



Red Sky Energy Limited

ANNUAL REPORT

FOR THE YEAR ENDED 31 DECEMBER 2011

ABN 94 099 116 275

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CORPORATE DIRECTORY

Chairman	Mr Gerrit de Nys
Managing Director	Mr Rohan Gillespie
Non Executive Director	Mr Guy Le Page
Non Executive Director	Mr Murray Durham
Company Secretary	Mr Adrien Wing
Registered & Principal Office	Level 17, 500 Collins Street Melbourne VIC 3000
Postal Address	Level 17, 500 Collins Street Melbourne VIC 3000
Auditors	RSM Bird Cameron Partners Level 8, Rialto Sth Tower 525 Collins Street Melbourne VIC 3000
Solicitors	Quinert Rodda and Associates Level 19, 500 Collins Street Melbourne VIC 3000
Website Address	www.redskyenergy.com.au
Stock Exchange Listings	Red Sky Energy Ltd shares are listed on the Australian Securities Exchange under the code ROG
Share Registry	Advanced Share Registry Services 150 Striling Highway Nedland WA 6009 Telephone: + 61 8 9369 8033 Facsimile: +61 8 9389 7871

CHAIRMAN'S LETTER

Dear Shareholders,

It has been a frustrating year for Red Sky Energy. By any measure the Company had a very successful two well exploration program in the Clarence Moreton Basin in north east New South Wales. A major new discovery was made in the shallow Kangaroo Creek Sandstones. In addition substantial coal seam gas reserves and resources were independently certified. However the value of these resources failed to show in the Company's share price. In the Board's view there are two main reasons for this; the highly volatile share market and the adverse publicity that coal seam gas has attracted.

This year the share market has seen a large number of investors cash out their holdings for placing in term deposits. It is hoped the situation starts to reflect fundamentals soon. In the case of natural gas resources in Eastern Australia, the fundamentals are very strong. The emergence of five major LNG projects in Gladstone has created a huge new gas market, as well as a high price gas market because LNG contracts are linked to the global oil price. This means domestic gas prices are likely to rise strongly over the next few years. Some people are expecting gas prices to rise from about \$5/GJ now to over \$10/GJ assuming the oil price stays above or at current levels.

This year we have also seen more consolidation, with Eastern Star Gas being acquired by Santos and Bow Energy being acquired by Arrow Energy (Shell). This is good news for Red Sky. It is evidence that the major companies developing the Gladstone LNG projects are seeking more gas for further expansion. This also means that gas is scarce for power companies looking to develop new gas fired power stations. Red Sky's resources are well positioned to supply into the eastern Australia gas market.

The adverse publicity that coal seam gas has attracted has had a significant impact on the Company. Permitting for new wells requires far more upfront planning, consultation and reporting of potential impacts, which adds to the cost of doing business and significantly increases the time to have work programs approved. Red Sky's view is the industry produces minimal impacts on the environment, has been adequately regulated to date and new regulatory measures add no value. However Red Sky is prepared to work with the current arrangements as long as they provide a stable framework within which to do business.

Red Sky is in the process of securing regulatory approvals for the proposed Talma pilot, to test the prospectivity of the Kangaroo Creek sandstone gas resource, and is excited about the potential results. We see this as a stepping stone to adding value to the Company and being able to further explore and appraise our high quality tenements.

Gerrit J de Nys
Non-Executive Chairman

REVIEW OF OPERATIONS

Summary

- The Company drilled two very successful exploration wells in the Clarence Moreton Basin in north east NSW, with resulting substantial independent reserves and resources certified in the Walloon coals.
- Coal seam gas resource within the Walloon coals comprises multiple coal seams over an interval of up to 300 metres.
- One of the wells was the discovery well for a shallow gas resource within the Kangaroo Creek Sandstone. Analysis of core taken and expert advice concluded the resource could be substantive (laterally extensive, thick sandstones) and flow to surface from high permeability streaks in the bedding planes.
- The Company strategy shifted to a focus on near term production with the discovery of the highly prospective Kangaroo Creek sandstone gas resource. A single pilot is proposed to appraise the resource, and regulatory approvals are pending.
- A number of non-core permits were relinquished.
- A capital raising was undertaken to fund permitting and well rehabilitation costs.

Corporate

The Company raised \$1.44m via a placement in May 2011.

In addition, an equity line of credit for \$3m was put in place in September 2011 with YA Global.

Operational Overview

Clarence Moreton Project

This project encompasses the permits PEL 479, 457, 478 in the Clarence Moreton Basin north east NSW. In late 2010 and early 2011, Red Sky drilled two exploration core holes; Annvale and Talma. Both wells targeted the coal seam gas resource within the Walloon coals.

The wells intersected 23.5m across 29 seams within the interval 630m to 800m depth at Talma, and 19.4m across 23 seams within the interval 670m to 900m depth at Annvale. The coal seams have good gas contents of 5m³/t raw gas contents and 15m³/t dry ash free. Notably the Talma gas contained 25% ethane, which indicates the high rank and thermal maturity of the coal seams.

Subsequently in March 2011, Red Sky announced independently certified reserves and resources (100% basis) of:

Probable Reserves	2P	17PJ
Possible Reserves	3P	380PJ
Contingent Resources	2C	629PJ

With the drilling of the two wells, Red Sky earned a 30% interest in each of PEL 479 and 457, and hence 30% of the above significant reserves and resources.

During drilling of the Talma 1 well, a discovery of gas in the Kangaroo Creek sandstones was made. An 83 metre section of core was taken and has been analysed. The discovery is considered highly prospective because the sandstones:

- Are laterally extensive within the Clarence Moreton Basin
- Are gassy in the depth interval from 480 metres to 563 metres
- Have an estimated gross pay of 83 metres
- Have scope for significant increase in gross pay above 480 metre level
- Could flow gas to surface un-stimulated at rates that could be economic.

Red Sky decided the most effective and low cost method of appraisal of this discovery is via the proposed Talma Pilot. Subsequently the Company submitted an application for regulatory approval of the Talma pilot well. This was in the form of a Review of Environmental Factors (REF) document totalling 110 pages. The REF was comprehensive and included extensive stakeholder consultation and a rigorous assessment of impacts. The concluded impacts can be adequately managed.

The NSW Department of Trade and Investment, Resources and Energy requested additional information in the REF document and a revised application was submitted. The Department again requested further information and the approval is now expected in April 2012.

The Company announced the significance of its reserves in the context of the overall gas market:

- Red Sky Energy has 114 PJ of 3P reserves in the Clarence Moreton Basin in north east NSW;
- This is the fifth largest amongst non-major companies with gas in eastern Australia;
- The proposed Talma pilot well is expected to add to this reserves position;
- The Company aims to position itself as a major supply source.

Red Sky's reserves in the Clarence Moreton Basin put the Company in the top five on a 3P basis, as is highlighted in the below table.

Company	3P Gas Reserves*
Metgasco	2,542 PJ
Molopo	817 PJ
Westside	369 PJ
Senex	249 PJ
Red Sky	114 PJ
Dart Energy	102 PJ
Blue Energy	39 PJ

*Source: Reserves numbers taken from publicly released information from each company.

Yaraka Project

This project encompasses the permit ATP 946 in western Queensland. A farm-in with Resolve Geo gives Red Sky the right to earn up to a 100% interest in phases.

The permit is large (approx 7650km²) and potentially contains a significant resource of Cretaceous age coal of the Winton Formation. These coals were discovered by previous petroleum wells within the permit, as well as to the east in EPC 1149 by East Energy Resources and abutting the south west corner of ATP 946 by Bow Energy in ATP 794.

Assuming an average coal thickness across the permit of 8 metres, there is a potential 95 billion tonnes present. Given the low rank of the coal, the primary play is biogenic gas. If the coals are found to be fully gas saturated, gas contents would be approximately 3m³/tonne of coal.

The permit was granted on 16th March 2011. No work has been undertaken during the year.

Taroom Trough Project

This project encompasses the permit ATP 840 in southern Queensland. Through a farm-in with Clark Oil and Gas (Operator), Red Sky has a 25% interest in the non-conventional resources. The joint venture partners recently unitized their interests across both conventional and non-conventional. Red Sky now has a 18.75% interest across conventional and non-conventional resources within ATP 840.

Two formations within ATP 840 are considered prospective for gas; the Triassic Rewan Formation and the Permian Tinowon Formation which have a thickness up to 600 metres and are found in the depth range of 2800 metres to 4000 metres. Resource gas-in-place volumes are estimated to be 48 TCF with a 10% recovery factor.

There have been gas flows from both these formations in wells drilled around ATP 840, including Kinkabilla, Overston and Cabawin, with the latter flowing 200,000 cubic feet per day (cfd) based on 1960s drilling technology. Well flow rates with the latest stimulation and horizontal drilling techniques could be substantially greater than this amount.

Unconventional gas, which includes basin centred gas, contributes half of all gas production in the contiguous 48 states of USA. The Piceance Basin and other areas in the USA have analogous plays to those identified in ATP 840. The Piceance Basin, which is thought to contain in excess of 200 TCF, produced 360 PJ of basin centred gas in 2009 from 4800 wells. A basin-centred gas system is typically described as a regionally extensive gas accumulation situated in the central, deeper parts of a basin. This is where ATP 840 sits in the Surat Basin. Reservoir rocks are typically low porosity, low permeability discontinuous sandstones, with no obvious structural closures or stratigraphic traps, as is the case with conventional gas. Average flow rates per well in the USA are around 800,000cfd, with some wells in excess of 13 million cfd with stimulation. ATP 840 is in the heart of the Surat Basin and is well located as a supply option to the proposed LNG projects for Gladstone. Should a gas resource be defined and developed, it could be connected to proposed major gas pipelines which are within 70kms of the permit.

The Operator undertook technical study work during the year as part of the fifth year work commitments. Also a renewal application has been submitted, with the intention to bring in a farm-in partner to fund testing of the prospective basin centred gas play.

Methane Enhancement Technology

In March 2010, Red Sky announced the signing of a term sheet with Enhanced Biogenic Methane Limited for application of emerging biogenic methane enhancement technology. Subsequently Red Sky was unable to find a suitable site for a demonstration project and the term sheet has lapsed.

CORPORATE GOVERNANCE

COMPLIANCE WITH ASX CORPORATE GOVERNANCE RECOMMENDATIONS

Introduction

Red Sky Energy Ltd ("Company") has adopted systems of control and accountability as the basis for the administration of corporate governance. These policies and procedures are summarised below.

Corporate governance is the system by which companies are directed and managed. It influences how the objectives of the Company are achieved, how risk is monitored and assessed and how performance is optimised.

The Board and management are committed to corporate governance and, to the extent that they are applicable to the Company, have adopted the Eight Essential Corporate Governance Principles as set out in the Corporate Governance Principles and Recommendation (2nd Edition) as published by the ASX Corporate Governance Council.

To obtain a copy of these principles please go to the ASX website
asx.com.au/documents/professionals/cg_principles_recommendations_with_2010_amendments.pdf

Whilst the Board has demonstrated, and continues to demonstrate, its commitment to best practice in corporate governance, it emphasises that good corporate governance is only one factor contributing to the success of the Company's operations.

Additional information about the Company's corporate governance practices is set out on the Company's website at www.redskyenergy.com.au.

