adoption.

The following amendments to standards issued by the IASB and endorsed by the EU have yet to be adopted by the Group:

- Annual improvements to IFRSs 2010-2012 Cycle (effective 1 July 2014)

The adoption of these amendments will have no material impact on Cairn's results or financial statement disclosures. There are no other standards or amendments issued by the IASB and endorsed by the EU that will impact the Group.

#### c) Basis of consolidation

The consolidated financial statements include the results of Cairn Energy PLC and its subsidiary undertakings to the Balance Sheet date. Where subsidiaries follow differing accounting policies from those of the Group, those accounting policies have been adjusted to align with those of the Group. Inter-company balances and transactions between Group companies are eliminated on consolidation, though foreign exchange differences arising on inter-company balances between subsidiaries with differing functional currencies are not offset.

The results of subsidiaries acquired in any year are included in the Income Statement and Statement of Cash Flows from the effective date of acquisition while the results of subsidiaries disposed of during the year are included in the Income Statement and Statement of Cash Flows to the date at which control passes from the Group.

## 1.1 Significant Accounting Policies – Continued

### 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 144 to 146.

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 (see sections 2.1 and 2.2). All of the Group's Intangible exploration/appraisal assets and Property, plant & equipment – development/producing assets are related to interests in joint operations.

Cairn's working capital balances relating to joint operations are included in Other receivables (section 3.4) and Trade and other payables (section 3.5). 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. 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 parent and subsidiary accounts into the presentation currency, US\$, using the closing rate method for assets and liabilities which are translated at the rate of exchange prevailing at the Balance Sheet date and rates at the date of transactions for Income Statement accounts. Cairn takes exchange differences arising on the translation of net assets of Group companies whose functional currency is non-US\$ directly to reserves.



## Section 2 – Oil and Gas Assets and Related Goodwill

This section focuses on the assets in the Balance Sheet which form the core of Cairn's business. This section quantifies the financial impact of the operations for the year fully described in the Operational review on pages 22 to 27.

Included are details of the costs of multi-well programmes in Morocco and Senegal and the impairment reviews and tests performed on the Group's assets.

### Significant accounting judgements in this section:

#### Impairment testing on oil and gas assets

Given the recent fall in oil prices which lowers the Group's short-term oil price assumption, Cairn has tested its oil and gas assets which contain discovered resources for impairment. Remaining exploration assets are reviewed for indicators of impairment and tested where indicators are identified. This is consistent with the Group's accounting policies.

The impairment tests resulted in an impairment of an asset in the North Sea and Greenland. For details of the indicators and the subsequent impairment tests conducted on those assets, see section 2.1.

### 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. Where there is a verifiable third-party arm's-length transaction from which a market value can be obtained this market value represents the fair value. In January 2015, Cairn completed the sale of a 10% working interest in the Catcher development and this transaction provides evidence of the fair value less costs of disposal of this asset at the Balance Sheet date.

Where there is no verifiable third-party arm's-length transaction, the fair value less costs of disposal of an asset is calculated using discounted post-tax cash flow models.

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\$90 per boe escalated at 2.5% per annum;
- Reserve estimates of discovered resource (2P and 2C) based on P50 reserve estimates;
- Production profiles based on Cairn's internal estimates 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 2.5% per annum; and
- Discount rates of 10% for the Group's UK and Norwegian North Sea assets.

#### Impairment testing of goodwill

The goodwill arising from past corporate transactions in the UK and Norwegian North Sea is tested for impairment by comparing the recoverable amount against the carrying value of the underlying oil and gas assets in the UK and Norwegian North Sea operating segment. As with 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.

## 2.1 Intangible Exploration/Appraisal Assets

### Accounting policy

Cairn follows a successful-efforts-based accounting policy for oil and gas assets.

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

Expenditure incurred on the acquisition of a licence interest is initially capitalised on a licence-by-licence basis. Costs are held, un-depleted, within intangible exploration/appraisal assets until such time as the exploration phase on the licence area is complete or commercial reserves have been discovered. Exploration expenditure incurred in the process of determining oil and gas exploration targets is capitalised initially within intangible exploration/appraisal assets and subsequently allocated to drilling activities. Exploration/appraisal drilling costs are initially capitalised on a well-by-well basis until the success or otherwise of the well has been established. The success or failure of each exploration/appraisal effort is judged on a well-by-well basis. Drilling costs are written off on completion of a well unless the results indicate that hydrocarbon reserves exist and there is a reasonable prospect that these reserves are commercial.

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

### Impairment

Intangible exploration/appraisal assets are reviewed regularly for indicators of impairment and tested for impairment where such indicators exist. An indicator that one of the Group's assets may be impaired is most likely to be one of the following:

- There are no further plans to conduct exploration activities in the area;
- Exploration drilling in the area has failed to discover commercial reserve volumes; or
- Development proposals for appraisal assets in the pre-development stage indicate that it is unlikely that the carrying value of the exploration/appraisal asset will be recovered in full.

In such circumstances the intangible exploration/appraisal asset is allocated to any property, plant & equipment – development/producing assets within the same cash-generating unit and tested for impairment. Any impairment arising is recognised in the Income Statement for the year. Where there are no development/producing assets within the cash-generating unit, the excess of the carrying amount of exploration/appraisal asset over its recoverable amount are charged immediately to the Income Statement.

	Atlantic Margin					Total US\$m
	Senegal US\$m	Other Africa US\$m	Greenland and Republic of Ireland US\$m	Mediterranean US\$m	North West Europe – UK and Norway US\$m	
<b>Net book value</b>						
At 1 January 2013	–	2.2	44.5	3.6	849.5	899.8
Foreign exchange	–	–	–	–	7.4	7.4
Additions	41.6	136.3	17.3	4.5	160.5	360.2
Disposals	–	–	–	(0.5)	(5.1)	(5.6)
Transfers	–	–	–	–	(298.7)	(298.7)
Impairment	–	–	–	–	(251.4)	(251.4)
Unsuccessful exploration costs	–	(107.4)	(23.6)	(0.8)	(81.3)	(213.1)
At 1 January 2014	41.6	31.1	38.2	6.8	380.9	<b>498.6</b>
Foreign exchange	–	–	(0.8)	(0.8)	(28.6)	<b>(30.2)</b>
Additions	145.7	99.8	19.1	5.5	108.8	<b>378.9</b>
Disposals	(20.5)	(0.3)	(5.5)	–	(0.3)	<b>(26.6)</b>
Transfers	–	–	–	–	(148.4)	<b>(148.4)</b>
Impairment	–	–	(22.7)	–	(24.2)	<b>(46.9)</b>
Unsuccessful exploration costs	–	(100.1)	(6.6)	(6.9)	(94.8)	<b>(208.4)</b>
<b>At 31 December 2014</b>	<b>166.8</b>	<b>30.5</b>	<b>21.7</b>	<b>4.6</b>	<b>193.4</b>	<b>417.0</b>

## Section 2 – Oil and Gas Assets and Related Goodwill continued

### 2.1 Intangible Exploration/Appraisal Assets – Continued

#### Atlantic Margin – Senegal

Cairn completed the farm-down of the three contiguous Senegalese blocks to ConocoPhillips in January 2014. Back costs received under the agreement are shown as disposals of US\$20.5m. Cairn had originally farmed-in to the three blocks during 2013.

During 2014, Cairn completed two exploration wells offshore Senegal: the FAN-1 and SNE-1 wells. Both wells encountered hydrocarbons. Results to date indicate that the SNE-1 well discovered commercial volumes of oil while further work is required to determine the commerciality of the FAN-1 discovery. Capitalised costs of US\$166.8m at 31 December 2014 include the cost of these wells. Cairn, along with its partners in the joint operation, are preparing further exploration and appraisal programmes for submission to the Government of Senegal in May 2015, with a drilling programme due to commence in Q4 2015.

#### Atlantic Margin – Other Africa: Morocco and Mauritania

Cairn completed two exploration wells offshore Morocco in the current year. The Fom Draa and Juby Maritime wells did not encounter commercial hydrocarbons and both were plugged and abandoned. US\$53.2m of unsuccessful exploration costs were charged to the Income Statement in 2014. Costs of US\$107.4m incurred to 31 December 2013 were charged as unsuccessful costs in the prior year.

A third well in Morocco, offshore Western Sahara, the non-operated Cap Boujdour well, commenced drilling in December 2014. The well failed to encounter commercial hydrocarbons and costs to 31 December of US\$46.9m were charged to the Income Statement in 2014 as unsuccessful exploration costs.

Work continued on the C-19 licence offshore Mauritania during 2014 with additions of US\$2.9m in the current year (2013: US\$27.0m). Costs of US\$30.5m remaining at the year end represent US\$29.9m of Mauritania costs and US\$0.6m of other costs.

#### Atlantic Margin – Greenland and Republic of Ireland

Cairn is actively seeking to farm-down the Group's interests in Greenland before undertaking any further exploration activities across the licence interests it holds. Though Cairn remains encouraged by the Pitu prospect, with no firm plans for future exploration activity, the remaining costs of US\$22.7m associated with the Greenland licences were fully impaired at the year end.

The costs of US\$21.7m remaining at the year end relate to the Spanish Point appraisal prospect, offshore Republic of Ireland.

#### North West Europe – UK and Norway

##### UK and Norwegian North Sea

Additions in the current year of US\$108.8m (2013: US\$160.5m) relate to expenditure on exploration and appraisal wells drilled and new prospects added to the portfolio. The Group added to its existing exploration portfolio through the acquisition of non-operated interests in the PL248c Grosbeak prospects in the Norwegian North Sea and through licences awarded under the latest rounds in both the UK and Norway.

During 2014, two exploration wells were completed in the North Sea. Neither the UK Aragon well nor the Norwegian Atlas well discovered hydrocarbons. Unsuccessful exploration costs of US\$50.0m were charged to the Income Statement together with US\$2.2m relating to other licences. 2013 unsuccessful costs of US\$81.3m included costs of US\$53.5m and US\$18.6m relating to the Frode and Klara exploration wells in the Norwegian North Sea.

Following the two-well appraisal programme on the Skarvfjell discovery which completed drilling operations in 2013, the interpretation of the well results concluded in the current year. The appraisal wells confirmed the estimated reserve volumes of the discovery without materially increasing the future economic value of the field. As the Skarvfjell asset was initially recognised at fair value, it is unlikely that the costs relating to the appraisal wells will be recovered and costs of US\$25.2m are charged as unsuccessful exploration costs in the year.

DECC approval of the Catcher FDP was received in June 2014. Costs of US\$148.4m were transferred from Intangible exploration/appraisal assets to Property, plant & equipment – development/producing assets during the year. A similar transfer of US\$298.7m was made in 2013 following approval of the Kraken FDP.

Exploration costs remaining at the year end include the net book value of the Catcher satellite discoveries and exploration prospects and the Skarvfjell discovery and associated satellite prospects.

At the year end, Cairn reviewed its intangible exploration/appraisal assets for indicators of impairment. Impairment tests identified impairment on one of the Group's intangible exploration assets, resulting in a charge of US\$24.2m to the Income Statement.

The 2013 year end impairment review identified an indicator of impairment on the Catcher asset. The subsequent test resulted in an impairment charge of US\$251.4m.