The table below summarises the Company's compliance with the Corporate Governance Council's Recommendations:

Principle	ASX Corporate Governance Council Recommendations	Comply
1	Lay solid foundations for management and oversight	
1.1	Establish the functions reserved to the board and those delegated to senior executives and disclose those functions.	Yes
1.2	Disclose the process for evaluating the performance of senior executives.	Yes
1.3	Provide the information indicated in the Guide to reporting on principle 1.	Yes
2	Structure the Board to add value	
2.1	A majority of the board should be independent Directors.	Yes
2.2	The chair should be an independent director.	Yes
2.3	The roles of chair and chief executive officer should not be exercised by the same individual.	Yes
2.4	The board should establish a nomination committee.	Yes
2.5	Disclose the process for evaluating the performance of the board, its committees and individual Directors.	Yes
2.6	Provide the information indicated in the Guide to reporting on principle 2.	Yes
3	Promote ethical and responsible decision-making	
3.1	Establish a code of conduct and disclose the code or a summary as to:	Yes
	- the practices necessary to maintain confidence in the Company's integrity; - the practices necessary to take into account the Company's legal obligations and the reasonable expectations of its stakeholders; and - the responsibility and accountability of individuals for reporting and investigating reports of unethical practices.	
3.2	Establish a policy concerning diversity and disclose the policy or a summary of that policy which includes requirements for the board to establish measurable objectives for achieving gender diversity and for the board to assess annually the objectives and progress in achieving them.	No
3.3	Disclose annually the measurable objectives set for achieving gender diversity and progress towards achieving them.	No
3.4	Disclose annually the proportion of woman employees in the whole organization, women in senior executive positions and women on the board.	No
3.5	Provide the information indicated in the Guide to reporting on principle 3.	Yes
4	Safeguard integrity in financial reporting	
4.1	The board should establish an audit committee.	Yes
4.2	The audit committee should be structured so that it:	
	- consists only of non-executive Directors; - consists of a majority of independent Directors; - is chaired by an independent chair, who is not chair of the board; and - has at least three members.	No Yes Yes Yes

4.3	The audit committee should have a formal charter	Yes
4.4	Provide the information indicated in the Guide to reporting on principle 4.	Yes
5	Make timely and balanced disclosure	
5.1	Establish written policies designed to ensure compliance with ASX Listing Rule disclosure requirements and to ensure accountability at senior executive level for that compliance and disclose those policies or a summary of those policies.	Yes
5.2	Provide the information indicated in the Guide to reporting on principle 5.	Yes
6	Respect the rights of shareholders	
6.1	Design a communications policy for promoting effective communication with shareholders and encouraging their participation at general meetings and disclose the policy or a summary of that policy.	Yes
6.2	Provide the information indicated in the Guide to reporting on principle 6.	Yes
7	Recognise and manage risk	
7.1	Establish policies for the oversight and management of material business risks and disclose a summary of those policies.	Yes
7.2	The board should require management to design and implement the risk management and internal control system to manage the Company's material business risks and report to it on whether those risks are being managed effectively. The board should disclose that management has reported to it as to the effectiveness of the Company's management of its material business risks.	Yes
7.3	The board should disclose whether it had received assurance from the chief executive officer and the chief financial officer that the declaration provided in accordance with section 295A of the Corporations Act is founded on a sound system of risk management and internal control and that the system is operating effectively in all material respects in relation to financial reporting risks.	Yes
7.4	Provide the information indicated in the Guide to reporting on principle 7.	Yes
8	Remunerate fairly and responsibly	
8.1	The board should establish a remuneration committee.	Yes
8.2	The remuneration committee should be structured so that : - it consists of a majority of independent directors; - it is chaired by an independent director; - has at least three members.	Yes Yes No
8.3	Clearly distinguish the structure on non-executive Directors' remuneration from that of executive Directors and senior executives.	Yes
8.4	Provide the information indicated in the Guide to reporting on principle 8.	Yes

Council Principle 1: Lay solid foundations for management and oversight

1.1 Role of the Board

The Board's primary role is the protection and enhancement of medium to long term shareholder value. To fulfil this role, the Board is responsible for the overall Corporate Governance of the consolidated entity including its strategic direction, establishing goals for management and monitoring the achievement of these goals.

1.2 Responsibility of the Board

The Board is collectively responsible for promoting the success of the Company by:

- Supervising the Company's framework of control and accountability systems to enable risk to be assessed and managed;
- Ensuring the Company is properly managed;
- Approving and monitoring the progress of major capital expenditure, capital management, and acquisitions and divestitures;
- Approval of the annual budget;
- Monitoring the financial performance of the Company;
- Approving and monitoring financial and other reporting;
- Overall corporate governance of the Company, including conducting regular reviews of the balance of responsibilities within the Company to ensure division of functions remain appropriate to the needs of the Company;
- Liaising with the Company's external auditors as appropriate; and
- Monitoring, and ensuring compliance with, all of the Company's legal obligations, in particular those obligations relating to the environment, native title, cultural heritage and occupational health and safety.

The Board must convene regular meetings with such frequency as is sufficient to appropriately discharge its responsibilities. Between regular meetings it will also ensure that important matters are addressed by way of circular resolutions. The Board may, from time to time, delegate some of the responsibilities listed above to its senior management team.

1.3 Materiality threshold

The Board has agreed on both quantitative and qualitative guidelines for assessing the materiality of matters. Qualitative indications of materiality would include if:

- They impact on the reputation of the Company;
- They involve a breach of legislation;
- They are outside the ordinary course of business;
- They could affect the Company's rights to its assets; or
- If accumulated they would trigger the quantitative tests.

1.4 The Chairman

The chairman is responsible for leadership of the Board, for the efficient organisation and conduct of the Board's function and for the briefing of all directors in relation to issues arising at Board meetings. The chairman is also responsible for chairing shareholder meetings, and arranging Board performance evaluation.

1.5 The Managing Director

The managing director is responsible for running the affairs of the Company under delegated authority from the Board and to implement the policies and strategy set by the Board. In carrying out his/her responsibilities the managing director must report to the Board in a timely manner and ensure all reports to the Board present a true and fair view of the Company's financial condition and operational results.

1.6 Role and responsibility of management

The role of management is to support the managing director and implement the running of the general operations and financial business of the Company, in accordance with the delegated authority of the Board. Management is responsible for reporting all matters which fall within the Materiality Threshold at first instance to the managing director or if the matter concerns the managing director then directly to the chairman or the lead independent director, as appropriate.

1.7 Relationship of Board with management

Management of the day-to-day business of the Company is to be conducted by or under the supervision of the Board, and by those other officers and employees to whom the management function is properly delegated by the Board.

The Board will adopt appropriate structures and procedures to ensure that the Board functions independently of management. Appropriate procedures may involve the Board meeting on a regular basis without management present, or may involve expressly assigning the responsibility for administering the Board's relationship to management to a Committee of the Board.

Information is formally presented to the Board at Board meetings by way of Board reports and review of performance to date. When directors are providing information about opportunities for the Company, this should always be through the Board.

Council Principle 2: Structure the board to add value

The Company presently has three non-executive directors and one executive director. Three directors are independent in accordance with the terms of the ASX Corporate Governance Council's definition of an independent director. The Chairman (Mr Gerrit de Nys) is a non-executive and independent director in terms of the ASX Corporate Governance Council's definition of an independent director. The Board considers that its structure has been and continues to be appropriate in the context of the Company's current projects and operations. The Company considers that each director possesses skills and experience suitable for building the Company. The Board intends to reconsider its composition as the Company's operations evolve, and appoint directors as appropriate.

The full board of directors performs the role of the nomination committee.

Council Principle 3: Promote ethical and responsible decision-making

The Company complies with this recommendation other than with regard to the adoption of a diversity policy. The Company has adopted a code of conduct incorporating all corporate executives. It requires all business affairs to be conducted legally, ethically and with integrity. The code provides for reporting of breach of the code by others. The code of conduct has been made available on the Company's website.

The Board has prepared a draft diversity policy and currently is still taking advice with regard to a diversity policy prior to its adoption. The draft policy contemplates the recommendations of the Corporate Governance Council on diversity, which includes:

- requirements for the board to establish objectives for achieving gender diversity;
- the annual assessment and measurement of the company against these objectives;
- the annual disclosure of the measurement and progress in achieving the set objectives; and
- the disclosure of the proportion of women employed in the whole organization, women in senior executive positions and women on the board.

Currently there are no women in the organisation at any level. Other than the board members, there are no employees within the Company. The Company has a broad policy of "outsourcing" immediately. The formulation of a final policy will also contemplate these issues and how they affect the Company.

Council Principle 4: Safeguard integrity in financial reporting

The Company's Managing Director and Chief Financial Officer (or equivalent) report in writing to the Board that the consolidated financial statements of the Company and its controlled entities for each half and full year present a true and fair view, in all material aspects, of the Company's financial condition and operational results and are in accordance with accounting standards.

The Company has established an audit committee and the committee fulfills its role by:

- Monitoring the integrity of the financial statements of the Company, and reviewing significant financial reporting judgments.
- Reviewing the Company's internal financial control system and risk management systems.
- Reviewing the appointment of the external auditor and approving the remuneration and terms of engagement.
- Monitoring and reviewing the external auditor's independence, objectivity and effectiveness, taking into consideration relevant professional and regulatory requirements.

Council Principle 5: Make timely and balanced disclosure

Compliance procedures for ASX Listing Rule disclosure requirements have been adopted by the Company. It has appointed an officer of the Company to be responsible for compliance.

Council Principle 6: Respect the rights of shareholders

Information will be communicated to shareholders as follows:

- The annual report is distributed to all shareholders. The Board ensures that the annual report includes relevant information about the operations of the consolidated entity during the year, changes in the state of affairs of the consolidated entity and details of future developments, in addition to the other disclosures required by the Corporations Act. The annual report is made available on the Company's website, and is provided in hard copy format to any shareholder who requests it.
- The half-yearly report contains summarised financial information and a review of the operations of the consolidated entity during the year. The half-year audited financial report is prepared in accordance with the requirements of applicable Accounting Standards and the Corporations Act and is lodged with the Australian Securities Exchange. The half-yearly report is made available on the Company's website, and is sent to any shareholder who requests it.
- The quarterly report contains summarised cash flow financial information and details about the Company's activities during the quarter. The quarterly report is made available on the Company's website, and is sent to any shareholder who requests it.
- Proposed major changes in the consolidated entity which may impact on share ownership rights are submitted to a general meeting of shareholders.
- The Company's website is well promoted to shareholders and shareholders may register to receive updates, either by email or in hard copy.

The Board encourages full participation of shareholders at the Annual General Meeting to ensure a high level of accountability and identification with the consolidated entity's strategy and goals. Important issues are presented to the shareholders as resolutions.

The shareholders are requested to vote on the appointment and aggregate remuneration of directors, the granting of options and shares to directors and changes to the constitution. Copies of the constitution are available to any shareholder who requests it.

Company's website

The Company maintains a website at www.redskyenergy.com.au

On its website, the Company makes the following information available on a regular and up to date basis:

- Company announcements;
- latest information briefings;
- notices of meetings and explanatory materials; and
- quarterly, half yearly and annual reports.

The website is being continuously updated with any information the directors and management may feel is material. The Company also ensures that the audit partner attends the Annual General Meeting.

Council Principle 7: Recognise and manage risk

The Company has developed an initial framework for risk management and internal compliance and control systems which covers organisational, financial and operational aspects of the Company's affairs. The framework is the subject of ongoing review and yet to be finalised. It appoints the Managing Director and Company Secretary as being responsible for ensuring that the systems are maintained and complied with.

Council Principle 8: Remunerate fairly and responsibly

The Board has established a remuneration committee. The remuneration committee is responsible for administering the remuneration policy adopted by the Company and the remuneration arrangements for non executive Directors, executive Directors and executives of the Company.

DIRECTORS' REPORT

Your directors present their report consisting of Red Sky Energy Ltd (the Company) and Red Sky Energy Ltd and controlled entities (the Group) as at the end of, or during, the year ended 31 December 2011.

Directors

The following persons were directors of Red Sky Energy Ltd during the year and up to the date of this report:

Mr Gerrit de Nys – Non Executive Chairman
Mr Rohan Gillespie – Managing Director
Mr Murray Durham – Non Executive Director
Mr Guy Le Page – Non Executive Director

Mr Adrien Wing – Company Secretary - Appointed 3 February 2011
Mr Lloyd Flint – Company Secretary - Resigned 3 February 2011

Principal Activities

The Principal activity of the Group during the year was exploration for economic deposits of oil and gas. There have been no significant changes in the nature of these activities during the year.

Operating Results

The net operating loss of the Group for the year ended 31 December 2011 after income tax amounted to \$6,227,134 (31 December 2010: \$7,404,679).

Dividends Paid or Recommended

No dividend was paid or declared during the period and the Directors do not recommend the payment of a dividend.

Review of Operations

A detailed review of the Group's activities is contained in the Operations Review section of the Annual Report.

Significant changes in the state of affairs

During the year the company issued 191,395,605 fully paid ordinary shares. Refer to note 12 of this financial report for details.

Events Subsequent to Balance Sheet Date

In February 2012, a summary judgement decision in respect of a claim by a former drilling contractor, TDC Drilling Pty Ltd ("TDC"), was awarded against the Company's subsidiary Cydonia Resources Pty Ltd ("Cydonia"), however the decision provides for the summary judgement to be immediately stayed pending trial of a counterclaim against TDC by Cydonia or further orders.

The proceedings in the Supreme Court of Western Australia concern the Annvale No 1 well in PEL 479 in New South Wales. The decision was made in respect of a claim by TDC for \$205,792, liability for which was disputed by Cydonia. As the well was not completed to the satisfaction of the Board and costs were incurred with a replacement contractor in drilling the alternative Annvale No 2 well nearby, Cydonia considers it has a counterclaim against TDC substantially in excess of the amount of its invoice. The stay of the summary judgement as referred to above preserves Cydonia's ability to pursue its counterclaim which, if successful, would have the effect of completely eliminating the stayed judgement.