##### Norwegian Barents Sea

Cairn has farmed-in to Block PL393B in the Barents Sea, which included the Ensis exploration well which completed in September 2014. The well did not encounter any hydrocarbons and was plugged and abandoned. Farm-in costs and additional costs incurred of US\$17.4m were charged to the Income Statement as unsuccessful exploration costs. No costs remain capitalised at the year end.

## 2.2 Property, Plant & Equipment – Development/Producing Assets

### Accounting policy

#### Costs

All costs incurred after the technical feasibility and commercial viability of producing hydrocarbons has been demonstrated are capitalised within development/producing assets on a field-by-field basis. Subsequent expenditure is capitalised only where it either enhances the economic benefits of the development/producing asset or replaces part of the existing development/producing 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 of development/producing assets are credited against the previously capitalised cost. A gain or loss on disposal of a development/producing asset is recognised in the Income Statement to the extent that the net proceeds exceed or are less than the appropriate portion of the net capitalised costs of the asset.

#### Impairment

Development/producing assets are reviewed for indicators of impairment at the Balance Sheet date. Indicators of impairment for the Group's development/producing 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/producing 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 cash-generating unit containing the asset and tested against the carrying value of the assets and liabilities in the cash-generating unit for impairment. Where an asset can be tested independently for impairment, this test is performed prior to the inclusion of the asset into a cash-generating unit for further impairment tests.

If the carrying amount of the asset or cash-generating unit exceeds its recoverable amount, an impairment charge is made.

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.

	North West Europe – UK and Norway US\$m	Total US\$m
<b>Cost and net book value</b>		
At 1 January 2013	71.0	71.0
Foreign exchange	1.7	1.7
Additions	44.2	44.2
Transfers from intangible exploration/appraisal assets	298.7	298.7
Disposals	(115.7)	(115.7)
At 1 January 2014	299.9	<b>299.9</b>
Foreign exchange	(30.5)	<b>(30.5)</b>
Additions	50.0	<b>50.0</b>
Transfers from intangible exploration/appraisal assets	148.4	<b>148.4</b>
<b>At 31 December 2014</b>	<b>467.8</b>	<b>467.8</b>

Exploration and appraisal costs of US\$148.4m relating to the Catcher fields included in the FDP were transferred to development/producing assets in 2014. A similar transfer of exploration costs for the Kraken field was made in 2013 upon receiving DECC approval.

In September 2014, Cairn entered into an agreement to farm-down 10% of the Group's 30% working interest in the Catcher development, satellite fields and surrounding exploration acreage to Dyas UK Limited ('Dyas'). Under the terms of the deal, Dyas will fund Cairn's exploration and development costs in respect of the licences up to a cap of US\$182.0m.

Final approval for the sale to Dyas was received in January 2015. As the deal had an effective economic date of 1 January 2014, on completion, Cairn received a refund of costs of US\$54.7m including US\$36.5m received under the carry.

During 2013, Cairn agreed the sale of the Mariner asset in the UK North Sea to Dyas BV, receiving formal approval in December 2013. The disposal of Mariner resulted in a US\$24.7m loss to the Income Statement.

## Section 2 – Oil and Gas Assets and Related Goodwill continued

### 2.2 Property, Plant & Equipment – Development/Producing Assets – Continued

Impairment tests were performed on the Group's development/producing assets at the Balance Sheet date. The value of Catcher implicit in the Dyas sale supports the carrying value of the Group's remaining 20% working interest. Impairment tests were also performed on the Kraken development asset and concluded that no impairment existed (2013: US\$nil). Sensitivity analysis is provided in section 2.5.

### 2.3 Capital Commitments

	2014 US\$m	2013 US\$m
Oil and gas expenditure:		
Intangible exploration/appraisal assets – non-rig commitments	146.1	292.6
Intangible exploration/appraisal assets – drilling rig commitments	-	195.2
Property, plant & equipment – development/producing assets	1,271.4	372.8
Contracted for	1,417.5	860.6

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 relate to operations in Africa and the UK and Norwegian North Sea. The capital commitments on Property, plant & equipment – development/producing assets relate to the North Sea development projects and include US\$215.0m of capital commitments for the 10% share of Catcher which was farmed-down to Dyas in January 2015 (section 6.1). Dyas will be responsible for funding this in full.

Capital commitments for property, plant & equipment – development/producing assets include US\$685.9m relating to two FPSO lease commitments due within the next eight years. This includes US\$119.7m of lease commitments on the 10% of Catcher which was farmed-down to Dyas as noted above. The lease term for these assets has not yet commenced.

The Group has no further material capital expenditure committed at the Balance Sheet date.

### 2.4 Intangible Assets – Goodwill

#### Accounting policy

##### Goodwill

Cairn allocates the purchase consideration on the acquisition of a subsidiary to the assets and liabilities acquired on the basis of fair value at the date of acquisition. Any excess of the cost of acquisition over the fair value of the assets and liabilities is recognised as goodwill. Any goodwill arising is recognised as an asset and is subject to annual review for impairment. Goodwill is written off where circumstances indicate that the recoverable amount of the underlying cash-generating unit including the asset may no longer support the carrying value of goodwill. Any such impairment loss arising is recognised in the Income Statement for the year. Impairment losses relating to goodwill cannot be reversed in future years.

In testing for impairment, goodwill arising on business combinations is allocated from the date of acquisition to the group of cash-generating units representing the lowest level at which it will be monitored. Cairn's policy is to monitor goodwill at operating segment level before combining segments for reporting.

The recoverable amount of a cash-generating unit, or group of cash-generating units, within the segment is based on its fair value less costs of disposal, using estimated cash flow projections over the licence period of the exploration assets risk-weighted for future exploration success. The key assumptions are sensitive to market fluctuations and the success of future exploration drilling programmes. The most likely factor which will result in a material change to the recoverable amount of the cash-generating unit is the result of future exploration drilling, which will determine the licence area's future economic potential.

	UK and Norwegian North Sea US\$m	Total US\$m
<b>Net book value</b>		
At 1 January 2013	485.5	485.5
Foreign exchange	2.1	2.1
Impairment	(324.2)	(324.2)
At 1 January 2014	163.4	163.4
Foreign exchange	(18.3)	(18.3)
<b>At 31 December 2014</b>	<b>145.1</b>	<b>145.1</b>

Goodwill is fully allocated to the UK and Norwegian North Sea operating segment. At 31 December 2014, the goodwill impairment test did not identify any impairment, with the carrying value of the UK and Norwegian North Sea operating segment being less than the recoverable amount of the underlying assets, principally the Catcher, Kraken and Skarvfjell assets.



## 2.4 Intangible Assets – Goodwill – Continued

The impairment of the Catcher asset in 2013 (see section 2.1) reduced both the carrying value of the operating segment and its recoverable amount in equal measures. The release of deferred tax provided on the Catcher asset, however, increased the carrying value of the segment in relation to the recoverable amount. Additionally, the recognition of tax credits for field allowances to which the Kraken asset was eligible further increased the carrying value of the segment. As a result, the recoverable amount of the assets could no longer support their carrying value and at 31 December 2013 the year end impairment test identified impairment and a charge of US\$324.2m was recorded.

The remaining carrying value of goodwill at 31 December 2013 was supported by the fair value less costs of disposal of the Group's UK and Norwegian North Sea assets.

## 2.5 Sensitivity Analysis

### North West Europe oil and gas assets

At 31 December 2014, impairment tests were conducted on the Group's North Sea exploration/appraisal assets and development/producing assets resulting in an impairment charge of US\$24.2m. An impairment test was also conducted on goodwill allocated to the North Sea Operating Segment. No impairment of goodwill was identified.

For assets where the recoverable amount is based on fair value less costs of disposal estimated using discounted cash flow modelling, the key assumptions used in determining the valuations are 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.

Cairn has run sensitivities on its long-term oil price assumptions at US\$75 and US\$70. Cairn also increased the short-term period, where assumptions are based on the forward curve, from three to four years. The impact of these changes on the carrying value of the Group's assets at the Balance Sheet date is summarised below:

	Decrease in Intangible exploration/ appraisal assets US\$m	Decrease in Property, plant & equipment – development assets US\$m	Decrease in Goodwill US\$m
Short-term period increased from three to four years	–	–	–
Decrease in oil price assumption to US\$75 per boe	(14.6)	–	(37.1)
Decrease in oil price assumption to US\$70 per boe	(32.6)	(27.1)	(88.1)

A Key Performance Indicator ("KPI") for the Group is to ensure effective engagement with partners to progress the North Sea development projects on time and within budget. Cairn's base case asset valuations, used to estimate fair value less costs of disposal in impairment tests, assume this KPI is met. With the value of the Catcher development asset supported by the sale to Dyas, Cairn has run sensitivities on the Kraken development asset, delaying the date of first oil production by up to 12 months and increasing costs by 10%. The resultant fall in value would not impact the carrying value of any of the assets on the Group's Balance Sheet.

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.

### Other oil and gas assets

At the year end, an impairment charge was recognised on intangible exploration assets in Greenland as noted in section 2.1. These assets are fully impaired in accordance with IFRS and the Group's accounting policies and therefore there is no meaningful sensitivity analysis to provide.

There are no reasonable changes in assumptions that would lead to a material impairment of any of the Group's remaining assets in the Atlantic Margin.

## Section 3 – Financial Assets and Working Capital

Cairn’s liquid cash resources supported by the undrawn US\$575.0m 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.

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:

#### Impairment of Available-for-sale Financial Asset

The Group’s ~10% shareholding in Cairn India Limited, classified as a non-current available-for-sale financial asset, suffered a significant fall in value during 2014. The size of the deficit was such that cumulative mark-to-market valuation movements recognised in ‘Other Comprehensive Income’ and classified as an available-for-sale reserve in equity, were recycled to the Income Statement as impairment.

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 9.8% 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 assets represent listed equity shares which are held at fair value (the quoted market price). Movements in the fair value during the year are recognised directly in equity and are disclosed in the Statement of Comprehensive Income. The cumulative gains or losses that arise on subsequent disposal of available-for-sale assets are recycled through the Income Statement.

At each reporting date, the fair value of the financial asset is compared to the value at the date of its initial recognition for signs of a prolonged or significant deficit in the valuation, which would indicate impairment. Where impairment is identified, cumulative losses recognised in Other comprehensive income are recycled to the Income Statement. In the event of a subsequent recovery in the valuation of the asset, there is no reversal of impairment; any such post-impairment gains are recognised as a surplus through Other comprehensive income. Any further impairment losses will be recognised through the Income Statement.

	Listed equity shares US\$m
<b>Fair Value</b>	
As at 1 January 2013	1,138.4
Deficit on valuation	(110.8)
As at 1 January 2014	<b>1,027.6</b>
Deficit on valuation	<b>(261.1)</b>
Disposal	<b>(63.9)</b>
<b>As at 31 December 2014</b>	<b>702.6</b>

Available-for-sale financial assets represent the Group’s remaining investment in the fully diluted share capital of Cairn India Limited, listed in India, which by its nature has no fixed maturity or coupon rate. These listed equity securities present the Group with an opportunity for return through dividend income and trading gains.