On 4 January 2012, 5,666,667 ordinary fully paid shares were issued for \$0.0065.
On 30 January 2012, 8,333,334 ordinary fully paid shares were issued for \$0.006.
On 17 February 2012, 6,250,000 ordinary fully paid shares were issued for \$0.007.
These shares were issued under the \$3m equity facility in place with YA Global.

Likely developments

The group will continue an active exploration focus while also reviewing and participating in technologies that have the capability to deliver higher and/or more efficient recoveries.

Environmental Issues

The Group's operations are subject to various environmental regulations under the Federal and State Laws in Australia. The majority of the Company's activities involve low level disturbance associated with its production facilities and exploration drilling programs. As at the date of this report the group complies fully with all such regulations.

The Group is subject to the reporting requirements of both the Energy Efficiency Opportunities Act 2006 and the National Greenhouse and Energy Reporting Act 2007.

The Energy Efficiency Opportunities Act 2006 requires the Group to assess its energy usage, including the identification, investigation and evaluation of energy saving opportunities, and to report publicly on the assessments undertaken, including what action the Group intends to take as a result.

The National Greenhouse and Energy Reporting Act 2007 requires the Group to report its annual greenhouse gas emissions and energy use. The first measurement period for this Act ran from 1 July 2008 to 31 December 2009. The Group is not in commercial production. No measurements have been recorded.

Information on Directors and Secretary

Names, qualifications, experience and special responsibilities of current directors and Company secretary:

Gerrit de Nys – Non Executive Chairman, B.Tech, FAICD, FIE Aust, CPEng(Ret.)

Mr de Nys is a Chartered Professional Engineer (Civil Engineering) and has had approximately 40 years experience in construction, contracting and development of businesses in Australia and overseas, having spent in excess of 30 years in Asia. He has been the CEO of a number of Asian based groups of companies involved in a broad range of industries including shipyards and heavy engineering as well as offshore construction activities. He is currently the Resident Director of the IMC Resources Australia Group of Companies.

Current Directorship and date of appointment:

Shui On Construction and Materials Ltd- Hong Kong (now SOCAM Development Ltd), director since 18/08/07, Horizon Oil Ltd- director since 14/07/07.

Other Directorships within the last three years:

Ashton Coal Mines Ltd.

Rohan Gillespie – Managing Director, BEng (Civil), MBA- University of Queensland

Mr Gillespie is Managing Director of Energy Infrastructure and Resources Limited ("EIR"). Mr Gillespie previously held senior roles with BHP Billiton in its engineering, coal and petroleum divisions, most recently as Vice President and Chief Operating Officer of its coal seam gas ("CSG") business. He has also held corporate development roles with two energy start-ups, Ceramic Fuel Cells and Renewable Energy Corp, as well as a credit executive role with Commonwealth Bank.

Current Directorship and date of appointment:

SOLEIR Limited (9/9/08), Energy Infrastructure and Resources Limited (13/7/05), Regal Resources Limited (16/6/09), Great Southern Gas Limited (22/2/08)

Other Directorships within the last three years:

Enhanced Biogenic Methane Limited, Pacific GTL Limited

Guy Le Page – Non Executive Director, B.A., B.Sc. (Adel), B.App.Sc. (Hons) (Curt), M.B.A.,(Adel) Grad. Dip. App. Fin & Inv. (FINSIA), MAusIMM, FFin

Mr Le Page is currently a Director & Corporate Adviser of RM Research and is actively involved in a range of corporate initiatives from mergers and acquisitions, initial public offerings to valuations, consulting and corporate advisory roles. Mr Le Page was Head of Research at Morgan Stockbroking Limited (Perth) prior to joining TolhurstNoall as a Corporate Advisor in July of 1998. As Head of Research, Mr Le Page was responsible for the supervision of all Industrial and Resources Research. As a Resources Analyst, Mr Le Page published detailed research on various mineral exploration and mining companies listed on the Australian Stock Exchange. The majority of this research involved valuations of both exploration and production assets. Prior to entering the stockbroking industry, he spent 10 years as an exploration and mining geologist in Australia, Canada and the United States. His experience spans gold and base metal exploration and mining geology, and he has acted as a consultant to private and public companies. This professional experience included the production of both technical and valuation reports for resource companies.

Mr Le Page holds a Bachelor of Arts, a Bachelor of Science and a Masters Degree in Business Administration from the University of Adelaide, a Bachelor of Applied Science (Hons) from the Curtin University of Technology and a Graduate Diploma in Applied Finance and Investment from the Financial Securities Institute of Australia.

Current Directorship and date of appointment:

Tasman Resources Ltd- director since February 2001, Fission Energy Ltd- director since 30/03/2006, Eden Energy Ltd- director since May 2004, Palace Resources Ltd- director since 07/08/2009; Soil Sub Technologies Ltd – director since 07/01/2010.

Other Directorships within the last three years:

Enerji Ltd (resigned 15/03/2010)
AAQ Holdings Ltd (director since 29 October 2010, resigned 14/03/2011)

Murray Durham- Non Executive Director, B. Sc. (Hons) Geol. UBC, Grad. Dip. FINSIA

Mr Durham's most recent role was Director - Oil and Gas marketing at Apache Energy where he was responsible for marketing Apache's crude oil and gas production in Australia and managing its many gas supply agreements. Prior to Apache, Mr Durham was Global Business Manager for the coal seam gas business at BHP Billiton. Mr Durham has extensive oil and gas exploration, pipeline industry, gas marketing and commercial experience, as well as a sound technical foundation as an exploration geologist with Shell Canada and BHP Billiton.

Current Directorships and date of appointment:

Durham Energy Consulting Pty Ltd – director since November 2009
Cady Energy Limited - director since November 2011

Other Directorships within the last three years:

Australian Pipeline Industry Association – director from October 2007 to October 2011

Roland Berzins – Non Executive Director, B.Comm, ACPA FFIN TA

Mr Berzins resigned on 25 May 2010.

Adrien Wing - Company Secretary, B.Acc, CPA

Mr Wing was appointed on 3 February 2011. Mr Wing is a Certified Practising Accountant qualified. He practiced in the audit and corporate divisions of a chartered accounting firm before working with a number of public companies listed on the Australian Securities Exchange as a corporate/accounting consultant and company secretary.

Current Directorships and date of appointment:

New Age Exploration Ltd – appointed 12 March 2004, Transol Corporation Ltd – appointed 5 May 2011.

Other Directorships within the last three years:

None

Lloyd Flint - Company Secretary, B.Acc, MBA, ICAA, FFin

Mr Flint resigned on 3 February 2011.

David Ballantyne - Company Secretary, MA (Hons) University of Edinburgh, ACA

Mr Ballantyne resigned on 25 May 2010.

Meetings of Directors

The number of meetings held by the Company's board of directors during the year and the number of meeting attended by each director were:

Director	Board meetings held	Board meetings attended
Gerrit de Nys	12	12
Rohan Gillespie	12	11
Murray Durham	12	12
Guy Le Page	12	12

During the year 12 board meetings were held by the Company which includes circular resolutions (which are deemed Board Meetings under the Company's constitution).

Securities held and controlled by Directors

As at the date of this report, the interests of the Directors in shares and options of the Company were:

Ordinary shares

Holder	Held at beginning of the year	Acquired	Disposed	Final interest	Balance at end of the year
Gerrit de Nys	1,000,000	3,000,000	-	-	4,000,000
Rohan Gillespie	180,000,000	-	-	-	180,000,000
Murray Durham	15,000,000	-	-	-	15,000,000
Guy Le Page	-	-	-	-	-

Options

Holder	Held at beginning of the year	Granted	Disposed	Final interest	Balance at end of the year
Gerrit de Nys	-	37,500,000	-	-	37,500,000
Rohan Gillespie	97,500,000	-	-	-	97,500,000
Murray Durham	-	7,500,000	-	-	7,500,000
Guy Le Page	-	15,000,000	-	-	15,000,000

At a meeting of shareholders held on 21 March 2011 the issue of 60,000,000 options to directors was approved. The options were issued free and are exercisable at 2.25 cents, expiring on 31 March 2016.

Remuneration Report (audited)

The information provided in this remuneration report has been audited as required by section 308(3C) of the Corporation Act 2001.

This report outlines the remuneration arrangements in place for Directors and executives of Red Sky Energy Limited. This report has been set out under the following main headings:

- A. Principles Used to Determine the Nature and Amount of Remuneration
- B. Service Agreements
- C. Details of Remuneration
- D. Share-based Compensation
- E. Additional Information

A. Principles Used to Determine the Nature and Amount of Remuneration

The Board of Directors is responsible for determining and reviewing compensation arrangements for the Directors and Executive Officers. The Board will assess the appropriateness of the nature and amount of emoluments of such officers on a periodic basis by reference to relevant employment market conditions with the overall objective of ensuring maximum stakeholder benefit from the retention of a high quality Board and executive team.

The objective of the Group's executive reward framework is to ensure reward for performance is competitive and appropriate for the results delivered. The framework aligns executive reward with achievement of strategic objectives and the creation of value for shareholders, and conforms to market best practice for delivery of reward. The Board ensures that executive reward satisfies the following key criteria for good reward governance practices:

- Competitiveness and reasonableness
- Acceptability to shareholders
- Performance linkage/alignment of executive compensation
- Transparency
- Capital management

The board policy is to remunerate non executive Directors at fair market rates for comparable companies for the relevant time, commitment and responsibilities. The board determines payments to the non-executive Directors and reviews their remuneration annually based on market practice, duties and accountability. The maximum amount of fees that can be paid to non executive Directors is subject to approval by shareholders at the Annual General Meeting. The maximum amount approved is \$250,000. Fees for non-executive Directors are not linked to the performance of the Group. However, to align Director's interests with shareholder interests the Directors are encouraged to hold shares in the Company and may be issued with additional securities as deemed appropriate.

The Board believes that the remuneration policy is appropriate given the stage of development of the Company and the activities which it undertakes and is appropriate for aligning Director and executive objectives with shareholder and business objectives. The board will continually develop new practices which are appropriate to the Company's size and stage of development.

Executive Officers are those directly accountable for the operational management and strategic direction of the Company and the consolidated entity. All contracts with Directors and executives may be terminated by either party with three months notice.

Fixed remuneration

Fixed remuneration consists of a base remuneration package, which includes Directors' fees (in the case of Directors), salaries, consulting fees and employer contributions to superannuation funds.

Fixed remuneration levels for Directors and executive officers will be reviewed annually by the board through a process that considers the employee's personal development, achievement of key performance objectives for the year, industry benchmarks wherever possible and CPI data.

Performance-linked remuneration

All employees may receive bonuses and/or share options based on achievement of specific goals related to performance against individual KPIs and to the performance of the Company as a whole as determined by the Directors, based on a range of factors. These factors include traditional financial considerations such as operating performance, cash consumption and deals concluded. They also include industry-specific factors relating to the advancement of the Company's activities and relationships with third parties and internal employees.

B. Service Agreements

The directors and key management personnel during the year included:

Directors

Mr Gerrit de Nys – Non Executive Chairman

- Agreement commenced 16/10/2009, no termination date;
- Consulting fees (including directors' fees) of \$80,000 to be reviewed annually by the board; and
- Payment of a termination benefit on early termination by the Company, other than for gross misconduct, equal to 3 months' consulting fees.

Mr Rohan Gillespie – Managing Director

- Agreement commenced 21/09/2009, no termination date;
- Consulting fees (including directors' fees) of \$250,000 plus 9% superannuation to be reviewed annually by the board; and
- Payment of a termination benefit on early termination by the Company, other than for gross misconduct, equal to 3 months' consulting fees.

Mr Murray Durham – Non Executive Director (effective 1 December 2010)

- Agreement commenced 18/01/2010 modified 1 December 2010, no termination date;
- Consulting fees (including directors' fees) of \$40,000 (\$220,000 prior to 1 December 2010) to be reviewed annually by the board;
- Payment of a termination benefit on early termination by the Company, other than for gross misconduct, equal to 3 months' consulting fees; and
- Modified during the prior year based on time available for director duties to \$40,000 p.a. as a non executive role, effective 1 December 2010.

Mr Guy Le Page – Non Executive Director

- Agreement commenced 18 February 2009, no termination date;
- Consulting fees (including directors' fees) of \$40,000 to be reviewed annually by the board; and
- Payment of a termination benefit on early termination by the Company, other than for gross misconduct, equal to 3 months' consulting fees.

Key Management Personnel Remuneration

Mr A Wing, Company Secretary

- The company has signed an agreement with Northern Star Nominees Pty Ltd for company secretarial services at a rate of \$5,500 per month.

Mr L Flint, former Company Secretary

- The company signed an agreement with GBU Capital Pty Ltd on 11/09/2009 for the management facility charges and consulting fees. The monthly invoice of \$20,000 included company secretarial charges (refer note 18). Three months Notice was given at the end of December 2010. Mr Flint resigned 3 February 2011.