In January 2014, Cairn was contacted by the Indian Income Tax Department to provide information in relation to the year ending 31 March 2007. While interaction with the Indian Income Tax Department continues, Cairn has been restricted by the Indian Income Tax Department from selling its shares in, or receiving dividends declared by, Cairn India Limited.

Prior to the restriction in January, the Company disposed of 12,048,836 shares in Cairn India Limited, recognising a gain of US\$3.9m. This includes prior year unrealised gains recycled from equity of US\$5.1m. The disposal of 0.6% shareholding leaves a residual 9.8% interest in Cairn India Limited.

At 31 December 2014, the value of the investment in Cairn India Limited had fallen to US\$702.6m. The significant accumulated deficit of US\$194.3m from the date of a previous impairment was recycled to the Income Statement and recorded as impairment. An impairment of US\$267.5m was recycled to the Income Statement in June 2013 following a significant fall in value from the date of original recognition.

### 3.1 Available-for-sale Financial Assets – Continued

#### Sensitivity analysis

At the year end the closing Cairn India Limited share price used to value the available-for-sale financial assets was INR 240.55/US\$3.82 (2013: INR 323.75/US\$5.24). 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 the highest and lowest share prices measured in the preceding 12-month period and on decreases of 10% and 20% on the share price at 31 December 2014. Those prices are determined using the closing INR share price converted to US\$ at the daily rate.

	Effect on loss for year US\$m	Effect on Equity US\$m
<b>As at 31 December 2014</b>		
Increase to the highest share price in 2014 – INR 383 (US\$6.46)	–	<b>382.2</b>
Decrease to the lowest share price in 2014 – INR 229 (US\$3.61)	<b>(30.0)</b>	<b>(30.0)</b>
Decrease of 10% on closing share price in 2014 – INR 216 (US\$3.43)	<b>(60.8)</b>	<b>(60.8)</b>
Decrease of 20% on closing share price in 2014 – INR 192 (US\$3.05)	<b>(131.1)</b>	<b>(131.1)</b>
<b>As at 31 December 2013</b>		
Increase to the highest share price in 2013 – INR 340 (US\$6.33)	–	167.7
Decrease to the lowest share price in 2013 – INR 274 (US\$4.51)	(54.6)	(111.2)

### 3.2 Net Funds

	2014 US\$m	2013 US\$m
Cash and cash equivalents	<b>869.3</b>	1,308.3
Loans and borrowings	–	(55.3)
<b>Net funds</b>	<b>869.3</b>	1,253.0

Cash and cash equivalents earn interest at floating rates based on daily bank deposit rates. Short-term deposits are made for varying periods from overnight deposits to three months depending on the cash requirements of the Group.

Cairn limits the placing of deposits, certificates of deposit 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 CDS exceeding 250 bps. Investments in money market liquidity funds are only made with AAA rated liquidity funds and the maximum holding in any single fund is 5% of total investments.

The 2013 bank loan represents amounts drawn under the Capricorn Norge AS revolving exploration loan facility. During 2014, this facility was fully repaid and subsequently cancelled.

## Section 3 – Financial Assets and Working Capital continued

### 3.2 Net Funds – Continued

On 18 July 2014, Cairn Energy PLC signed a US\$575.0m senior secured borrowing base facility with a syndicate of six international banks (BNP Paribas, Commonwealth Bank of Australia, DNB Bank ASA, HSBC Bank PLC, Societe Generale 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. 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 is 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. The outstanding 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.

Cairn Energy PLC had issued a US\$100.0m Letter of Credit on 22 July 2013 as required under the membership of the Oil Spill Response Scheme’s “Cap and Contain” arrangement which was fully cash backed. On 31 December 2014, the Letter of Credit was released by the beneficiary and the cash released such that no restrictions now apply. Any future requirement for such a Letter of Credit could be drawn from the US\$575.0m committed facility signed in 2014.

### 3.3 Income Tax Assets

Income tax assets of US\$60.3m (2013: US\$81.3m) relate to cash tax refunds due from the Norwegian authorities on the tax value of exploration expenses incurred in Norway during the current year.

### 3.4 Other Receivables

	2014 US\$m	2013 US\$m
Prepayments	19.1	5.2
Other receivables	105.8	86.2
Joint operation receivables	113.7	60.9
	238.6	152.3

Prepayments include facility fees of US\$16.3m incurred to secure debt funding. The amount will be amortised over the useful life of the facility, commencing on the date of the first draw-down under the facility, using an effective interest rate method. Costs directly related to development projects will be capitalised.

Other receivables includes costs incurred by Cairn awaiting recharge to joint operations and dividends receivable of US\$35.2m from Cairn India Limited. While the restriction over Cairn’s investment remains, Cairn India Limited is unable to remit these dividends to the Group. See section 3.1.

Joint operation receivables includes Cairn’s working interest share of the receivables relating to joint operations and amounts recoverable from partners in joint operations.

At 31 December 2014 no amount within the Group’s other receivables or joint operation receivables was past due or impaired (2013: US\$nil).

There was no Group allowance for doubtful debts in 2014. In determining the recoverability of other receivables the Group carries out a risk analysis based on the type and age of the outstanding receivable.

### 3.5 Trade and Other Payables

	2014 US\$m	2013 US\$m
Trade payables	28.5	10.3
Other taxation and social security	6.4	6.4
Other payables	3.0	15.2
Joint operation payables	235.6	135.6
Accruals	4.7	33.5
	278.2	201.0

Joint operation payables includes 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 includes amounts that Cairn will settle and recover from partners.

### 3.6 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 and fair value	2014 US\$m	2013 US\$m
<i>Loans and receivables</i>		
Cash and cash equivalents	869.3	1,308.3
Joint operation receivables	113.7	60.9
Other receivables	105.8	86.2
<i>Available-for-sale financial assets</i>		
Listed equity shares	702.6	1,027.6
	<b>1,791.4</b>	<b>2,483.0</b>

All of the above loans and receivables are current and unimpaired. The impairment of the available-for-sale financial asset recycled to the Income Statement does not impact the carrying amount in the Balance Sheet.

#### Financial liabilities

Carrying amount and fair value	2014 US\$m	2013 US\$m
<i>Amortised cost</i>		
Trade payables	28.5	10.3
Joint operation payables	235.6	135.6
Accruals	4.7	33.5
Other payables	3.0	15.2
Provisions	14.4	14.0
Loans and borrowings	-	55.3
	<b>286.2</b>	<b>263.9</b>

The fair value of financial assets and liabilities, other than available-for-sale financial assets, has been calculated by discounting the expected future cash flows at prevailing interest rates.

#### Maturity analysis

All of the Group financial liabilities have a maturity of less than one year, other than a provision of US\$2.8m (2013: US\$2.6m) that falls due after one year.

#### Fair value

The Group holds listed equity shares as a non-current available-for-sale financial asset. The Group determines and discloses the fair value of these by reference to the quoted (unadjusted) prices in active markets for those shares at the measurement date.

At 31 December 2014 the Group held the following financial instruments measured at fair value:

Assets measured at fair value – Level 1	2014 US\$m	2013 US\$m
<i>Available-for-sale financial assets</i>		
Equity shares – listed	702.6	1,027.6
	<b>702.6</b>	<b>1,027.6</b>



# 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 core regions of the Atlantic Margin, North West Europe and the Mediterranean.

This section also includes details of the Group tax credits in the year and deferred tax assets and liabilities held at the year end.

## Significant accounting judgements in this section:

### Deferred taxation

The deferred tax liability relating to the Group’s investment in Cairn India Limited, classified as an available-for-sale financial asset, is provided on the assumption that any future disposal will result in a tax liability.

At the year end Cairn recognised a deferred tax asset in respect of UK North Sea oil and gas assets. This deductible temporary difference represents eligible field allowances on the Kraken and Catcher assets, offset by other taxable temporary differences. Deferred tax assets are not included in the impairment tests conducted on the Group’s oil and gas assets. However, at each reporting date, Cairn reviews the carrying value of deferred tax assets to assess whether taxable profits will be available against which the Group can utilise unused tax losses and allowances which give rise to the asset.

Cairn believes 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.

## Key estimates and assumptions in this section:

### Deferred taxation

Deferred tax liabilities relating to UK and Norwegian North Sea assets are measured using the tax rates and laws that are enacted at the Balance Sheet date and are expected to apply to the period when the assets are realised, based on the conditions that existed at the Balance Sheet date. Deferred tax assets do not include additional field allowances that certain assets in the UK may qualify for in future periods, but which are subject to Government approval of respective field development plans which did not exist at the Balance Sheet date.

## 4.1 Segmental Analysis

### Operating segments

Cairn holds a balanced portfolio of exploration and development assets focused in three geographical regions: North West Europe; the Atlantic Margin; and the Mediterranean.

The operations of the Group are organised on a country-by-country basis; countries form the Group’s operating segments. For management reporting purposes, operating segments are combined into regional business units. Cairn monitors the results of each regional unit separately for the purposes of making decisions about resource allocation and performance assessment.

The Group’s Atlantic Margin exploration region contains two regional units. Assets in Greenland and the Republic of Ireland are combined into one unit while the Group’s African assets in Senegal, Morocco and Mauritania also form a separate unit.

The North West Europe regional unit holds the UK and Norway operating segments. This region was previously reported as “UK and Norwegian North Sea”. Currently the segment contains the Group’s North Sea assets including the Skarvfjell discovery in Norway and the UK Catcher and Kraken developments. The Ensis prospect in the Norwegian Barents Sea is also included in this segment.

The results of the Mediterranean region are reported along with the Group’s corporate assets within “Other Cairn Energy Group”. The Mediterranean includes licences in Spain, France and Malta.

## 4.1 Segmental Analysis – Continued

### Geographical information: non-current assets

#### Atlantic Margin: Greenland and Republic of Ireland

2014	2013
<b>US\$21.7m</b>	US\$38.2m

#### Other Cairn Energy Group: Others

2014	2013
<b>US\$4.8m</b>	US\$5.1m

#### Other Cairn Energy Group: Mediterranean

2014	2013
<b>US\$4.6m</b>	US\$6.9m

#### North West Europe: UK and Norway

2014	2013
<b>US\$807.0m</b>	US\$844.6m

#### Atlantic Margin: Senegal, Morocco and Mauritania

2014	2013
<b>US\$197.3m</b>	US\$73.1m

Non-current assets for this purpose consist of intangible exploration/appraisal assets; property, plant & equipment – development/producing assets; intangible assets – goodwill; and other property, plant & equipment and intangible assets.

The segment results for the year ended 31 December 2014 are as follows:

	Atlantic Margin				
	Senegal, Morocco and Mauritania US\$m	Greenland and Republic of Ireland US\$m	North West Europe – UK and Norway US\$m	Other Cairn Energy Group US\$m	Total US\$m
Pre-award costs	–	(0.7)	(45.1)	(9.0)	<b>(54.8)</b>
Unsuccessful exploration costs	(100.1)	(6.6)	(94.8)	(6.9)	<b>(208.4)</b>
Inventory disposal/write down	–	–	–	(8.4)	<b>(8.4)</b>
Depreciation	–	(0.1)	(0.3)	(0.7)	<b>(1.1)</b>
Amortisation	–	–	–	(2.2)	<b>(2.2)</b>
Other income and administrative expenses	–	(0.4)	(2.1)	(50.3)	<b>(52.8)</b>
Impairment of oil and gas assets	–	(22.7)	(24.2)	–	<b>(46.9)</b>
Gain on disposal of oil and gas assets	–	–	2.3	–	<b>2.3</b>
<b>Operating loss</b>	<b>(100.1)</b>	<b>(30.5)</b>	<b>(164.2)</b>	<b>(77.5)</b>	<b>(372.3)</b>
Gain on disposal of available-for-sale financial assets	–	–	–	3.9	<b>3.9</b>
Impairment of available-for-sale financial assets	–	–	–	(194.3)	<b>(194.3)</b>
Interest income	–	–	1.2	1.9	<b>3.1</b>
Interest expense	–	–	(0.1)	–	<b>(0.1)</b>
Other finance income and costs	0.8	(0.4)	3.5	(3.3)	<b>0.6</b>
<b>Loss before taxation</b>	<b>(99.3)</b>	<b>(30.9)</b>	<b>(159.6)</b>	<b>(269.3)</b>	<b>(559.1)</b>
Tax (charge)/credit	(1.3)	–	134.0	45.3	<b>178.0</b>
<b>Loss for the year</b>	<b>(100.6)</b>	<b>(30.9)</b>	<b>(25.6)</b>	<b>(224.0)</b>	<b>(381.1)</b>
<b>Capital expenditure</b>	<b>245.5</b>	<b>19.1</b>	<b>159.5</b>	<b>8.0</b>	<b>432.1</b>
<b>Total assets</b>	<b>358.1</b>	<b>28.0</b>	<b>988.8</b>	<b>1,642.5</b>	<b>3,017.4</b>
<b>Total liabilities</b>	<b>203.7</b>	<b>0.8</b>	<b>119.2</b>	<b>30.6</b>	<b>354.3</b>

# Section 4 – Results for the Year continued

## 4.1 Segmental Analysis – Continued

The segment results for the year ended 31 December 2013 are as follows:

	Atlantic Margin			Other Cairn Energy Group US\$m	Total US\$m
	Senegal, Morocco and Mauritania US\$m	Greenland and Republic of Ireland US\$m	North West Europe – UK and Norway US\$m		
Pre-award costs	–	(1.1)	(10.3)	(12.1)	(23.5)
Unsuccessful exploration costs	(107.4)	(23.6)	(81.3)	(0.8)	(213.1)
Depreciation	–	(0.1)	(0.5)	(1.1)	(1.7)
Amortisation	–	–	–	(2.8)	(2.8)
Other income and administrative expenses	(0.5)	(0.2)	(2.6)	(34.4)	(37.7)
Impairment of oil and gas assets	–	–	(251.4)	–	(251.4)
Loss on disposal of oil and gas assets	–	–	(24.7)	–	(24.7)
Impairment of goodwill	–	–	(324.2)	–	(324.2)
Operating loss	(107.9)	(25.0)	(695.0)	(51.2)	(879.1)
Impairment of available-for-sale financial assets	–	–	–	(267.5)	(267.5)
Interest income	–	–	1.3	2.5	3.8
Interest expense	–	–	(2.5)	–	(2.5)
Other finance income and costs	–	0.4	(0.2)	46.2	46.4
Loss before taxation	(107.9)	(24.6)	(696.4)	(270.0)	(1,098.9)
Tax credit	–	–	468.7	74.3	543.0
Loss for the year	(107.9)	(24.6)	(227.7)	(195.7)	(555.9)
Capital expenditure	177.9	17.3	204.9	8.4	408.5
Total assets	49.4	163.8	1,129.1	2,263.8	3,606.1
Total liabilities	8.8	135.1	169.0	105.4	418.3

## 4.2 Pre-award costs

During the year, the Group incurred total pre-award costs of US\$54.8m (2013:US\$23.5m) as Cairn looked at new opportunities in North West Europe and elsewhere.

US\$30.3m (2013: US\$nil) relates to pursuing new opportunities to follow up on the recent entry in the Norwegian Barents Sea, including US\$22.0m acquiring seismic data. US\$14.8m (2013: US\$10.3m) relates to new opportunities in the UK and Norway including licensing round applications. In the Norwegian 2014 APA Licensing Round, Cairn was awarded non-operated interests in five licences: PL788 (Cairn 50%), PL787 (Cairn 30%), PL790 (Cairn 25%), PL159 (Cairn 18%) and PL800 (Cairn 35%). Further costs of US\$9.7m (2013: US\$13.2m) were incurred in pursuit of new opportunities in the Mediterranean and other regions.

## 4.3 Net Operating Expenses

	2014 US\$m	2013 US\$m
Other income	(3.1)	–
Administrative expenses	59.2	42.2
Inventory disposal/write down	8.4	–
	64.5	42.2

Administrative expenses include US\$7.6m relating to the Group reorganisation, US\$1.6m of which were accelerated share-based payment charges. US\$8.5m (2013: US\$nil) incurred to defend the Group’s tax position in India are also included in administrative expenses.

## 4.4 Finance Income

	2014 US\$m	2013 US\$m
Bank and other interest receivable	3.1	3.8
Dividend income	35.2	40.5
Exchange gain	-	6.3
	<b>38.3</b>	<b>50.6</b>

Dividend income is receivable from Cairn India Limited. See section 3.1.

## 4.5 Finance Costs

	2014 US\$m	2013 US\$m
Bank loan and overdraft interest	0.3	2.6
Other finance charges	3.1	0.3
Exchange loss	31.3	-
	<b>34.7</b>	<b>2.9</b>

## 4.6 Taxation on Loss

### Accounting policy

The total tax charge or credit represents the sum of current tax and deferred tax. The current tax is based on taxable profit or loss for the year. Taxable profit or loss differs from net profit or loss as reported in the Income Statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit or loss.

Deferred tax liabilities are recognised for all taxable temporary differences except in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint 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. Deferred tax assets are recognised for deductible temporary differences that exist only where it is probable that taxable profits will be generated against which the carrying value of the deferred tax asset can be recovered.

A deferred tax asset or liability is not recognised if a temporary difference arises on initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

Current and deferred tax is calculated using tax rates and laws that have been enacted or substantively enacted by the Balance Sheet date.

## Section 4 – Results for the Year continued

### 4.6 Taxation on Loss – Continued

#### a) Analysis of tax credit on loss in the year

	2014 US\$m	2013 US\$m
<b>Current tax credits:</b>		
Norwegian tax refunds receivable	(67.3)	(81.6)
Withholding taxes deducted at source	1.4	–
	(65.9)	(81.6)
<b>Deferred tax credit:</b>		
Norwegian deferred tax (credit)/charge	(13.4)	20.3
Recognition of eligibility to future field allowances on UK development asset	(71.2)	(211.9)
Release of provision on disposal of UK development asset	–	(32.8)
Release of provision on impairment of UK intangible exploration/appraisal asset	(15.0)	(152.2)
Other UK deferred tax credits	28.4	(10.3)
Recycled from other comprehensive income on impairment of financial assets	(42.0)	(74.5)
Recycled from other comprehensive income on sale of financial assets	1.1	–
	(112.1)	(461.4)
<b>Total tax credit on loss</b>	<b>(178.0)</b>	<b>(543.0)</b>
<b>Tax included in Other Comprehensive Income:</b>		
Deferred tax credit on valuation of financial assets	(56.6)	(48.8)
Deferred tax charge on valuation movement recycled to Income Statement	40.9	74.5
<b>Total tax charge in Other Comprehensive Income</b>	<b>(15.7)</b>	<b>25.7</b>

Norwegian deferred tax credit includes a credit of US\$6.9m (2013: charge of US\$23.8m) on temporary differences in respect of non-current assets and a credit of US\$6.5m (2013: US\$3.5m) on losses and other temporary differences.

Other UK deferred tax charges includes a charge of US\$112.9m (2013: US\$59.0m) on temporary differences in respect of non-current assets and a credit of US\$84.5m (2013: credit of US\$69.3m) on losses and other temporary differences.

#### b) Factors affecting tax credit for the year

A reconciliation of income tax credit applicable to loss before income tax at the UK statutory rate to income tax credit at the Group's effective income tax rate is as follows:

	2014 US\$m	2013 US\$m
<b>Loss before taxation</b>	<b>(559.1)</b>	<b>(1,098.9)</b>
Loss before tax multiplied by the UK statutory rate of corporation tax of 21.5% (2013: 23.25%)	(120.2)	(255.5)
<b>Effect of:</b>		
Special tax rates and reliefs applying to oil and gas activities	(145.5)	(200.6)
Impact of field allowances on deferred tax	(47.8)	(145.5)
Additional deferred tax credit on disposal of development asset	–	(27.0)
Non-deductible impairment of goodwill	–	72.3
Adjustments in respect of prior periods	(2.6)	(16.6)
Temporary differences not recognised	147.2	46.0
Deferred tax credit on disposal of available-for-sale financial asset	(3.3)	–
Foreign exchange movements	(1.6)	(12.1)
Other	(4.2)	(4.0)
<b>Total tax credit on loss</b>	<b>(178.0)</b>	<b>(543.0)</b>

The reconciliation shown above has been based on the average UK statutory rate of corporation tax for 2014 of 21.5% (2013: 23.25%).

The UK main rate of corporation tax was 23% prior to 1 April 2014, and 21% from that date onwards. The reduction in the tax rate from 23% to 21% has resulted in an average rate of corporation tax of 21.5% for the year ended 31 December 2014, as shown above. The rate will reduce to 20% on 1 April 2015.

Special rates of tax apply to oil and gas activities in the UK and Norwegian North Sea operating segment. The applicable UK statutory tax rate applying to North Sea oil and gas activities is 62% and the applicable Norwegian rate applying to oil and gas activities is 78%.



## 4.6 Taxation on Loss – Continued

### c) Deferred tax assets and liabilities recoverable/due after more than one year

#### Reconciliation of movement in deferred tax assets/(liabilities):

	Temporary difference in respect of non-current assets US\$m	Losses US\$m	Other temporary differences US\$m	Total US\$m
<b>Deferred tax assets</b>				
At 1 January 2013	–	–	–	–
Deferred tax credit through Income Statement	(50.6)	109.3	–	58.7
At 1 January 2014	(50.6)	109.3	–	<b>58.7</b>
Deferred tax credit through Income Statement	(31.3)	84.5	–	<b>53.2</b>
Exchange differences arising	(0.2)	(5.5)	–	<b>(5.7)</b>
<b>At 31 December 2014</b>	<b>(82.1)</b>	<b>188.3</b>	<b>–</b>	<b>106.2</b>
<b>Deferred tax liabilities</b>				
At 1 January 2013	(597.4)	62.7	3.8	(530.9)
Deferred tax credit through Income Statement	448.4	(49.3)	3.7	402.8
Deferred tax charge through Other Comprehensive Income	(25.6)	–	–	(25.6)
Exchange differences arising	18.4	(12.4)	(0.3)	5.7
At 1 January 2014	(156.2)	1.0	7.2	<b>(148.0)</b>
Deferred tax credit through Income Statement	52.3	3.9	2.6	<b>58.8</b>
Deferred tax charge through Other Comprehensive Income	15.7	–	–	<b>15.7</b>
Exchange differences arising	14.5	4.2	(6.9)	<b>11.8</b>
<b>At 31 December 2014</b>	<b>(73.7)</b>	<b>9.1</b>	<b>2.9</b>	<b>(61.7)</b>

#### Deferred tax assets/(liabilities) analysed by country:

	2014 US\$m	2013 US\$m
<b>Deferred tax assets:</b>		
UK	<b>106.2</b>	58.7
	<b>106.2</b>	58.7
<b>Deferred tax liabilities:</b>		
Norway	<b>(52.2)</b>	(77.5)
India	<b>(9.5)</b>	(70.5)
	<b>(61.7)</b>	(148.0)

#### Recognised deferred tax assets

As at the Balance Sheet date, a net deferred tax asset of US\$106.2m (2013: US\$58.7m) has been recognised in the UK on other temporary differences and tax losses in excess of the UK deferred tax liability arising on temporary differences in respect of non-current assets attributable to UK Ring Fence trading activity. This includes the recognition in the year of a deferred tax credit to UK temporary differences in respect of non-current assets of US\$71.2m (2013: US\$211.9m), reflecting the eligibility to future field allowances on the Kraken and Catcher developments which will reduce future Ring Fence profits subject to Supplementary Charge. The eligible field allowances were confirmed when DECC approved the Kraken field development plan in 2013 and the Catcher field development plan in 2014, and will be claimed when production commences.