C. Details of Remuneration

The key management personnel of Red Sky Energy Limited during the year ended 31 December 2011 included all directors and executives mentioned above. There are no other executives of the Company which are required to be discussed.

Remuneration packages contain the following key elements:

- Primary benefits – salary/fees and bonuses;
- Post-employment benefits – including superannuation;
- Equity – share options and other equity securities; and
- Other benefits.

Nature and amount of remuneration for the years ended 31 December 2011 and 2010:

2011		Short-term employee benefits	Post -employment benefits	Equity Performance related		
		Salary, consulting fees, director's fees \$	Superannuation \$	Options \$	Shares \$	Total \$
Executive directors						
R Gillespie		250,000	22,500	-	-	272,500
Non Executive directors						
G de Nys		85,077	7,800	450,000	-	542,877
G Le Page		40,000	-	180,000	-	220,000
M Durham		40,000	-	90,000	-	130,000
Total directors' compensation		415,077	30,300	720,000		1,165,377
Other key management personnel						
L Flint - (Company Secretary – resigned 03/02/11)		-	-	-	-	-
A Wing - (Company Secretary – appointed 03/02/11)		54,994	-	-	-	54,994
Total other key management compensation		54,994	-	-	-	54,994
TOTAL		470,071	30,300	720,000	-	1,220,371

2010		Short-term employee benefits	Post -employment benefits	Equity Performance related		
		Salary, consulting fees, director's fees \$	Superannuation \$	Options \$	Shares \$	Total \$
Executive directors						
R Gillespie		301,771	-	-	-	301,771
M Durham – (non executive effective 1/12/2010)		215,408	-	-	-	215,408
Non Executive directors						
G de Nys		80,000	7,200	-	-	87,200
G Le Page		38,000	-	-	-	38,000
R Berzins		13,016	-	-	-	13,016
Total directors' compensation		648,195	7,200	-	-	655,395
Other key management personnel						
D Ballantyne - (Company Secretary – resigned 25/5/10)		-	-	-	-	-
L Flint - (Company Secretary – appointed 25/5/10)		-	-	-	-	-
Total other key management compensation		-	-	-	-	-
TOTAL		648,195	7,200	-	-	655,395

D. Share-based Compensation

During the financial year ended 31 December 2011, there were options granted to directors as follows:

Directors	Granted	Grant Date	Vesting Date	Value at Grant Date	Exercise Price	Expiry Date
G de Nys	37,500,000	21 Mar 11	21 Mar 11	\$0.012	\$0.0225	31 Mar 16
M Durham	7,500,000	21 Mar 11	21 Mar 11	\$0.012	\$0.0225	31 Mar 16
G Le Page	15,000,000	21 Mar 11	21 Mar 11	\$0.012	\$0.0225	31 Mar 16
	60,000,000					

The fair value of the share options granted is estimated as at the date of grant using a Black Scholes model taking into account the terms and conditions upon which the options were granted. The model inputs used an expected volatility of 105%, a risk free rate of 5.19%, and a share price at the grant date of 1.6 cents.

During the year, the directors and their related entities received no other share based compensation.

E. Additional information

Principles used to determine the nature and amount of remuneration: relationship between remuneration and Company performance.

In considering the Company's performance and its effect on shareholder wealth, the Board has regard to a broad range of factors, some of which are financial and others of which relate to the progress on the Company's projects, results and progress of exploration and development activities, joint venture agreements, etc.

The Board also gives consideration to the Company's result and cash consumption for the year. It does not utilise earnings per share as a performance measure or contemplate payment of any dividends in the short to medium term given that all efforts are currently being expended to build the business and establish self-sustaining revenue streams.

END OF AUDITED REMUNERATION REPORT

INDEMNIFICATION AND INSURANCE OF DIRECTORS AND OFFICERS

During the financial year, the Company maintained an insurance policy which indemnifies the Directors and Officers of Red Sky Energy Limited in respect of any liability incurred in connection with the performance of their duties as Directors or Officers of the Company. The Company's insurers have prohibited disclosure of the amount of the premium payable and the level of indemnification under the insurance contract.

PROCEEDINGS ON BEHALF OF THE COMPANY

Refer above in the section describing events subsequent to balance sheet date for details of a current legal dispute.

No other person has applied to the Court under section 237 of the Corporations Act 2001 for leave to bring proceedings on behalf of the Company, or to intervene in any proceedings to which the Company is a party, for the purpose of taking responsibility on behalf of the Company for all or part of those proceedings.

No other proceedings have been brought or intervened in on behalf of the Company with leave of the court under section 237 of the Corporations Act 2001.

NON-AUDIT SERVICES

The Company may decide to employ the auditor on assignments additional to their statutory audit duties where the auditor's expertise and experience with the Company and/or the Group are important.

There were no non audit services provided during the year.

A copy of the auditor's independence declaration as required under section 307C of the Corporations Act 2001 is set out on page 19.

Auditor's Independence Declaration

Section 307C of the Corporations Act 2001 requires the consolidated entity's auditor, RSM Bird Cameron Partners to provide the directors with a written Independence Declaration in relation to their audit of the financial report for the period ended 31 December 2011. The written Auditor's Independence Declaration is attached to the Auditor's Independent Audit Report to the members and forms part of this Director's Report.

This report is made in accordance with a resolution of directors.

A handwritten signature in black ink, appearing to read 'R. Gillespie', is written over a faint, light blue rectangular background.

Rohan Gillespie
Managing Director
9 March 2012

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AUDITOR'S INDEPENDENCE DECLARATION

As lead auditor for the review of the financial report of Red Sky Energy Limited for the year ended 31 December 2011, I declare that, to the best of my knowledge and belief, there have been no contraventions of:

- (i) the auditor independence requirements of the *Corporations Act 2001* in relation to the review; and
- (ii) any applicable code of professional conduct in relation to the review.

Rsm Bird Cameron Partners
RSM BIRD CAMERON PARTNERS

Chartered Accountants

Jason Croall
J S CROALL
Partner

Dated: 9 March 2012
Melbourne, Victoria

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2011

		Group	
	Notes	2011 \$	2010 \$
Revenue from continuing operations	5	50,867	193,805
Administration expenses		(454,203)	(591,112)
Consultancy		(435,962)	(716,158)
Employee remuneration expense	6 (a)	(92,877)	(79,933)
Share based remuneration	6 (a)	(720,000)	-
Rehabilitation costs		(96,734)	-
Exploration costs written off	6 (b)	(4,478,225)	(6,211,281)
Loss from continuing activities before income tax		(6,227,134)	(7,404,679)
Income tax (expense)/benefit		-	-
Loss from continuing activities after income tax		(6,227,134)	(7,404,679)
Other comprehensive income		-	-
Total comprehensive loss for the year		(6,227,134)	(7,404,679)
Total comprehensive loss is attributable to:			
Equity holders of Red Sky Energy Ltd		(6,227,134)	(7,404,679)
Basic and diluted (loss) per share (cents per share)	15	(0.47)	(0.75)

The above consolidated statement of comprehensive income should be read in conjunction with the accompanying notes to the financial statements.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

As at 31 December 2011

		Group	
	Notes	2011 \$	2010 \$
Current Assets			
Cash and cash equivalents	8	612,676	2,668,158
Receivables	9	21,606	124,042
Other financial assets – tenement security deposits		71,000	226,000
Prepayments		40,202	-
Total current assets		745,484	3,018,200
Non Current Assets			
Exploration and evaluation assets	10	4,726,607	6,256,926
Total Non-Current Assets		4,726,607	6,256,926
Total Assets		5,472,091	9,275,126
Current Liabilities			
Trade and other payables		15,288	262,832
Accrued expenses		155,612	330,663
Total Current Liabilities		170,900	593,495
Total Liabilities		170,900	593,495
Net Assets		5,301,191	8,681,631
Equity			
Issued share capital	12	29,915,004	27,788,310
Reserves	13	1,458,000	738,000
Accumulated losses	14	(26,071,813)	(19,844,679)
Total Equity		5,301,191	8,681,631

The above consolidated statement of financial position should be read in conjunction with the accompanying notes to the financial statements.

CONSOLIDATED STATEMENT OF CASHFLOWS

For the year ended 31 December 2011

		Group	
	Notes	2011 \$	2010 \$
Cash flows from operating activities			
Payments to suppliers and staff		(845,086)	(1,332,750)
Interest received		50,088	193,805
Net cash (used in) operating activities	16	(794,998)	(6,177,152)
Cash flows from investing activities			
Exploration and evaluation expenditure		(2,742,178)	(5,038,207)
Deposits refunded		155,000	-
Net cash provided by (used in) investing activities		(2,587,178)	(5,038,207)
Cash flows from financing activities			
Proceeds from issues of shares		1,471,475	1,400,000
Capital raising costs		(144,781)	(103,690)
Net cash flows provided by financing activities		1,326,694	1,296,310
Net increase or decrease in cash and cash equivalents		(2,055,482)	(4,880,842)
Cash and cash equivalents at the beginning of the financial year		2,668,158	7,549,000
Cash and cash equivalents at the end of the financial year	8	612,676	2,668,158

The above consolidated statement of cash flows should be read in conjunction with the accompanying notes to the financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2011

Consolidated	2011			
	Issued Capital	Accumulated Losses	Option Reserve	Total Equity
Balance at beginning of year	27,788,310	(19,844,679)	738,000	8,681,631
Total comprehensive loss for the year	-	(6,227,134)	-	(6,227,134)
Total	27,788,310	(26,071,813)	738,000	2,454,497
Transactions with equity holders in their capacity as equity holders				
Issues of share capital	2,349,000	-	-	2,349,000
Equity raising costs	(222,306)	-	-	(222,306)
Share based remuneration	-	-	720,000	720,000
Balance at the end of the year	29,915,004	(26,071,813)	1,458,000	5,301,191
Consolidated	2010			
	Issued Capital	Accumulated Losses	Option Reserve	Total Equity
Balance at beginning of year	25,967,000	(12,440,000)	738,000	14,265,000
Total comprehensive loss for the year	-	(7,404,679)	-	(7,404,679)
Total	25,967,000	(19,844,679)	738,000	6,860,321
Transactions with equity holders in their capacity as equity holders				
Issues of share capital	1,925,000	-	-	1,925,000
Equity raising costs	(103,690)			(103,690)
Balance at the end of the year	27,788,310	(19,844,679)	738,000	8,681,631

The above consolidated statement of changes in equity should be read in conjunction with the accompanying notes to the financial statements.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies adopted in the preparation of the financial report are set out below. These policies have been consistently applied to all the year presented, unless otherwise stated. The financial report includes separate financial statements for Red Sky Energy Limited as an individual entity and the consolidated entity consisting of Red Sky Energy Limited and its subsidiaries.

(a) Basis of Preparation

The financial statements are a general purpose financial statement that have been prepared in accordance with Australian Accounting Standards, Australian Accounting Interpretations, other authoritative pronouncements of the Australian Accounting Standards Board (AASB) and the Corporations Act 2001.

Australian Accounting Standards set out accounting policies that the AASB has concluded would result in financial statements containing relevant and reliable information about transactions, events and conditions. Compliance with Australian Accounting Standards ensures that the financial statements and notes also comply with International Financial Reporting Standards. Material accounting policies adopted in the preparation of these financial statements are presented below and have been consistently applied unless otherwise stated.

The financial statements have been prepared on an accruals basis and are based on historical costs, modified, where applicable, by the measurement at fair value of selected non-current assets, financial assets and financial liabilities.

i) Compliance with IFRSs

Australian Accounting Standards include Australian Equivalents to International Financial Reporting Standards (AIFRSs). Compliance with AIFRSs ensures that the financial report of Red Sky Energy Limited comply with International Financial Reporting Standards (IFRSs).

ii) Early adoption of standards

The Group has not elected to apply any early pronouncements.

iii) Historical cost convention

These financial statements have been prepared under the historical cost convention, as modified by the revaluation of available-for-sale financial assets.

iv) Critical accounting estimates

The preparation of financial statements in conformity with AIFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Group's accounting policies (refer note 3).

v) Going Concern

The financial report has been prepared on the going concern basis, which contemplates the continuity of normal business activity and the realisation and settlement of liabilities in the normal course of business.

The consolidated entity incurred a loss of \$6.2m and had net cash outflows from operating activities of \$0.8m for the year ended 31 December 2011. Notwithstanding this, the Directors are satisfied that the consolidated entity will have sufficient cash resources to meet its working capital requirements in the future. They have reviewed the cashflow forecasts and believe that for a period in excess of 12 months from the date of signature of the financial report, the consolidated entity will be capable of meeting its minimum expenditure commitments and that it has the ability to meet its debts as and when they fall due. The Directors believe there are sufficient funding strategies and alternatives to meet working capital requirements should the need arise including:

- Utilisation of the \$3m equity facility available as detailed in note 12 to fund on-going expenditure;
- Other alternatives to issue securities and raise funds; and
- Consideration of re-arranging agreements on existing projects through sale or farming in a third party.