A deferred tax asset has also been recognised in respect of Norwegian tax losses and other temporary differences of US\$12.0m (2013: US\$8.2m) against a Norwegian deferred tax liability arising on temporary differences in respect of non-current assets.

# Section 4 – Results for the Year continued

## 4.6 Taxation on Loss – Continued

### c) Deferred tax assets and liabilities recoverable/due after more than one year (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:

	2014 US\$m	2013 US\$m
UK fixed asset temporary differences	244.5	163.8
UK Ring Fence trading losses	167.8	–
UK Ring Fence pre-trade losses	–	16.1
UK non-Ring Fence trading losses	3.9	–
UK non-Ring Fence pre-trade losses	5.3	5.3
UK excess management expenses	311.9	205.4
UK non-trade deficits	39.8	53.2
UK other temporary differences	7.6	6.6
Greenlandic tax losses	1,301.5	1,277.0

### d) Tax strategy and governance

The Group's tax strategy is fully aligned with its overarching business objectives and principles. Cairn commits to managing its tax affairs in a transparent and responsible manner and ensuring that all statutory obligations and disclosure requirements are met. We aim to comply with both the letter and spirit of the law in the relevant jurisdictions in which we operate, to ensure that the right amount of tax is paid, at the right time, within the right jurisdiction.

As the Group is currently at an early stage in the value creation cycle and the level of its exploration activities is high, there are currently no taxable profits in the UK. Taxable profits in other jurisdictions are also minimal, and as a result cash payments of corporation taxes are currently low.

Cairn's policy is to not enter into any artificial tax avoidance schemes and to build and maintain strong collaborative working relationships with all relevant tax authorities, based on honesty, integrity and proactive cooperation. The Group aims for certainty in relation to the tax treatment of all items; however, we acknowledge that this will not always be possible, for example where transactions are complex and there is a lack of maturity in the tax regime in the relevant jurisdiction in which we are operating. In such circumstances the Group will seek external advice where appropriate and ensure that the approach adopted in any relevant tax return is supportable and includes full disclosure of the position taken.

## 4.7 Earnings per Ordinary Share

Basic and diluted earnings per share are calculated using the following measures of loss:

	2014 US\$m	2013 US\$m
Loss and diluted loss attributable to equity holders of the parent	(381.1)	(555.9)

The following reflects the share data used in the basic and diluted earnings per share computations:

	2014 '000	2013 '000
Weighted average number of shares	578,845	602,279
Less weighted average shares held by ESOP and SIP Trusts	(5,730)	(5,969)
<b>Basic weighted average number of shares</b>	<b>573,115</b>	<b>596,310</b>
Dilutive potential ordinary shares:		
Employee share options	33	389
<b>Diluted weighted average number of shares</b>	<b>573,148</b>	<b>596,699</b>

## Section 5 – Capital Structure and Other Disclosures

The disclosures in this section focus on the issued share capital, the share schemes in operation and the associated share-based payment charge to profit or loss. Other mandatory disclosures, such as details of related party transactions, can also be found here.

### Significant accounting judgements in this section:

There are no significant accounting judgements in this section.

### Key estimates and assumptions in this section:

#### Share-based payments

Charges for share-based payments are based on the fair value at the date of the award. The shares are valued using appropriate modelling techniques and inputs to the models include assumptions on leaver rates, trigger points, discount rates and volatility. See section 5.4.

### 5.1 Issued Capital and Reserves

#### Called-up share capital

Group and Company	Number 231/169p ordinary '000	231/169p ordinary US\$m
<b>Allotted, issued and fully paid ordinary shares</b>		
At 1 January 2013	603,261	13.0
Issued and allotted for employee share options	14	–
Shares repurchased and cancelled by the Company	(8,218)	(0.2)
At 1 January 2014	<b>595,057</b>	<b>12.8</b>
Issued and allotted for employee share options	<b>94</b>	<b>–</b>
Shares repurchased and cancelled by Company	<b>(18,887)</b>	<b>(0.4)</b>
<b>At 31 December 2014</b>	<b>576,264</b>	<b>12.4</b>

#### Share premium

Group and Company	2014 US\$m	2013 US\$m
At 1 January	<b>486.9</b>	486.9
Arising on shares issued for employee share options	<b>0.1</b>	–
<b>At 31 December</b>	<b>487.0</b>	486.9

#### Share buy-back

The Company's share buy-back programme (US\$100.0m plus associated fees of \$0.9m) ran from October 2013 until its suspension in March 2014. The first US\$50.0m was entered into with Cairn's brokers during 2013, and a further US\$50.0m during 2014. During 2014 18.9m shares were repurchased at a cost of US\$63.7m (2013: 8.2m shares at a cost of US\$36.3m) plus associated fees of US\$0.6m (2013: US\$0.3m).

#### 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 2014 of US\$19.3m (2013: US\$22.4m). The number of shares held by the Cairn Energy PLC Employees' Share Trust at 31 December 2014 was 4,284,055 (2013: 4,965,135) and the market value of these shares was £7.6m/US\$11.9m (2013: £13.4m/US\$22.2m).

#### 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 2014 of US\$7.4m (2013: US\$5.6m). The number of shares held by the Cairn Energy PLC Share Incentive Plan Trust at 31 December 2014 was 1,351,203 (2013: 938,846) and the market value of these shares was £2.4m/US\$3.8m (2013: £2.5m/US\$4.1m).

#### 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 Agora Oil and Gas AS. Capital reserves – non-distributable include non-distributable amounts arising on various Group acquisitions and the capital redemption reserve arising from the 2013/2014 share buy-back programme.

# Section 5 – Capital Structure and Other Disclosures continued

## 5.1 Issued Capital and Reserves – Continued

### Available-for-sale reserve

The available-for-sale reserve represents fair value movements on the available-for-sale financial assets (see section 3.1). At 31 December 2014, the cumulative deficit was recycled to the Income Statement as impairment.

## 5.2 Capital Management

The objective of the Group's capital management structure is to ensure that there remains sufficient liquidity within the Group to carry out committed work programme requirements. The Group monitors the long-term cash flow requirements of the business in order to assess the requirement for changes to the capital structure to meet that objective and to maintain flexibility.

Cairn manages the capital structure and makes adjustments to it in light of changes to economic conditions. To maintain or adjust the capital structure, Cairn may buy back shares, make a special dividend payment to shareholders, return capital, issue new shares for cash, repay debt, put in place new debt facilities (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 2014.

Capital and net debt were made up as follows:

	2014 US\$m	2013 US\$m
<b>Continuing operations</b>		
Trade and other payables	278.2	201.0
Loans and borrowings	-	55.3
Less cash and cash equivalents	(869.3)	(1,308.3)
Net funds less payables	(591.1)	(1,052.0)
Equity	2,663.1	3,187.8
Capital and net funds less payables	2,072.0	2,135.8
Gearing ratio	0%	0%

## 5.3 Staff Costs

	2014 US\$m	2013 US\$m
Wages and salaries	43.2	38.4
Social security costs and other taxes	5.6	4.8
Redundancy costs	4.7	0.3
Other pension costs	3.4	2.8
Share-based payments charge	21.4	14.0
	78.3	60.3

Staff costs are shown gross before amounts recharged to joint operations and include the costs of share-based payments. The share-based payments charge includes amounts in respect of both equity and cash-settled phantom options.

During 2014 the Company carried out a programme of restructuring which included redundancy costs of US\$4.7m.

The average number of full time equivalent employees, including executive directors and individuals employed by the Group working on joint operations, was:

	Number of employees	
	2014	2013
UK	164	158
Norway	14	15
Spain	4	5
Greenland	15	12
Nepal	-	2
Morocco	1	1
Group	198	193

## 5.4 Share-based Payments

### Accounting policy

The cost of awards to employees under Cairn's LTIP and share option plans are recognised over the three-year period to which the performance relates. The amount recognised is based on the fair value of the shares as measured at the date of the award. The shares are valued using a Monte Carlo model with the exception of the SIP awards which have been valued using a Black-Scholes model. Awards in prior years were valued using a Monte Carlo model.

The cost of equity-settled transactions is recognised, together with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award ("the vesting date"). The cumulative expense recognised for equity-settled transactions at each reporting date until the vesting date reflects the extent to which the vesting period has expired and the Company's best estimate of the number of equity instruments that will ultimately vest. The Income Statement charge or credit for a year represents the movement in cumulative expense as recognised at the beginning and end of that year.

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

The Group operates a number of share-based schemes for the benefit of its employees.

The number of Share Awards made by the Company during the year is given in the table below together with their weighted average fair value ("WAFV") and weighted average grant or exercise price ("WAGP/WAEP"):

	2014 WAFV £	2014 WAGP/WAEP £	2014 Number of shares	2013 WAFV £	2013 WAGP/WAEP £	2013 Number of shares
2010 SIP – free shares	1.40	1.68	264,810	2.50	2.82	129,578
2010 SIP – matching shares	1.40	1.86	197,097	2.50	2.79	121,474
2009 Approved Plan	0.28	1.68	589,320	0.72	2.78	485,814
2009 Unapproved Plan	0.28	1.68	6,479,802	0.72	2.78	4,277,846
2009 LTIP	1.06	1.68	10,986,850	1.35	2.78	5,648,805
2014 Share awards	1.81	1.81	55,096	–	–	–
			18,572,975			10,663,517

The analysis of the charge to the Income Statement in the year is:

	2014 US\$m	2013 US\$m
<b>Included within administrative expenses:</b>		
2010 SIP	0.8	0.9
2009 Approved Plan	1.0	0.6
2009 Unapproved Plan	4.4	3.6
2009 LTIP	15.0	8.3
2012 Share awards	0.2	0.6
	21.4	14.0

As a result of the Group reorganisation in 2014, administrative expenses include US\$1.6m (2013: US\$nil) of accelerated share-based payment charges reflecting the reduced performance period for staff leaving through redundancy.

Details of those awards with a significant impact on the results for the current and prior years are given below together with a summary of the remaining awards.

Further details on assumptions and inputs applying to all share awards can be found in appendix 3.

### 2009 LTIP

The awards existing under the 2009 LTIP are detailed in the table below together with the weighted average grant price ("WAGP") at 31 December:

	2014		2013	
	Number	WAGP (£)	Number	WAGP (£)
Outstanding as at 1 January	12,710,604	3.04	9,337,452	3.50
Granted during the year	10,986,850	1.68	5,648,805	2.78
Lapsed during the year	(5,673,289)	2.84	(2,275,653)	4.29
<b>Outstanding at 31 December</b>	<b>18,024,165</b>	<b>2.28</b>	<b>12,710,604</b>	<b>3.04</b>

Weighted average remaining contractual life of outstanding awards	1.5 years	1.6 years
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## Section 5 – Capital Structure and Other Disclosures continued

### 5.4 Share-based Payments – Continued

#### Summary of all other share schemes

The awards existing under all share schemes other than the 2009 LTIP but including the SIP are detailed in the table below together with the weighted average of the grant price, exercise price and notional exercise prices ("WAGP/WAEP") at 31 December:

	2014		2013	
	Number	WAGP/WAEP (£)	Number	WAGP/WAEP (£)
Outstanding at 1 January	11,011,826	2.82	7,126,626	2.94
Granted during the year	7,586,125	1.69	5,014,712	2.78
Vested/exercised during the year	(363,053)	2.10	(175,799)	2.94
Lapsed during the year	(2,456,149)	3.00	(953,713)	3.57
<b>Outstanding at 31 December</b>	<b>15,778,749</b>	<b>2.26</b>	<b>11,011,826</b>	<b>2.82</b>
Weighted average remaining contractual life of outstanding awards		<b>8.0 years</b>	8.0 years	

#### LTIP

The fair value of the 2009 LTIP scheme awards has been calculated using a Monte Carlo model, as described at appendix 3. The main inputs to the model have been laid out in the appendix, though vesting percentages for LTIPs can be above 100%. For details on the vesting conditions attached to the LTIPs refer to the Directors' Remuneration report on pages 76 to 97.

### 5.5 Directors' Emoluments and Remuneration of Key Management Personnel

Details of each Director's remuneration, pension entitlements, share options and awards pursuant to the LTIP are set out in the Directors' Remuneration report on pages 76 to 97. Directors' remuneration, their pension entitlements, and any share awards vested during the year is provided in aggregate in section 7.8.

#### Remuneration of key management personnel

The remuneration of the directors of the Company and of the members of the Management and Corporate teams who are the key management personnel of the Group is set out below in aggregate.

	2014 US\$m	2013 US\$m
Short-term employee benefits	9.8	10.2
Termination benefits	0.3	–
Post-employment benefits	0.6	0.6
Share-based payments	6.8	5.3
	<b>17.5</b>	<b>16.1</b>

In addition employer's national insurance contributions for key management personnel in respect of short-term employee benefits were US\$1.4m (2013: US\$1.3m).

Share-based payments represent the cost to the Group of key management personnel's participation in the Company's share schemes, measured under IFRS 2.

### 5.6 Guarantees

It is normal practice for the Group to issue guarantees in respect of obligations during the normal course of business.

During the year, Cairn Energy PLC entered into a US\$575.0m senior secured borrowing facility with a syndicate of six international banks (BNP Paribas, Commonwealth Bank of Australia, DNB Bank ASA, HSBC Bank PLC, Societe Generale and Standard Chartered Bank). See 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 2014:

- Various guarantees under the Group's bank facility for the Group's share of minimum work programme commitments for the current year of US\$7.8m (2013: US\$33.8m); and
- Parent company guarantees for the Group's obligations under joint operating agreements and other contracts.

## Section 6 – Post Balance Sheet Events

### 6.1 Sale of 10% Working Interest in Catcher

In September 2014, Cairn entered into an agreement to farm-down 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 will fund Cairn’s exploration and development costs in respect of the licences up to a cap of US\$182.0m.

Final approval for the sale to Dyas was received in January 2015. As the deal had an effective economic date of 1 January 2014, on completion Cairn received a refund of costs of US\$54.7m including US\$36.5m received under the carry.

# Company Balance Sheet

## As at 31 December 2014

	Section	2014 US\$m	2013 US\$m
<b>Non-current assets</b>			
Investments in subsidiaries	7.6	2,804.7	1,649.7
<b>Current assets</b>			
Other receivables	7.3	18.9	309.9
Cash and cash equivalents	7.2	24.0	882.9
		42.9	1,192.8
<b>Total assets</b>		<b>2,847.6</b>	<b>2,842.5</b>
<b>Current liabilities</b>			
Trade and other payables	7.4	68.4	19.8
<b>Total liabilities</b>		<b>68.4</b>	<b>19.8</b>
<b>Net assets</b>		<b>2,779.2</b>	<b>2,822.7</b>
<b>Equity</b>			
Called-up share capital	5.1	12.4	12.8
Share premium	5.1	487.0	486.9
Shares held by ESOP/SIP Trusts	5.1	(26.7)	(28.0)
Capital reserves – non-distributable	5.1	0.7	0.3
Merger reserve	5.1	255.9	255.9
Retained earnings		2,049.9	2,094.8
<b>Total equity</b>		<b>2,779.2</b>	<b>2,822.7</b>

The financial statements on pages 132 to 142 were approved by the Board of Directors on 9 March 2015 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 2014

	Section	2014 US\$m	2013 US\$m
<b>Cash flows from operating activities</b>			
Loss before taxation		(14.9)	(291.6)
Share-based payments charge		4.6	4.0
Impairment of investment in subsidiary		-	336.7
Finance income		(0.9)	(59.8)
Finance costs		2.9	-
Other receivables movement		307.4	(324.6)
Trade and other payables movement		(1,075.5)	(0.4)
<b>Net cash used in operating activities</b>		<b>(776.4)</b>	<b>(335.7)</b>
<b>Cash flows from investing activities</b>			
Dividend received		-	57.7
Interest received		0.7	1.8
<b>Net cash from investing activities</b>		<b>0.7</b>	<b>59.5</b>
<b>Cash flows from financing activities</b>			
Cost of shares purchased		(64.3)	(36.6)
Facility and arrangement fees		(19.2)	-
Proceeds from exercise of share options		0.3	-
<b>Net cash flows used in financing activities</b>		<b>(83.2)</b>	<b>(36.6)</b>
Net decrease in cash and cash equivalents		(858.9)	(312.8)
Opening cash and cash equivalents at beginning of year		882.9	1,196.4
Exchange losses on cash and cash equivalents		-	(0.7)
<b>Closing cash and cash equivalents</b>	7.2	<b>24.0</b>	<b>882.9</b>

# Company Statement of Changes in Equity

## For the year ended 31 December 2014

	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 2013	499.9	(28.7)	256.0	2,423.7	3,150.9
Loss for the year	-	-	-	(291.6)	(291.6)
Total comprehensive income for the year	-	-	-	(291.6)	(291.6)
Share buy-back	(0.2)	-	0.2	(50.6)	(50.6)
Share-based payments	-	-	-	14.0	14.0
Cost of shares vesting	-	0.7	-	(0.7)	-
At 31 December 2013	499.7	(28.0)	256.2	2,094.8	2,822.7
Loss for the year	-	-	-	(14.9)	<b>(14.9)</b>
Total comprehensive income for the year	-	-	-	(14.9)	<b>(14.9)</b>
Share buy-back	(0.4)	-	0.4	(50.3)	<b>(50.3)</b>
Share-based payments	-	-	-	21.4	<b>21.4</b>
Exercise of employee share options	0.1	0.2	-	-	<b>0.3</b>
Cost of shares vesting	-	1.1	-	(1.1)	-
<b>At 31 December 2014</b>	<b>499.4</b>	<b>(26.7)</b>	<b>256.6</b>	<b>2,049.9</b>	<b>2,779.2</b>



## Section 7 – Notes to the Company Financial Statements

This section contains the notes to the Company Financial Statements.

The issued capital and reserves of the Company are largely consistent with Cairn Energy PLC Group Financial Statements. Refer to section 5.1 of the Group Financial Statements.

Key estimates and assumptions in this section:

### Impairment testing of investments in subsidiaries

The Company's investments in subsidiaries have been tested for impairment by comparison against the underlying value of the subsidiaries' exploration/appraisal assets based on fair value less costs of disposal calculated using the same assumptions as noted for the testing of goodwill impairment in section 2.4.

### 7.1 Basis of Preparation

The Financial Statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union.

The Company applies consistent accounting policies as applied by 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 2014 was US\$14.9m (2013: US\$291.6m).

### 7.2 Net Funds

	2014 US\$m	2013 US\$m
Cash and cash equivalents	24.0	882.9
<b>Net funds</b>	<b>24.0</b>	<b>882.9</b>

### 7.3 Other Receivables

	2014 US\$m	2013 US\$m
Prepayments	15.0	0.3
Other receivables	3.9	1.8
Amounts owed by subsidiary undertakings	-	307.8
	<b>18.9</b>	<b>309.9</b>

During the year, the Company received shares from Capricorn Oil Limited, its principal subsidiary, for settlement of inter-company debts of US\$1,138.9m. Refer to section 7.6 for further details.

During 2013 a provision for doubtful debts of US\$689.2m made in a prior year was released when the net debt due from the subsidiary was capitalised through a share issue.

### 7.4 Trade and Other Payables

	2014 US\$m	2013 US\$m
Trade payables	0.2	0.1
Amounts payable to subsidiary undertakings	57.6	4.2
Other taxation and social security	1.3	1.1
Accruals	9.3	14.4
	<b>68.4</b>	<b>19.8</b>

# Section 7 – Notes to the Company Financial Statements continued

## 7.5 Financial Instruments

Set out below is the comparison by category of carrying amounts and fair values of all the Company’s financial instruments that are carried in the Financial Statements.

	2014 US\$m	2013 US\$m
<b>Financial assets: Carrying amount and fair value</b>		
<i>Loans and receivables</i>		
Cash and cash equivalents	24.0	882.9
Other receivables	3.9	1.8
Amounts receivable from subsidiary undertakings	-	307.8
	27.9	1,192.5

All of the above financial assets are current and unimpaired.

	2014 US\$m	2013 US\$m
<b>Financial liabilities: Carrying amount and fair value</b>		
<i>Amortised cost</i>		
Trade payables	0.2	0.1
Accruals	9.3	14.4
Amounts payable to subsidiary undertakings	57.6	4.2
	67.1	18.7

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 (2013: less than one year).

## 7.6 Investments in Subsidiaries

### Accounting policy

The Company’s investments in subsidiaries are carried at cost less provisions resulting from impairment. In testing for impairment the carrying value of the investment is compared to its recoverable amount, being its fair value less costs of disposal. The fair value is based on the discounted future net cash flows of oil and gas assets held by the subsidiary, using estimated cash flow projections over the licence period. For exploration assets, 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\$90 per boe (2013: long-term oil price of US\$90 per boe), escalation for prices and costs of 2.5%, and a discount rate of 10% (2013: 2.5% and 10% respectively). 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
<b>Net book value</b>		
At 1 January 2013	916.9	916.9
Additions	1,069.5	1,069.5
Impairments	(336.7)	(336.7)
At 1 January 2014	1,649.7	1,649.7
Additions	1,155.0	1,155.0
<b>At 31 December 2014</b>	<b>2,804.7</b>	<b>2,804.7</b>

Details of the Company’s principal subsidiaries at the Balance Sheet date are included in appendix 1.