Based on the above, the Directors are of the opinion that the use of the going concern basis of accounting is appropriate.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(b) Principles of Consolidation

i) Subsidiaries

The consolidated financial statements incorporate the assets and liabilities of all subsidiaries of Red Sky Energy Limited ("Company" or "parent entity") as at 31 December 2011 and the results of all subsidiaries for the year then ended. Red Sky Energy Limited and its subsidiaries together are referred to in this financial report as the Group or the consolidated entity.

Subsidiaries are all those entities (including special purpose entities) over which the Group has the power to govern the financial and operating policies, generally accompanying a shareholding of more than one-half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity.

Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

Inter-Company transactions, balances and unrealised gains on transactions between Group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of the impairment of the asset transferred. Accounting policies of subsidiaries are consistent with the policies adopted by the Group.

Investments in subsidiaries are accounted for at cost in the individual financial statements of Red Sky Energy Limited.

ii) Jointly controlled assets and operations

Certain operations are carried out subject to joint venture arrangements. The proportionate interests in the assets, liabilities, income and expenditure of a joint venture activity have been incorporated in the financial statements under the appropriate headings.

The interest in a joint venture partnership is accounted for in the consolidated financial statements using the equity method and is carried at cost by the parent entity. Under the equity method, the share of the profits or losses of the partnership is recognised in the income statement, and the share of movements in reserves is recognised in reserves in the balance sheet.

(c) Segment reporting

The Group currently operates in the oil and gas industry segment in Australia.

(d) Revenue recognition

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the entity and the revenue can be reliably measured. Revenue is measured at the fair value of the consideration received or receivable. Amounts disclosed as revenue are net of returns, trade allowances and amounts collected on behalf of third parties. Revenue is recognised as follows:

(i) Interest income

Interest income is recognised on a time proportion basis using the effective interest method. When a receivable is impaired, the Group reduces the carrying amount to its recoverable amount, being the estimated future cash flow discounted at the original effective interest rate of the instrument, and continues unwinding the discount as interest income.

(ii) Oil and Gas revenue

Revenue is recognised when the significant risks and rewards of ownership of the goods have been delivered to the buyer and the costs incurred or to be incurred in respect of the transaction can be measured reliably.

The net amount of GST recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the balance sheet. Commitments and contingencies are disclosed net of the amount of GST recoverable from, or payable to, the taxation authority.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(e) Trade and other receivables

Trade receivables are recognised initially at fair value and subsequently measured at amortised cost, less allowance for doubtful debts. Trade receivables are due for settlement between thirty (30) and ninety (90) days from the date of recognition.

(f) Financial assets

Financial assets in the scope of AASB 139 Financial Instruments: Recognition and Measurement are classified as either financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, or available-for-sale investments, as appropriate. When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transactions costs. The Group determines the classification of its financial assets after initial recognition and, when allowed and appropriate, re-evaluates this designation at each reporting date.

All regular way purchases and sales of financial assets are recognised on the trade date (ie. the date that the Group commits to purchase the asset). Regular way purchases or sales are purchases or sales of financial assets under contracts that require delivery of the assets within the period established generally by regulation or convention in the marketplace

(i) Financial assets at fair value through profit or loss

Financial assets classified as held for trading are included in the category 'financial assets at fair value through profit or loss'. Financial assets are classified as held for trading if they are acquired for the purpose of selling in the near term. Derivatives are also classified as held for trading unless they are designated as effective hedging instruments. Gains or losses on investments held for trading are recognised in profit or loss.

(ii) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are carried at amortised cost using the effective interest method. Gains and losses are recognised in profit or loss when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

(iii) Available-for-sale investments

Available-for-sale investments are those non-derivative financial assets that are designated as available-for-sale or are not classified as any of the three preceding categories. After initial recognition available-for sale investments are measured at fair value with gains or losses being recognised as a separate component of equity until the investment is derecognised or until the investment is determined to be impaired, at which time the cumulative gain or loss previously reported in equity is recognised in profit or loss.

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

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(g) Impairment of financial assets

The Group assesses at each reporting date whether a financial asset or group of financial assets is impaired.

(i) Financial assets carried at amortised cost

If there is objective evidence that an impairment loss on loans and receivables carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition). The carrying amount of the asset is reduced either directly or through use of an allowance account.

The amount of the loss is recognised in profit or loss.

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If it is determined that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, the asset is included in a group of financial assets with similar credit risk characteristics and that group of financial assets is collectively assessed for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed. Any subsequent reversal of an impairment loss is recognised in profit or loss, to the extent that the carrying value of the asset does not exceed its amortised cost at the reversal date.

(ii) Financial assets carried at cost

If there is objective evidence that an impairment loss has been incurred on an unquoted equity instrument that is not carried at fair value (because its fair value cannot be reliably measured), or on a derivative asset that is linked to and must be settled by delivery of such an unquoted equity instrument, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the current market rate of return for a similar financial asset.

(iii) Available-for-sale investments

If there is objective evidence that an available-for-sale investment is impaired, an amount comprising the difference between its cost (net of any principal repayment and amortisation) and its current fair value, less any impairment loss previously recognised in profit or loss, is transferred from equity to the statement of comprehensive income. Reversals of impairment losses for equity instruments classified as available-for-sale are not recognised in profit. Reversals of impairment losses for debt instruments are reversed through profit or loss if the increase in an instrument's fair value can be objectively related to an event occurring after the impairment loss was recognised in profit or loss.

(h) Exploration, evaluation and development expenditure

Exploration, evaluation and development expenditure incurred is either written off as incurred or accumulated in respect of each identifiable area of interest. Costs are only carried forward to the extent that they are expected to be recouped through the successful development of the area or where activities in the area have not yet reached a stage which permits reasonable assessment of the existence of economically recoverable reserves.

Accumulated costs in relation to an abandoned area are written off in full against profit in the year in which the decision to abandon the area is made. A regular review is undertaken of each area of interest to determine the appropriateness of continuing to carry forward costs in relation to that area of interest.

When production commences, the accumulated costs for the relevant area of interest are amortised over the life of the area according to the rate of depletion of the economically recoverable reserves.

Restoration, rehabilitation and environmental costs necessitated by exploration and evaluation activities are expensed as incurred and treated as exploration and evaluation expenditure.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(i) Oil and gas properties

Following commencement of production activities all acquisition, exploration, evaluation and development expenditure in relation to an area of interest is accumulated into an oil and gas property.

When further development expenditure is incurred in respect of a property after the commencement of production, such expenditure is carried forward as part of the cost of that property only when substantial economic benefits are established, otherwise such expenditure is classified as part of the cost of production.

Amortisation of the cost of oil and gas properties is provided on the unit-of-production basis over the proved developed reserves of the field concerned with separate calculations being made for each resource. The unit-of-production basis results in an amortisation charge proportional to the depletion of the economically recoverable reserves. Amortisation is charged from the commencement of production.

The net carrying value of each property is reviewed regularly for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. If the asset does not generate largely independent cash flows, the recoverable amount is determined for the cash generating unit to which the asset belongs. If such indication exists and where the carrying value exceeds the estimated recoverable amount, the assets are written down to their recoverable amount.

The recoverable amount is the greater of fair-value less costs to sell and value in use. In assessing value in use, the estimated cash flows are discounted to their present value using the pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the assets.

(j) Fair value estimation

At each reporting date, the Group assesses whether there is any indication that an asset may be impaired at fair value. The fair value of financial assets and financial liabilities must be estimated for recognition and measured or for disclosure purposes.

The nominal value less estimated credit adjustments of trade receivables and payables are assumed to approximate their fair values. The fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate that is available to the Group for similar financial instruments.

(k) Trade and other payables

These amounts represent liabilities for goods and services provided to the Group prior to the end of the financial year, which remain unpaid at year end. The amounts are unsecured and are usually paid within 60 days of recognition. They are recognised at fair value on initial recognition and subsequently at amortised cost.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(l) Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Provisions are measured using the best estimate of the amounts required to settle the obligation at the end of the reporting period.

(m) Employee benefits

(i) Wages and salaries, annual leave and sick leave

Liabilities for wages and salaries, including non-monetary benefits, annual leave and accumulating sick leave expected to be settled within 12 months of the reporting date are recognised in other payables in respect of employees' services up to the reporting date and are measured at the amounts expected to be paid when the liabilities are settled.

(ii) Long service leave

The liability for long service leave is recognised in the provision for employee benefits and measured as the present value of expected future payments to be made in respect of services provided by employees up to the reporting date using the projected unit credit method. Consideration is given to expected future wage and salary levels, experience of employee departures and periods of service. Expected future payments are discounted using market yields at the reporting date on national government bonds with terms to maturity and currency that match, as closely as possible, the estimated future cash outflows.

(iii) Termination benefits

Termination benefits are payable when employment is terminated before the normal retirement date, or when an employee accepts voluntary redundancy in exchange for these benefits. The Group recognises termination benefits when it is demonstrably committed to either terminating the employment of current employees according to a detailed formal plan without possibility of withdrawal of providing termination benefits as a result of an offer made to encourage voluntary redundancy. Benefits falling due more than 12 months after reporting date are discounted to present value.

(n) Share Based Payments

The Group may at times provide benefits to employees (including directors) and consultants of the Group in the form of share-based payment transactions, whereby employees and consultants render services in exchange for shares or rights over shares ('equity-settled transactions'). The cost of these equity-settled transactions with employees and consultants is measured by reference to the fair value at the date at which they are granted. The fair value is determined using the Black & Scholes method.

The cost of equity-settled transactions is recognised, together with a corresponding increase in equity, over the year in which the performance conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award ('vesting date').

The cumulative expense recognised for equity-settled transactions at each reporting date until vesting date reflects (i) the extent to which the vesting period has expired and (ii) the number of awards that, in the opinion of the directors of the Group, will ultimately vest. This opinion is formed based on the best available information at balance date. No adjustment is made for the likelihood of market performance conditions being met as the effect of these conditions is included in the determination of fair value at grant date. No expense is recognised for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition.

Where the terms of an equity-settled award are modified, as a minimum an expense is recognized as if the terms had not been modified. In addition, an expense is recognised for any increase in the value of the transaction as a result of the modification, as measured at the date of modification. Where an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any expense not yet recognised for the award is recognised immediately. However, if a new award is substituted for the cancelled award, and designated as a replacement award on the date that it is granted, the cancelled and new award are treated as if they were a modification of the original award, as described in the previous paragraph. The dilutive effect, if any, of outstanding options is reflected as additional share dilution in the computation of earnings per share.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(o) Cash and cash equivalents

Cash and short-term deposits in the balance sheet comprise cash at bank and in hand and short term deposits with an original maturity of three months or less, which are subject to an insignificant risk of changes in value.

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

(p) Income Tax

Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the balance sheet date.

Deferred income tax is provided on all temporary differences at the balance sheet date arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements and are recognised for all taxable temporary differences:

- Except where the deferred income tax liability arises from the 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; and
- In respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, except where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred income tax assets are recognised for all deductible temporary differences, carry-forward of unused tax assets and unused tax losses can be utilised:

- Except where the deferred income tax asset relating to the deductible temporary difference arises from the 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 the taxable profit or loss; and
- In respect of taxable temporary differences associated with investments in subsidiaries, associates and interests and joint ventures, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future extent that it is probable that the temporary differences can be utilised.

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

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date. Income taxes relating to items recognised directly in equity are recognised in equity and not in the income statement.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(q) Goods and Services Tax (GST)

Revenues, expenses and assets are recognised net of the amount of GST, except:

- Where the GST incurred on a purchase of goods and services is not recoverable from the taxation authorities, in which case the GST is recognised as part of the cost of acquisition of the asset or as part of an item of the expense item as applicable; and
- Receivables and payables are stated with the amount of GST included.

The net amount of GST recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the balance sheet.

Cash flows are included the Cash Flow Statement on a gross basis and the GST component of cash flows arising from investing and financing activities, which is recoverable from, or payable to, the taxation authority are classified as operating cash flows included in receipts from customers or payments to suppliers.

Commitments and contingencies are disclosed net of the amount of GST recoverable from, or payable to, the taxation authority.

(r) Contributed Equity

Issued and paid up capital is recognised at the fair value of the consideration received by the Company. Any transaction costs arising on the issue of ordinary shares are recognised directly in equity as a reduction, net of tax, of the share proceeds received.