Additions during the year included US\$1,138.9m for the issue of 731,262,214 shares of £1 each at par by Capricorn Oil Limited which reduced the amounts owed to the Company by Capricorn Oil Limited.

A further US\$16.1m (2013: US\$9.7m) was recognised as additions relating to Capricorn Oil Limited for the award of share options of the Company to the employees of Capricorn Energy Limited (a principal subsidiary of Capricorn Oil Limited).

Additions during 2013 included US\$1,059.8m capital contribution by Cairn Energy PLC which reduced the amounts owed to the Company by Capricorn Oil Limited.

## 7.6 Investments in Subsidiaries – Continued

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. No impairments arose at the year end. At 31 December 2013 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\$336.7m was made to the Company's Income Statement.

## 7.7 Capital Management

Capital and net debt were made up as follows:

	2014 US\$m	2013 US\$m
Trade and other payables	68.4	19.8
Less cash and cash equivalents	(24.0)	(882.9)
Net debt	44.4	(863.1)
Equity	2,779.2	2,822.7
Capital and net debt	2,823.6	1,959.6
Gearing ratio	2%	0%

## 7.8 Related Party Transactions

The Company's principal subsidiaries are listed in appendix 1. The following table provides the Company's balances which are outstanding with subsidiary companies at the Balance Sheet date:

	2014 US\$m	2013 US\$m
Amounts receivable from subsidiary undertakings	-	307.8
Amounts payable to subsidiary undertakings	(57.6)	(4.2)
	(57.6)	303.6

The amounts outstanding are unsecured and repayable on demand and will be settled in cash.

During the year, the Company increased its investment in Capricorn Oil Limited through capitalisation of loan balances receivable from the subsidiary. See section 7.6 for further details.

The following table provides the Company's transactions with subsidiary companies recorded in the loss for the year:

	2014 US\$m	2013 US\$m
Amounts invoiced to subsidiaries	17.3	8.4
Amounts invoiced by subsidiaries	7.2	2.2
Dividend received from subsidiary	-	57.7

### 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 76 to 97.

	2014 US\$m	2013 US\$m
Emoluments	5.8	4.8
	5.8	4.8

Pension contributions were made on behalf of directors in 2014 of US\$0.4m (2013: US\$0.2m).

No share awards to directors vested during 2014 (2013: none).

### Other transactions

During the year the Company did not make any purchases in the ordinary course of business from an entity under common control (2013: US\$nil).

# Appendices to the Group and Company Financial Statements

## Appendix 1 – Principal Subsidiary Undertakings

The Company's principal subsidiaries as at the Balance Sheet date are set out below. A full list of subsidiaries can be found on the Annual Return. The Company holds 100% of the voting rights and ordinary shares of the following companies:

	Principal activity	Country of incorporation	Country of operation
<b>Direct holdings</b>			
Capricorn Oil Limited	Holding company	Scotland	Scotland
Cairn UK Holdings Limited	Holding company	Scotland	Scotland
<b>Indirect holdings – Capricorn Oil Limited Group</b>			
Capricorn Energy Limited	Holding company	Scotland	Scotland
Capricorn Spain Limited	Exploration	Scotland	Spain
Capricorn Malta Limited	Exploration	Scotland	Malta
Capricorn Greenland Exploration A/S	Exploration	Greenland	Greenland
Capricorn Exploration and Development Company Limited	Exploration	Scotland	Morocco
Capricorn Mauritania Limited	Exploration	Scotland	Mauritania
Capricorn Senegal Limited	Exploration	Scotland	Senegal
Capricorn Ireland Limited	Exploration	Scotland	Republic of Ireland
Capricorn Norge AS	Exploration	Norway	Norway
Nautical Petroleum Limited	Exploration	England	UK
Nautical Petroleum AG	Exploration and development	Switzerland	UK
Agora Oil and Gas (UK) Limited	Exploration	Scotland	UK

## Appendix 2 – Financial Risk Management: Objectives and Policies

### Group and Company

The main risks arising from the Company's and the Group's financial instruments are liquidity risk, credit risk, market risk arising from equity price fluctuations 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'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.

The primary financial assets and liabilities comprise cash, short and medium-term deposits, notice accounts, 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 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 significant financial headroom for the 12 months from the date of approval of the 2014 Annual Report and Accounts. Details of the Group's debt facilities can be found in section 3.2.

At 31 December 2013 Cairn Energy PLC Group had a total of US\$60.0m of facilities in place to cover the issue of performance guarantees. On 21 February 2014 the facilities were further increased to US\$100.0m. On 1 Aug 2014 these were cancelled and replaced by the US\$575.0m debt facility noted above.

The Group currently has surplus cash which is invested in a combination of money market liquidity funds, 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.

### Interest rate risk

Surplus funds are invested at floating rates. Borrowing arrangements are generally entered into at floating rates. From time to time the Group may opt to manage a proportion of the interest costs by using derivative financial instruments like interest rate swaps. At this time, however, there are no such instruments (2013: none).

The Group's loss before tax is not sensitive to changes in interest rates.

### Foreign currency risk

Cairn manages exposures that arise from non-functional currency receipts and payments by matching receipts and payments in the same currency and actively managing the residual net position. Generally the exposure has been limited given that receipts and payments have mostly been in US dollars and the functional currency of most companies in the Group is US dollars.

The Group also aims where possible to hold surplus cash, debt and working capital balances in functional currency which in most cases is US dollars, thereby matching the reporting currency and functional currency of most companies in the Group. This minimises the impact of foreign exchange movements on the Group's Balance Sheet.

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 exchange rates, with all other variables held constant, on the Group's and the Company's monetary assets and liabilities. The Group's and the Company's exposure to foreign currency changes for all other currencies is not material.

	2014		2013	
	Effect on loss before tax US\$m	Effect on Equity US\$m	Effect on loss before tax US\$m	Effect on Equity US\$m
<b>Group</b>				
10% increase in Sterling to US\$	28.3	80.1	9.2	41.4
10% decrease in Sterling to US\$	(28.3)	(80.1)	(9.2)	(41.4)
	2014		2013	
	Effect on loss before tax US\$m	Effect on Equity US\$m	Effect on loss before tax US\$m	Effect on Equity US\$m
<b>Company</b>				
10% increase in Sterling to US\$	89.8	89.8	93.5	93.5
10% decrease in Sterling to US\$	(89.8)	(89.8)	(93.5)	(93.5)



# Appendices to the Group and Company Financial Statements continued

## Appendix 2 – Financial Risk Management: Objectives and Policies – Continued

### 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 and maturity 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. 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 2014 the Group had investments with 22 counterparties (2013: 33) to ensure no concentration of counterparty investment risk. The maturity of these investments ranged from instant access to three months.

The maximum credit risk exposure relating to financial assets is represented by the carrying value as at the Balance Sheet date.

### Market risk: equity price risk

The Group is exposed to equity price risks arising from the listed equity investments it holds in Cairn India Limited. Equity investments are held for strategic rather than trading purposes and the Group does not actively trade these investments, which are classified as non-current available-for-sale financial assets.

Movements in the fair value during the year are recognised directly in equity and are disclosed in the Statement of Comprehensive Income. The cumulative gain or loss that arises on disposal of available-for-sale financial assets is recycled through the Income Statement.

Further details on the impact of equity price movements on the fair value of the available-for-sale financial assets are included in section 3.1.

Appendix 3 – Share-based Payments

Cairn Energy PLC Group and Company

The schemes below apply for both Group and Company.

Cairn Energy PLC share options were exercised on a regular basis throughout the year, subject to the normal employee dealing bans imposed at certain times by the Company. The weighted average share price during the year was £1.877 (2013: £2.753).

The Cairn Energy PLC share awards during 2014 were valued using a Monte Carlo model with the exception of the SIP awards which were valued using a Black-Scholes model. Awards in prior years were valued using a Monte Carlo model.

The main inputs to the models include the number of options, share price, leaver rate, trigger points, discount rate and volatility.

- Leaver rate assumptions are based on past history of employees leaving the Company prior to options vesting and are revised to equal the number of options that ultimately vest.
- Trigger points are based on the length of time after the vesting periods for awards in 2014. Awards in prior years have trigger points based on the profit points at which the relevant percentage of employees are assumed to exercise their options.
- The risk-free rate is based on the yield on a zero coupon Government bond with a term equal to the expected term on the option being valued.
- Volatility was determined as the annualised standard deviation of the continuously compounded rates of return on the shares of a peer group of similar companies selected from the FTSE, as disclosed in the Directors' Remuneration report on pages 76 to 97, over a 10-year period to the date of award.

The following assumptions and inputs apply to the share plans detailed in section 5.4:

Scheme name	Volatility	Risk-free rate per annum	Lapse due to withdrawals per annum
2010 Share Incentive Plan	29% – 52%	0% – 0.69%	5%
2009 Approved and Unapproved Plans	29% – 52%	0.29% – 3.20%	5%
2009 LTIP	29% – 52%	0% – 2.33%	0%
2012 Share awards	29% – 52%	–	5%

Employee exercise trigger point assumptions

For 2014 awards, the assumption used for the 2009 Approved and Unapproved awards is that employees will exercise half of the awards on the vesting date and the remaining half will be exercised equally each year over the following seven years. This assumption is modified for the 2009 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. The assumption used for the valuation of the SIP is that employees will withdraw shares five years after the award date.

For details on the vesting conditions attached to the LTIPs refer to the Directors' Remuneration report on pages 76 to 97.

Appendices to the Group and Company Financial Statements continued

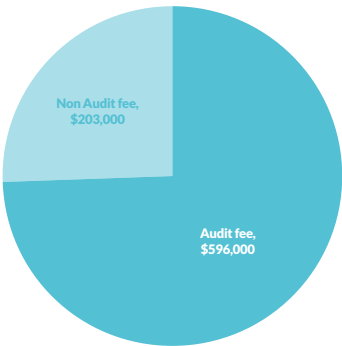
Appendix 4 – Auditors’ Remuneration

	2014 US\$'000	2013 US\$'000
<b>PwC LLP</b>		
Fees payable to the Group's auditors and its associate firms for:		
Audit of parent company and consolidated Financial Statements	346	246
Audit of Group companies pursuant to legislation	250	139
Tax advisory and other services	203	13
<b>Ernst &amp; Young LLP</b>		
Fees payable to the Group's auditors and its associate firms for:		
Audit of parent company and consolidated Financial Statements	-	86
Audit of Group companies pursuant to legislation	-	258
Tax advisory and other services	-	66

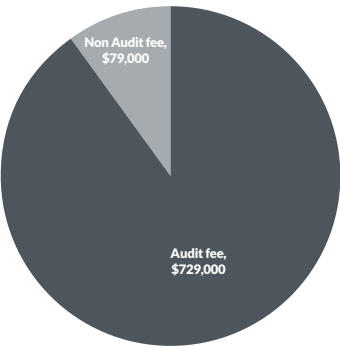
The Group has a policy in place for the award of non-audit work to the auditors which, in certain circumstances, requires Audit Committee approval (see the Audit Committee report on pages 73 to 75).

The split of audit fees to non-audit fees payable to the auditor is as follows:

2014 Fees to Auditors



2013 Fees to Auditors



## Group booked reserves and resources

A total of 56.1 mmboe were booked as 2P Reserves and 171.6 mmboe as 2C Resources at 31 December 2014 on a net working basis.

Net 2P Reserves	31.12.13 mmboe	Revisions mmboe	Discoveries & Extensions mmboe	Acquisitions & Disposals mmboe	Production mmboe	31.12.14 mmboe
UK	30.1	26.1	–	–	(0.0)	56.1
<b>Totals</b>	<b>30.1</b>	<b>26.1</b>	<b>–</b>	<b>–</b>	<b>(0.0)</b>	<b>56.1</b>
Net 2C Contingent Resources						
UK	33.7	(32.5)	–	–	–	1.1
Ireland	23.4	–	–	–	–	23.4
Norway	23.0	0.5	–	3.4	–	26.9
Senegal	–	–	120.1	–	–	120.1
<b>Totals</b>	<b>80.1</b>	<b>(32.0)</b>	<b>120.1</b>	<b>3.4</b>	<b>–</b>	<b>171.6</b>

- 2P Reserves increased by 26.0 mmboe during 2014 due to the Catcher project FDP approval.
- 2C Resources increased by 91.5 mmmboe during 2014 due to Senegal and promotion of Catcher Resources to Reserves.
- All 2P bookings are supported by independent Competent Persons Reports.
- In January 2015 Cairn completed the sale of a 10% interest in the Catcher development to Dyas UK Limited; this sale is not reflected in the reserves disclosed above.

# Licence list

As at 31 December 2014

Country	Asset Name	Block/Licence	Operator	Cairn Interest (%)
Atlantic Margin				
Morocco	FOUM DRAA OFFSHORE 1, 2 AND 3	Foum Draa	Cairn	50
Morocco	JUBY MARITIME I, II AND III	Juby Maritime	Cairn	37.5
Morocco	CAP BOUJDOUR I – XV	Cap Boujdour	Kosmos	20
Mauritania	C-19	PSC C-19	Chariot	35
Senegal	RUFISQUE OFFSHORE, SANGOMAR OFFSHORE AND SANGOMAR DEEP OFFSHORE	Sangomar-Rufisque	Cairn	40
Greenland	ATAMMIK	2002/15	Cairn	87.5
Greenland	EQQUA	2008/11	Cairn	87.5
Greenland	LADY FRANKLIN	2005/06	Cairn	87.5
Greenland	PITU	2011/13	Cairn	87.5
Republic of Ireland	SPANISH POINT	FEL 2/04 (Blocks 35/8, 35/9)	Cairn	38
Republic of Ireland	SPANISH POINT NORTH	FEL 4/08 (Blocks 35/2b, 35/3b, 35/4a)	Cairn	38
Republic of Ireland	FEL 1/14	FEL 1/14 (Blocks 35/13, 35/14, 35/15 (p), 35/18, 35/19)	Cairn	38
Mediterranean				
Spain	ALTA MAR 1	Alta Mar	Cairn	100
Spain	ALTA MAR 2	Alta Mar	Cairn	100
Spain	BENIFAYO	Albufera-Benifayo-Gandia	Cairn	100
Spain	GANDIA	Albufera-Benifayo-Gandia	Cairn	100
France	ST LAURENT	Saint Laurent (Block P566)	eCORP	22
France	GEX	GEX	eCORP	20
Malta	BLOCKS 1, 2 and 3	Area 03	Cairn	60
North West Europe				
UK	PEDL203	PEDL203 (Block SK/65b)	Egdon	15
UK	PEDL118	PEDL118 (Blocks SK/65c, SK/66d)	Egdon	15
UK	PEDL005	PEDL005 (Blocks TF/38b and TF/49b)	Egdon	10
UK	P218	P218 (Block 15/21a Gamma)	Premier	21
UK	P1763	P1763 (Blocks 9/9d, 9/14a, 9/15d)	MPX North Sea	32.5
UK	P1463	P1463 (Block 14/30a)	Premier	20
UK	P1077	P1077 (Block 9/2b ALL)	EnQuest	25

Country	Asset Name	Block/Licence	Operator	Cairn Interest (%)
<b>UK</b>	P2040	P2040 (Block 29/11)	Premier	20 (see Notes 4 and 5)
<b>UK</b>	P2124	P2124 (Block 113/22a)	Serica	10
<b>UK</b>	P2086	P2086 (Blocks 28/9b, 28/14)	Premier	20 (see Notes 4 and 5)
<b>UK</b>	P1995	P1995 (Blocks 210/25b, 211/21b, 211/26b)	TAQA	50
<b>UK</b>	P2070	P2070 (Block 28/4a)	Premier	46 (see Note 4)
<b>UK</b>	P2077	P2077 (Block 28/8)	Premier	46 (see Note 4)
<b>UK</b>	P1430	P1430 (Blocks 28/9a, 28/10c)	Premier	30 (see Note 4)
<b>UK</b>	P1655	P1655 (Block 15/21g)	Premier	21
<b>UK</b>	P1976	P1976 (Blocks 8/5, 9/1b)	EnQuest	40
<b>UK</b>	P1991	P1991 (Block 14/30c)	Endeavour	20
<b>UK</b>	P1659	P1659 (Block 20/7a)	Nexen	19
<b>UK</b>	P1887	P1887 (Blocks 12/16b and 12/17b)	First Oil	26.67
<b>UK</b>	P1482	P1482 (Blocks 113/26b, 113/27c)	Hydrocarbon Resources Ltd (Centrica)	10
<b>Norway</b>	PL159C	PL159C (Block 6507/3a)	Statoil	18
<b>Norway</b>	PL393B	PL393B (Blocks 7125/4c, 7125/5b)	Statoil	25
<b>Norway</b>	PL248C	PL248C (Blocks 35/11g, 35/11h)	Statoil	20
<b>Norway</b>	PL378	PL378 (Block 35/12a)	Wintershall	20
<b>Norway</b>	PL378B	PL378B (Block 35/12b)	Wintershall	20
<b>Norway</b>	PL418	PL418 (Blocks 35/8f, 35/9e)	Wintershall	20
<b>Norway</b>	PL630	PL630 (Blocks 35/10b, 31/1b)	Statoil	20
<b>Norway</b>	PL665S	PL665S (Blocks 2/2d, 2/3b, 3/1a)	Faroe Petroleum	20
<b>Norway</b>	PL632	PL632 (Block 33/9c)	Statoil	40
<b>Norway</b>	PL748	PL748 (Blocks 34/2, 34/5)	DNO	20
<b>Norway</b>	PL682	PL682 (Block 35/9b)	Bayerngas	10
<b>Norway</b>	PL758	PL758 (Blocks 6508/1, 6608/10, 6608/11)	EnQuest	35
<b>Norway</b>	PL747	PL747 (Block 35/8)	Bayerngas	40
<b>Norway</b>	PL420	PL420 (Block 35/9d)	RWE Dea Norge AS	20



# Licence list

As at 31 December 2014 – continued

Country	Asset Name	Block/Licence	Operator	Cairn Interest (%)
Asia Pacific				
Nepal	KARNALI AND DHANGARI	Petroleum Agr. 1 (Blocks 1 and 2)	Cairn	100
Nepal	LUMBINI, BIRGANJ AND MALANGAWA	Petroleum Agr. 2 (Blocks 4, 6 and 7)	Cairn	100

Notes:

1. Cairn has issued surrender notices in respect of Greenland Licences 2011/16, 2011/17, 2008/14, 2009/11, 2008/13, 2009/10 and 2008/10.
2. Cairn has received four new licences in the 28th Seaward Licensing Round in the UKCS (P2184, P2149, P2148 and P2918).
3. Cairn has issued surrender notices in respect of UKCS Licences P1633 and P1887.
4. Cairn has completed a transfer of a 10% interest in Licences P1430, P2040, P2070, P2077 and P2086 to Dyas UK Limited. The transfer took place on 20 January 2015 with an effective economic date of 1 January 2014.
6. Cairn has agreed to transfer its interest in Licences P2040 and P2086 to Statoil. This transfer is conditional on the usual third party approvals.

## Glossary

The following are the main terms and abbreviations used in this report:

### Corporate

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
Company	Cairn Energy PLC
CR	Corporate Responsibility
CRMS	Corporate Responsibility Management System
ELT	Exploration Leadership Team
Group	the Company and its subsidiaries
RMC	Risk Management Committee
SLT	Senior Leadership Team

### Other

2C	best estimate of contingent resources
2D/3D	two dimensional/three dimensional
2P	proven plus probable
ABC	anti-bribery and corruption
ALARP	as low as reasonably practicable
APA	awards in predefined area
bbl	barrel
boe	barrel(s) of oil equivalent
boepd	barrel(s) of oil equivalent per day
BOP	blow out preventer
bopd	barrels of oil per day
DC	drill centre
DECC	Department of Energy and Climate Change
DEFRA	Department for Environment Food & Rural Affairs
E&P	exploration and production
EAA	environmental area assessment
ESA	exploration study agreement
EIA	Environmental Impact Assessment
EITI	Extractive Industries Transparency Initiative
ESIA	Environmental and Social Impact Assessment
FDP	field development plan
FEED	front end engineering design
FEL	frontier exploration licence
FID	final investment decision
FPSO	floating production, storage and offloading
GHGs	Greenhouse gases
GMT	Greenwich Mean Time
GRI	Global Reporting Initiative
HSE	Health, safety and environment
IFRS	International Financial Reporting Standards
IOGP	International Association of Oil & Gas Producers
JV	Joint Venture (referring to industry term, not IFRS definition)
KPI	Key Performance Indicator
LPI	leading performance indicator
LTI	lost time incident/injury
LTIF	lost time injury frequency
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
NCS	Norwegian Continental Shelf
ONHYM	Office National des Hydrocarbures et des Mines
PCDP	Public Consultation and Disclosure Plan
PDP	Project Delivery Process
Q1/2/3/4	quarter 1/2/3/4
STOIIP	stock-tank oil initially in place
TRIR	total recordable injuries rate
TD	target depth
TVDSS	total vertical depth sub sea
UKCS	UK Continental Shelf
US\$	US dollar
WEC	well engineering and construction
WI	working interest

Notes

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These materials contain forward-looking statements regarding Cairn, our corporate plans, future financial condition, future results of operations, future business plans and strategies. All such forward-looking statements are based on our management's assumptions and beliefs in the light of information available to them at this time. These forward-looking statements are, by their nature, subject to significant risks and uncertainties and actual results, performance and achievements may be materially different from those expressed in such statements. Factors that may cause actual results, performance or achievements to differ from expectations include, but are not limited to, regulatory changes, future levels of industry product supply, demand and pricing, weather and weather-related impacts, wars and acts of terrorism, development and use of technology, acts of competitors and other changes to business conditions. Cairn undertakes no obligation to revise any such forward-looking statements to reflect any changes in Cairn's expectations with regard thereto or any change in circumstances or events after the date hereof.





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