(s) Earnings per share

(i) Basic earnings per share

Basic earnings per share is calculated by dividing the profit attributable to equity holders of the Company, excluding any costs of servicing equity other than ordinary shares, by the weighted average number of ordinary shares outstanding during the financial year, adjusted for bonus elements in ordinary shares issued during the year.

(ii) Diluted earnings per share

Diluted earnings per share adjusts the figures used in the determination of basic earnings per share to take into account the after income tax effect of interest and other financing costs associated with dilutive potential ordinary share and the weighted average number of shares assumed to have been issued for no consideration in relation to dilutive potential ordinary shares.

2. FINANCIAL RISK MANAGEMENT

The Group's principal financial instruments comprise receivables, payables, cash and short-term deposits. The Group manages its exposure to key financial risks in accordance with the Group's financial risk management policy. The objective of the policy is to support the delivery of the Group's financial targets while protecting future financial security.

The main risks arising from the Group's financial instruments are interest rate risk, credit risk and liquidity risk. The Group does not speculate in the trading of derivative instruments. The Group uses different methods to measure and manage different types of risks to which it is exposed. These include monitoring levels of exposure to interest rates and assessments of market forecasts for interest rates. Ageing analysis of and monitoring of receivables are undertaken to manage credit risk, liquidity risk is monitored through the development of future rolling cash flow forecasts.

The Board reviews and agrees policies for managing each of these risks as summarised below.

Primary responsibility for identification and control of financial risks rests with the Board. The Board reviews and agrees policies for managing each of the risks identified below, including for interest rate risk, credit allowances and cash flow forecast projections.

Details of the significant accounting policies and methods adopted, including the criteria for recognition, the basis of measurement and the basis on which income and expenses are recognised, in respect of each class of financial asset and financial liability are disclosed in note 1 to the financial statements.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

2. FINANCIAL RISK MANAGEMENT

Risk Exposures and Responses

Market Risk

Interest rate risk

The Group's exposure to risks of changes in market interest rates relates primarily to the Group's cash balances. The Group constantly analyses its interest rate exposure. Within this analysis consideration is given to potential renewals of existing positions, alternative financing positions and the mix of fixed and variable interest rates. As the Group has no interest bearing borrowings its exposure to interest rate movements is limited to the amount of interest income it can potentially earn on surplus cash deposits. The following sensitivity analysis is based on the interest rate risk exposures in existence at the reporting date.

At reporting date, the Group had the following financial assets exposed to variable interest rates that are not designated in cash flow hedges:

	Group	
	2011 \$	2010 \$
Tenement security bonds	20,000	-
Cash and cash equivalents (interest-bearing accounts)	612,676	2,066,082
Net exposure	632,676	2,066,082

The following sensitivity analysis is based on the interest rate risk exposures in existence at the reporting date. At 31 December 2011, if interest rates had moved, as illustrated in the table below, with all other variables held constant, post tax profit and equity relating to financial assets of the Group would have been affected as follows:

Judgments of reasonably possible movements:		
Post tax profit – higher / (lower)		
+ 0.5%	3,163	10,330
- 0.5%	(3,163)	(10,330)
Equity – higher / (lower)		
+ 0.5%	3,163	10,330
- 0.5%	(3,163)	(10,330)

Commodity Price and Foreign Currency Risk

The Group's exposure to price and currency risk is minimal given the Group is still in the exploration phase.

Liquidity Risk

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

Typically the Group ensures that it has sufficient cash on demand to meet expected operational expenses for a period of 60 days, including the servicing of financial obligations; this excludes the potential impact of extreme circumstances that cannot reasonably be predicted, such as natural disasters.

The Group has access to a \$3 million equity line of credit with YA Global. The financial liabilities the Group had at reporting date were trade payables incurred in the normal course of the business. Trade payables were non-interest bearing and were due within the normal 30-60 days terms of creditor payments.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

2. FINANCIAL RISK MANAGEMENT

Maturities of financial liabilities

The table below analyses the Group's financial liabilities into relevant maturity groupings based on the remaining period at the reporting date to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows.

	Group						
	Less than 1 month	1 - 3 months	3 months - 1 year	1 - 5 years	5+ Years	Total contractual cash flows	Carrying amount
	\$	\$	\$			\$	\$
As at 31 December 2011							
Receivables	-	21,606	-	-	-	21,606	21,606
Trade and other payables	15,288	-	-	-	-	15,288	15,288
Accrued expenses	109,612	46,000	-	-	-	155,612	155,612
As at 31 December 2010							
Receivables	124,043	-	206,000	-	-	330,043	330,043
Trade and other payables	262,832	-	-	-	-	262,832	262,832
Accrued expenses	330,663	-	-	-	-	330,663	330,663

Credit risk

Credit risk arises from the financial assets of the Group, which comprise deposits with banks and trade and other receivables. The Group's exposure to credit risk arises from potential default of the counter party, with the maximum exposure equal to the carrying amount of these instruments. The carrying amount of financial assets included in the statement of financial position represents the Group's maximum exposure to credit risk in relation to those assets. The Group does not hold any credit derivatives to offset its credit exposure.

The Group trades only with recognised, credit worthy third parties and as such collateral is not requested nor is it the Group's policy to securities it trade and other receivables. Receivable balances are monitored on an ongoing basis with the result that the Group does not have a significant exposure to bad debts.

There are no significant concentrations of credit risk within the Group.

Capital Management Risk

Management controls the capital of the Group in order to maximise the return to shareholders and ensure that the Group can fund its operations and continue as a going concern.

Management effectively manages the Group's capital by assessing the Group's financial risks and adjusting its capital structure in response to changes in these risks and in the market. These responses include the management of expenditure, debt levels and share and option issues.

There have been no changes in the strategy adopted by management to control capital of the Group since the prior year.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

2. FINANCIAL RISK MANAGEMENT

Fair Value

The methods of estimating fair value are outlined in the relevant notes to the financial statements. All financial assets and liabilities recognised in the statement of financial position, whether they are carried at cost or fair value, are recognised at amounts that represent a reasonable approximation of fair values unless otherwise stated in the applicable notes.

3. CRITICAL ACCOUNTING ESTIMATES AND ASSUMPTIONS

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

(i) Exploration expenditure

Expenditure and development expenditure that does not form part of the cash generating units assessed for impairment has been carried forward on the basis that exploration and evaluation activities have not yet reached a stage which permits a reasonable assessment of the existence or otherwise of economically recoverable reserves and active and significant operations in relation to the area are continuing. In the event that significant operations cease and/or economically recoverable reserves are not assessed as being present, this expenditure will be expensed to the Income Statement.

Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that may have a financial impact on the entity and that are believed to be reasonable under the circumstances.

4. SEGMENT REPORTING

The Group has identified its operating segments based on the internal reports that are reviewed and used by the Board of Directors (chief operating decision makers) in assessing performance and determining the allocation of resources.

Based on these reports, management has determined that the Company has one operating segment, being the exploration and development of properties for the development of oil and gas.

Types of products and services

The Group currently has no revenue from products or services.

Major customers

The Group has no reliance on major customers.

Geographical areas

The Group's non-current assets are located in Australia.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

5. REVENUE

	Group	
	2011	2010
	\$	\$
Interest Received	50,867	145,564
Other Revenue	-	48,241
	50,867	193,805

6. EXPENSES

	Group	
	2011	2010
	\$	\$
Loss from continuing operations before income tax has been determined after		
(a) Employee benefit expense:		
Salaries – G de Nys	85,077	73,333
Superannuation – G de Nys	7,800	6,600
Share based remuneration – directors	720,000	-
	812,877	79,933
(b) Exploration expenditure and impairment	4,478,225	6,211,181

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

7. INCOME TAX

	Group	
	2011	2010
	\$	\$

The prima facie income tax expense/(income) on pre-tax accounting loss from operations reconciles to the income tax expense/(income) in the financial statements as follows:

Loss before tax	(6,227,134)	(7,404,679)
Income tax expense/(income) calculated at 30%	(1,868,140)	(2,221,404)
Effect of expenses that are not deductible in determining taxable profit	261,109	891,284
Temporary differences and tax losses for which no deferred tax asset has been brought to account	1,607,031	1,330,120
		-

The tax rate used in the above reconciliation is the corporate tax rate of 30% payable by Australian corporate entities on taxable profits under Australian tax law. There has been no change in the corporate tax rate when compared with the previous reporting period.

Deferred tax assets		
Deferred tax assets not brought to account arising from tax losses, the benefits of which will only be realised if the conditions for deductibility set out in Note 1(v) occur:	5,494,554	4,091,523

8. CASH AND CASH EQUIVALENTS

	Group	
	2011	2010
	\$	\$
Cash at bank	612,676	2,668,000

9. TRADE AND OTHER RECEIVABLES

	Group	
	2011	2010
	\$	\$
Current		
GST Receivables	21,606	124,042

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

10. EXPLORATION ASSETS

	Group	
	2011 \$	2010 \$
Opening balance	6,256,926	7,430,000
Additions	2,947,906	5,038,207
Write offs	(4,478,225)	(6,211,281)
Exploration Assets ¹	4,726,607	6,256,926

¹ The ultimate recoupment of these costs is dependent on successful development and commercial exploitation, or alternatively, the sale of the respective areas.

11. INVESTMENT IN CONTROLLED ENTITIES

		Ownership Interest	
		2011 %	2010 %
Cydonia Resources Pty Ltd	Australia	100	100
Norwest Hydrocarbons Pty Ltd	Australia	100	100
Surat Resources Pty Ltd	Australia	100	100
Red Sky NT Pty Ltd	Australia	100	100
Summerland Way Energy Pty Ltd	Australia	100	100

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

12. ISSUED CAPITAL

a) Share Capital

Ordinary shares	Group	
	2011 \$	2010 \$
1,382,904,577 fully paid ordinary shares (31 December 2010: 1,191,508,972)	29,915,004	27,788,310
Movements during the year:		
Beginning of year	27,788,310	25,967,000
Shares issued during the prior year	-	1,925,000
40,000,000 shares issued @ \$0.017 – ATP946 farm-in	680,000	-
120,000,000 shares issued @ \$0.012 – share placement	1,440,000	-
15,000,000 shares issued @ \$0.008 – ATP904P farm-in termination	120,000	-
11,538,462 shares issued @ \$0.0065 – equity facility costs	75,000	-
4,857,143 shares issued @ \$0.007 – equity facility issue	34,000	-
Equity Raising Expenses	(222,306)	(103,690)
	29,915,004	27,788,310

Ordinary shares entitle the holder to participate in dividends and the proceeds on winding up of the Company in proportion to the number of and amounts paid on the shares held.

On a show of hands every holder of ordinary shares present at a meeting in person or by proxy, is entitled to one vote, and upon a poll each share is entitled to one vote.

Equity Facility

During the year, the Company entered into a \$3m equity facility with a US-Based Investment Fund, YA Global Master SPV Ltd, that can be drawn down at any time over a 3 year period. The Company is not obligated to use the facility and it can be cancelled at any time. \$34,000 before costs was raised under the facility during the year.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

b) Options Issued

Expiry Date	Exercise Price (cents)	Number on issue – 2010	Granted during year	Lapsed during year	Exercised during year	Number on issue - 2011
23/05/2011	20.00	2,000,000	-	(2,000,000)	-	-
18/02/2012	20.00	250,000	-	-	-	250,000
02/09/2011	2.00	298,300,000	60,000,000(i)	(358,300,000)	-	-
18/09/2014	4.00	200,000,000	-	-	-	200,000,000
31/03/2016	2.25	-	60,000,000(ii)	-	-	60,000,000
Total Options Issued		500,550,000	120,000,000	(360,300,000)	-	260,250,000

(i) Free attaching Options issued pursuant to a share placement.

(ii) Options issued to non-executive directors following shareholder approval on 21 March 2011 (Mr Gerrit de Nys 37,500,000, Mr Guy Le Page 15,000,000 and Mr Murray Durham 7,500,000).

13. RESERVES

	Group	
	2011 \$	2010 \$
Option expense reserve	1,458,000	738,000
Opening balance	738,000	738,000
Movement during the year – share based remuneration	720,000	-
	1,458,000	738,000

Nature and purpose of reserves:

Option expense reserve records the value of options issued which have been taken to expenses.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

14. ACCUMULATED LOSSES

	Group	
	2011	2010
	\$	\$
Accumulated losses at the beginning of the year	(19,844,679)	(12,440,000)
Net loss attributable to the members of the parent entity	(6,227,134)	(7,404,679)
Accumulated losses at the end of the financial year	(26,071,813)	(19,844,679)

15. LOSS PER SHARE

	Group	
	2011	2010
	\$	\$
Reconciliation of earnings to net loss		
Net loss	(6,227,134)	(7,404,679)
Calculation of basic and dilutive EPS (cents)	(0.47)	(0.75)
Weighted average number of ordinary shares outstanding during the year used in calculation of basic and dilutive EPS	Number 1,313,150,008	Number 993,782,945

Details of the shares issued are included under Note 12. Dilutive EPS is not reflected as the exercised options would result in the reduction of the loss per share.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

16. CASH FLOW INFORMATION

Reconciliation of cash flow from operations with loss from continuing operations after income tax

	GROUP	
	2011	2010
	\$	\$
Loss after income tax	(6,227,134)	(7,404,679)
Non cash flows in loss:		
Issue of share capital in lieu of cash	120,000	-
Share based remuneration	720,000	-
Exploration costs written off	4,478,225	6,211,281
Changes in assets and liabilities:		
Increase/(decrease) in trade creditors and accruals	51,677	192,495
(Increase)/decrease in trade and other receivables	102,436	(138,042)
(Increase)/decrease in prepayments	(40,202)	-
Cash flows from (used in) operations	(794,998)	(1,138,945)

17. DIVIDENDS

There were no dividends paid or payable in respect of the current financial year.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

18. RELATED PARTY TRANSACTIONS

(a) Transactions with related parties

Directors and officers, or their personally-related entities, hold positions in other entities that result in them having control or significant influence over the financial or operating policies of those entities.

Entity		Amount Paid \$	Relationship
AAG Management Pty Ltd	2011	-	AAG Management Pty Ltd is a management Company which provided facilities, human resources, and other administration and consulting services. David Ballantyne is the company secretary of AAG Management Pty Ltd and he was Company secretary of Red Sky Energy Ltd for part of the year.
	2010	5,210	
GBU Capital Pty Ltd	2011	40,000	GBU Capital Pty Ltd is a management Company which provided facilities, human resources, and other administration and consulting services. Lloyd Flint provided consulting services to GBU Capital Pty Ltd for the period beginning 01/01/2010 to 03/02/2011 and was Company secretary of Red Sky Energy Ltd.
	2010	240,000	
Energy Infrastructure and Resources Ltd	2011	956,706	Energy Infrastructure and Resources Ltd is a consulting Company which invoices the Company for director's fees and other reimbursement charges for Rohan Gillespie. During the year Energy Infrastructure and Resources Ltd has also invoiced consulting charges for Philip Jackson and Duncan Thomson for management of exploration programs. Rohan Gillespie is a director of Energy Infrastructure and Resources Ltd and he is managing director of Red Sky Energy Ltd.
	2010	745,432	

b) Details of the transactions including amounts accrued but unpaid at the end of the year are as follows:

	Transaction	2011 \$	2010 \$
Energy Infrastructure and Resources Ltd	Consulting Fees	58,381	97,568

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

18. RELATED PARTY TRANSACTIONS

(c) Share and Option holdings

As at the date of this report, the interests of the Directors in shares and options of the Company were:

Ordinary shares

Holder	Held at beginning of the year	Initial Interest	Acquired	Disposed	Final interest	Balance at end of the year
Gerrit de Nys	1,000,000	n/a	3,000,000	-	n/a	4,000,000
Rohan Gillespie	180,000,000	n/a	-	-	n/a	180,000,000
Murray Durham	15,000,000	n/a	-	-	n/a	15,000,000
Guy Le Page	-	n/a	-	-	n/a	-

Options

Holder	Held at beginning of the year	Initial Interest	Remuneration	Expired	Final interest	Balance at end of the year
Gerrit de Nys	-	n/a	37,500,000	-	n/a	37,500,000
Rohan Gillespie	97,500,000	n/a	-	97,500,000	n/a	-
Murray Durham	-	n/a	7,500,000	-	n/a	7,500,000
Guy Le Page	-	n/a	15,000,000	-	n/a	15,000,000

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

19. KEY MANAGEMENT PERSONNEL DISCLOSURES

- (a) Details of the names and positions of key management personnel and their remuneration are provided in the remuneration report on pages 14 to 17. Summary disclosures are as follows:

	Group	
Key Management Personnel Compensation	2011 \$	2010 \$
Short-term employee benefits	470,071	648,195
Post employment benefits	30,300	7,200
Long-term benefits	-	-
Termination benefits	-	-
Share-based payments	720,000	-
Total	1,220,371	655,395

- (b) Equity instrument disclosures relating to key management personnel.

Ordinary Shares

		Held at beginning of period	Acquired	Sold	Final Interest	Balance at end of period
David Ballantyne-Indirect	2011	-	-	-	-	-
	2010	4,627,912	12,627,912	8,000,000	4,627,912	-
Adrien Wing	2011	-	-	-	-	-
	2010	-	-	-	-	-
Lloyd Flint	2011	-	-	-	-	-
	2010	-	-	-	-	-

20. REMUNERATION OF AUDITORS

	GROUP	
	2011 \$	2010 \$
Amounts received or due and receivable by RSM Bird Cameron for:		
Audit and audit review services	29,500	25,000
Other non audit services	-	-

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

21. PARENT ENTITY DISCLOSURES

(a) Summary financial information

	Parent	
	2011	2010
	\$	\$
Financial Position		
Assets		
Current assets	646,837	2,823,256
Non-current assets	4,854,165	6,324,193
Total assets	5,501,002	9,147,449
Liabilities		
Current liabilities	199,811	465,818
Total liabilities	199,811	465,818
Equity		
Issued share capital	29,915,004	27,788,310
Option expense reserves	1,458,000	738,000
Accumulated losses	(26,071,813)	(19,844,679)
Total equity	5,301,191	8,681,631
Financial Performance		
Loss for the year	(6,227,134)	(7,454,987)
Other comprehensive income	-	-
Total comprehensive income	(6,227,134)	(7,454,987)

b) Guarantees

Red Sky Energy Limited has not entered into any guarantees in relation to the debts of its subsidiary.

c) Other Commitments and Contingencies

Red Sky Energy Limited has no commitments to acquire property, plant and equipment, and has no contingent liabilities apart from the amounts disclosed in note 23.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

22. EVENTS SUBSEQUENT TO BALANCE SHEET DATE

On 4 January 2012, 5,666,667 ordinary fully paid shares were issued for \$0.0065.
On 30 January 2012, 8,333,334 ordinary fully paid shares were issued for \$0.006.
On 17 February 2012, 6,250,000 ordinary fully paid shares were issued for \$0.007.
These shares were issued under the \$3m equity facility in place with YA Global.

Other than the above and the legal dispute disclosed in note 23 below, no matter or circumstance has arisen since 31 December 2011 that has significantly affected, or may significantly affect the Group's operations or affairs in future years.

23. COMMITMENTS AND CONTINGENCIES

The Consolidated Entity has exploration expenditure commitments on granted permits:

	2011	2010
	\$	\$
Not longer than 1 year	2,300,000	6,600,000
Longer than 1 year and not longer than 5 years	-	4,800,000
	2,300,000	11,400,000

The \$2,300,000 commitment could be met by additional capital raisings by the Company or by farming in a third party. Alternatively the work commitment could be ignored and the permit returned to the DPI. The group also has a number of permits in the application stage or subject to the Company exercising an option to increase its ownership percentage. Consequently, there may be additional exploration commitments over the term of the permits.

Legal Dispute:

In February 2012, a summary judgement decision in respect of a claim by a former drilling contractor, TDC Drilling Pty Ltd ("TDC"), was awarded against the Company's subsidiary Cydonia Resources Pty Ltd ("Cydonia"), however the decision provides for the summary judgement to be immediately stayed pending trial of a counterclaim against TDC by Cydonia or further orders. The proceedings in the Supreme Court of Western Australia concern the Annvale No 1 well in PEL 479 in New South Wales. The decision was made in respect of a claim by TDC for \$205,792, liability for which was disputed by Cydonia. As the well was not completed to the satisfaction of the Board and costs were incurred with a replacement contractor in drilling the alternative Annvale No 2 well nearby, Cydonia considers it has a counterclaim against TDC substantially in excess of the amount of its invoice. The stay of the summary judgement preserves Cydonia's ability to pursue its counterclaim which, if successful, would have the effect of completely eliminating the stayed judgement.

24. NEW ACCOUNTING STANDARDS FOR APPLICATION IN FUTURE PERIODS

Certain new accounting standards and interpretations have been published that are not mandatory for 31 December 2011 reporting periods. The group's assessment of the impact of these new standards and interpretations is set out below:

- 1) *AASB 9: Financial Instruments (December 2010) and AASB 2010-7: Amendments to Australian Accounting Standards arising from AASB 9 (December 2010) [AASB 1, 3, 4, 5, 7, 101, 102, 108, 112, 118, 120, 121, 127, 128, 131, 132, 136, 137, 139, 1023 & 1038 and Interpretations 2, 5, 10, 12, 19 & 127] (applicable for annual reporting periods commencing on or after 1 January 2013).*

These Standards are applicable retrospectively and include revised requirements for the classification and measurement of financial instruments, as well as recognition and derecognition requirements for financial instruments.

The key changes made to accounting requirements include:

- simplifying the classifications of financial assets into those carried at amortised cost and those carried at fair value;
- simplifying the requirements for embedded derivatives;
- removing the tainting rules associated with held-to-maturity assets;
- removing the requirements to separate and fair value embedded derivatives for financial assets carried at amortised cost;
- allowing an irrevocable election on initial recognition to present gains and losses on investments in equity instruments that are not held for trading in other comprehensive income. Dividends in respect of these investments

that are a return on investment can be recognised in profit or loss and there is no impairment or recycling on disposal of the instrument;

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

24. NEW ACCOUNTING STANDARDS FOR APPLICATION IN FUTURE PERIODS (cont.)

- requiring financial assets to be reclassified where there is a change in an entity's business model as they are initially classified based on: (a) the objective of the entity's business model for managing the financial assets; and (b) the characteristics of the contractual cash flows; and
- requiring an entity that chooses to measure a financial liability at fair value to present the portion of the change in its fair value due to changes in the entity's own credit risk in other comprehensive income, except when that would create an accounting mismatch. If such a mismatch would be created or enlarged, the entity is required to present all changes in fair value (including the effects of changes in the credit risk of the liability) in profit or loss.

The Group has not yet been able to reasonably estimate the impact of these pronouncements on its financial statements.

- 2) *AASB 2010-6: Amendments to Australian Accounting Standards – Disclosures on Transfers of Financial Assets [AASB 1 & AASB 7] (applicable for annual reporting periods beginning on or after 1 July 2011).*

This Standard adds and amends disclosure requirements about transfers of financial assets, especially those in respect of the nature of the financial assets involved and the risks associated with them. Accordingly, this Standard makes amendments to AASB 1: First-time Adoption of Australian Accounting Standards and AASB 7: Financial Instruments: Disclosures, establishing additional disclosure requirements in relation to transfers of financial assets.

This Standard will only affect certain disclosures relating to financial instruments and is not expected to significantly impact the Group.

- 3) *AASB 2010-8: Amendments to Australian Accounting Standards – Deferred Tax: Recovery of Underlying Assets [AASB 112] (applies to periods beginning on or after 1 January 2012).*

This Standard makes amendments to AASB 112: Income Taxes and incorporates Interpretation 121 into AASB 112.

Under the current AASB 112, the measurement of deferred tax liabilities and deferred tax assets depends on whether an entity expects to recover an asset by using it or by selling it. The amendments introduce a presumption that an investment property is recovered entirely through sale. This presumption is rebutted if the investment property is held within a business model whose objective is to consume substantially all of the economic benefits embodied in the investment property over time, rather than through sale.

The amendments are not expected to significantly impact the Group.

- 4) *AASB 1054: Australian Additional Disclosures and AASB 2011-1: Amendments to Australian Accounting Standards arising from the Trans-Tasman Convergence Project [AASB 1, AASB 5, AASB 101, AASB 107, AASB 108, AASB 121, AASB 128, AASB 132 & AASB 134 and Interpretations 2, 112 & 113] (applicable for annual reporting periods commencing on or after 1 July 2011).*

AASB 1054 sets out the Australian-specific disclosures that are additional to IFRS disclosure requirements. The disclosure requirements in AASB 1054 were previously located in other Australian Accounting Standards.

These Standards are not expected to significantly impact the Group.

- 5) *AASB 10: Consolidated Financial Statements, AASB 11: Joint Arrangements, AASB 12: Disclosure of Interests in Other Entities, AASB 127: Separate Financial Statements (August 2011), AASB 128: Investments in Associates and Joint Ventures (August 2011) and AASB 2011-7: Amendments to Australian Accounting Standards arising from the Consolidation and Joint Arrangements Standards [AASB 1, 2, 3, 5, 7, 9, 2009-11, 101, 107, 112, 118, 121, 124, 132, 133, 136, 138, 139, 1023 & 1038 and Interpretations 5, 9, 16 & 17] (applicable for annual reporting periods commencing on or after 1 January 2013).*

AASB 10 replaces parts of AASB 127: Consolidated and Separate Financial Statements (March 2008, as amended) and Interpretation 112: Consolidation – Special Purpose Entities. AASB 10 provides a revised definition of control and additional application guidance so that a single control model will apply to all investees.

The Group has not yet been able to reasonably estimate the impact of this Standard on its financial statements.

AASB 11 replaces AASB 131: Interests in Joint Ventures (July 2004, as amended). AASB 11 requires joint arrangements to be classified as either 'joint operations' (whereby the parties that have joint control of the arrangement have rights to the assets and obligations for the liabilities) or 'joint ventures' (where the parties that have joint control of the arrangement have rights to the net assets of the arrangement). Joint ventures are required to adopt the equity method of accounting (proportionate consolidation is no longer allowed).

AASB 12 contains the disclosure requirements applicable to entities that hold an interest in a subsidiary, joint venture, joint operation or associate. AASB 12 also introduces the concept of a 'structured entity', replacing the 'special purpose entity' concept currently used in Interpretation 112, and requires specific disclosures in respect of any investments in unconsolidated structured entities. This Standard will only affect disclosures and is not expected to significantly impact the Group.

To facilitate the application of AASBs 10, 11 and 12, revised versions of AASB 127 and AASB 128 have also been issued. These Standards are not expected to significantly impact the Group.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

24. NEW ACCOUNTING STANDARDS FOR APPLICATION IN FUTURE PERIODS (cont.)

- 6) *AASB 13: Fair Value Measurement and AASB 2011-8: Amendments to Australian Accounting Standards arising from AASB 13 [AASB 1, 2, 3, 4, 5, 7, 9, 2009-11, 2010-7, 101, 102, 108, 110, 116, 117, 118, 119, 120, 121, 128, 131, 132, 133, 134, 136, 138, 139, 140, 141, 1004, 1023 & 1038 and Interpretations 2, 4, 12, 13, 14, 17, 19, 131 & 132] (applicable for annual reporting periods commencing on or after 1 January 2013).*

AASB 13 defines fair value, sets out in a single Standard a framework for measuring fair value, and requires disclosures about fair value measurements. AASB 13 requires:

- inputs to all fair value measurements to be categorised in accordance with a fair value hierarchy; and
- enhanced disclosures regarding all assets and liabilities (including, but not limited to, financial assets and financial liabilities) measured at fair value.

These Standards are not expected to significantly impact the Group.

- 7) *AASB 2011-9: Amendments to Australian Accounting Standards – Presentation of Items of Other Comprehensive Income [AASB 1, 5, 7, 101, 112, 120, 121, 132, 133, 134, 1039 & 1049] (applicable for annual reporting periods commencing on or after 1 July 2012).*

The main change arising from this Standard is the requirement for entities to group items presented in other comprehensive income (OCI) on the basis of whether they are potentially reclassifiable to profit or loss subsequently.

This Standard affects presentation only and is not expected to significantly impact the Group.

- 8) *AASB 119: Employee Benefits (September 2011) and AASB 2011-10: Amendments to Australian Accounting Standards arising from AASB 119 [AASB 1, AASB 8, AASB 101, AASB 124, AASB 134, AASB 1049 & AASB 2011-8 and Interpretation 14] (applicable for annual reporting periods commencing on or after 1 January 2013).*

These Standards introduce a number of changes to the presentation and disclosure of defined benefit plans, including:

- removal of the 'corridor' approach from AASB 119, thereby requiring entities to recognise all changes in a net defined benefit liability (asset) when they occur;
- disaggregation of changes in a net defined benefit liability (asset) into service cost (including past service cost and gains and losses on non-routine settlements and curtailments), net interest expense [interest based on the net defined benefit liability (asset) using the discount rate applicable to post-employment benefits] and remeasurements [comprising actuarial gains and losses, return on plan assets less the 'revenue' component of the net interest expense, and any change in the limit on a defined benefit asset]. In addition, AASB 119 [September 2011] requires recognition of:
 - o service cost and net interest expense in profit or loss; and
 - o remeasurements in OCI; and
- introduces enhanced disclosure requirements to facilitate the provision of more useful information in relation to entity's defined benefit plans.

AASB 119 [September 2011] also includes changes to the accounting for termination benefits that require an entity to recognise an obligation for such benefits at the earlier of:

- (i) for an offer that may be withdrawn – when the employee accepts;
- (ii) for an offer that cannot be withdrawn – when the offer is communicated to affected employees; and
- (iii) where the termination is associated with a restructuring of activities under AASB 137: Provisions, Contingent Liabilities and Contingent Assets, and if earlier than the first two conditions – when the related restructuring costs are recognised.

The Group has not yet been able to reasonably estimate the impact of these changes on its financial statements.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2011

DIRECTORS' DECLARATION

The directors of the company declare that:

1. the financial statements and notes, as set out on pages 20 to 48, are in accordance with the *Corporations Act 2001* and:
 - a. comply with Accounting Standards; and
 - b. give a true and fair view of the financial position As at 31 December 2011 and of the performance for the year ended on that date of the company and consolidated group;
2. the Chief Executive Officer and Chief Finance Officer have each declared that:
 - a. the financial records of the company for the financial year have been properly maintained in accordance with s 286 of the *Corporations Act 2001*;
 - b. the financial statements and notes for the financial year comply with the Accounting Standards; and
 - c. the financial statements and notes for the financial year give a true and fair view;
3. in the directors' opinion there are reasonable grounds to believe that the company will be able to pay its debts as and when they become due and payable.

This declaration is made in accordance with a resolution of the Board of Directors.



Rohan Gillespie
Managing Director

Melbourne, Victoria
9 March 2012

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525 Collins Street Melbourne VIC 3000
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www.rsmi.com.au

INDEPENDENT AUDITOR'S REPORT

THE MEMBERS OF

RED SKY ENERGY LIMITED

We have audited the accompanying financial report of Red Sky Energy Limited ("the company"), which comprises the consolidated statement of financial position as at 31 December 2011, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, a summary of significant accounting policies, other explanatory notes and the directors' declaration of the consolidated entity comprising the company and the entities it controlled at the year's end or from time to time during the financial year.

Directors' Responsibility for the Financial Report

The directors of the company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the directors determine is necessary to enable the preparation of the financial report that is free from material misstatement, whether due to fraud or error. In Note 1, the directors also state, in accordance with Accounting Standard AASB 101 *Presentation of Financial Statements*, that the financial statements comply with *International Financial Reporting Standards*.

Auditor's Responsibility

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

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

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

Independence

In conducting our audit, we have complied with the independence requirements of the *Corporations Act 2001*. We confirm that the independence declaration required by the *Corporations Act 2001*, which has been given to the directors of Red Sky Energy Limited, would be in the same terms if given to the directors as at the time of this auditor's report.

Opinion

In our opinion:

- (a) the financial report of Red Sky Energy Limited is in accordance with the *Corporations Act 2001*, including:
 - (i) giving a true and fair view of the consolidated entity's financial position as at 31 December 2011 and of its performance for the year then ended; and
 - (ii) complying with Australian Accounting Standards and the *Corporations Regulations 2001*; and
- (b) the financial report also complies with *International Financial Reporting Standards* as disclosed in Note 1.


RSM BIRD CAMERON PARTNERS
Chartered Accountants


J S CROALL
Partner

Dated: 9 March 2012
Melbourne, Victoria

SHAREHOLDER INFORMATION

TWENTY LARGEST SHAREHOLDERS

SHAREHOLDERS (Fully Paid Ordinary) 27 February 2012	NUMBER OF SHARES	Percentage
ENERGY INFRASTRUCTURE AND RESOURCES LTD	180,000,000	12.75
MR GLEN KENNETH CUNNINGHAM & MRS ROBYN GWENDOLINE CUNNINGHAM	40,000,000	2.85
PLF INVESTMENTS PTY LTD	40,000,000	2.85
RESOLVE GEO PTY LTD	40,000,000	2.85
SEREC PTY LTD	30,000,000	2.14
SANTELLE PTY LTD	17,352,223	1.24
DURHAM ENERGY CONSULTING PTY LTD	15,000,000	1.07
ADELAIDE ENERGY LTD	15,000,000	1.07
MARE E MONTI PTY LTD	15,000,000	1.07
MR NICOLA LUCANO	15,000,000	1.07
MR ZANI ILYAZOVSKI	13,241,887	0.94
HSBC CUSTODY NOMINEES	13,016,026	0.93
MR GARRY ARNEPHY	12,336,708	0.88
MR DEAN RONALD FIEDLER	12,000,000	0.86
SUNNYRIDGE ENTERPRISES PTY LTD	10,500,000	0.75
MR WAN HOW NG	10,000,000	0.71
BROWNWARD PTY LTD	10,000,000	0.71
MR SIMON WILLIAM TRITTON	9,000,000	0.64
FINOT PTY LTD	9,000,000	0.64
CIMB SECURITIES (SINGAPORE)	8,000,000	0.57
TOP 20 SHAREHOLDERS	514,446,844	36.66
TOTAL ISSUED SHARES	1,403,154,578	100%

Distribution schedule of the number of fully paid ordinary shareholders in each class of equity security.

By Class	Holder of Ordinary shares	Number of Ordinary shares	Percentage
1 – 1,000	36	6,146	0.00
1,001 - 5,000	34	117,335	0.01
5,001 – 10,000	81	732,818	0.05
10,001 – 100,000	1,179	65,138,918	4.64
100,001 and over	1,314	1,337,159,361	95.30
Totals	2,644	1,403,154,578	100 %

Share options unlisted as at 27 February 2012

Total Number of Options	Exercise Price	Expiry Date
200,000,000 *	4 Cents	18/09/2014
60,000,000	2.25 Cents	31/03/2016

* Holder	Vendor Options
Energy Infrastructure and Resources Limited	97,500,000
Serec Pty Ltd as trustee for The Family Account	45,000,000
Mare Monti P/L < The Thompson Family A/C>	7,500,000
Distinct Racing & Breeding Pty Ltd	10,000,000
Bluebase Pty Ltd	10,000,000
Spartan Nominees Pty Ltd	10,000,000
Formaine Pty Ltd	10,000,000
Fay Holdings Pty Ltd	10,000,000
TOTAL	200,000,000

ADDITIONAL SHAREHOLDER INFORMATION

A. CORPORATE GOVERNANCE

A statement disclosing the extent to which the Company has followed the best practice recommendations set by the ASX Corporate Governance Council during the reporting period is contained in this document on page 6.

B. SHAREHOLDING

1. Substantial Shareholders

The following substantial Shareholders were listed on the Company's register as at 27 February 2012.

Shareholder	Number of Shares	Percentage
ENERGY INFRASTRUCTURE AND RESOURCES LTD	180,000,000	12.75

2. Unquoted Securities

There are no shareholders holding greater than 20% of a class of unquoted securities.

3. Number of holders in each class of equity securities and the voting rights attached.

At the general meeting, every ROG shareholder present in person or by proxy, representative or attorney has one vote on a show of hands and on a poll, one vote for each share (which is fully paid). There are 2,644 holders of fully paid ordinary shares. The Company has no partly paid shares on issue.

4. Marketable parcel

There are 949 Shareholders with less than a marketable parcel as at 27 February 2012.

C. OTHER DETAILS

1. Company Secretary

Mr Adrien Wing

2. Address and telephone details of the entity's registered and administrative office

The address and telephone details of the registered and administrative office:

Level 17, 500 Collins Street
 Melbourne VIC 3000

Telephone: + (61) 03 9614 0600
 Facsimile: + (61) 03 9614 0550

3. Address and telephone details of the office at which a register of securities is kept

The address and telephone number of the office at which a registry of securities is kept:

Advanced Share Registry Services
 150 Stirling Highway
 NEDLANDS Western Australia 6009

Telephone: + (61) 08 9389 8033
 Facsimile: + (61) 08 9389 7871

4. Stock exchange on which the Company's securities are quoted

The Company's listed equity securities are quoted on the Australian Stock Exchange.

5. Restricted Securities

The Company has no restricted securities on issue.

6. Permit Schedule

Red Sky Energy Limited - Exploration Permit Schedule

Subsidiary	Permit	Nature of Interest	Extent of Interest
Cydonia Resources			
	ATP 840	farm-in	50%
	ATP 946	farm-in	right to earn 100%
Summerland Way Energy			
	PEL 479	farm-in	right to earn 100%
	PEL 457	farm-in	right to earn 100%
	PEL 478	farm-in	right to earn 100%
	PSPA 37	farm-in	right to earn 100%