OTTO ENERGY

# ANNUAL REPORT 2009

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OTTO7501

# CHAIRMAN'S LETTER

Dear Shareholders,

During 2008/09, we experienced notable successes and some disappointments. However, I am pleased to report that we are now in a good position, both financially and managerially.

The share price came under pressure over the past financial year due to both external and internal factors. Clearly, the impact of severe weather conditions with unfortunate timing had the result of Galoc production failing to meet forecasts and Otto's share price suffered accordingly. Moreover, following the collapse of the oil price and due no doubt to the general economic crisis experienced worldwide, investors re-adjusted valuations back to earnings fundamentals and away from future exploration expectations. This continues to impact Otto notwithstanding improved consistent production from Galoc and an improved oil price.

Otto raised approximately $31.5 million during the financial year from a capital raising comprising two share placements and a pro-rata entitlement issue to shareholders, which was completed in June 2009. The fact that the Company was able to successfully raise such a significant sum during poor market conditions, is testament to the support of shareholders and I thank you for the faith shown.

The Galoc Production Company WLL project debt over the Galoc Field was also fully repaid during the year, resulting in Otto having no debt and cash reserves of $13 million at 30 June 2009.

Going forward, we will continue to receive cash flow from Galoc which is producing at 11,000 bbls/day on a natural decline. Furthermore, the technical and commercial fundamentals of the Galoc field remain strong and planning for further appraisal and potential incremental development is currently underway.

Taking further steps to add production, generate cash flow and unlock the value of current discoveries is core to the growth of Otto. To this end the Company continues to progress the development of the Edirne gas fields in the onshore Thrace Basin in Turkey. Bringing these fields on stream is within the Company's current funding capability and was envisioned at the time of the June capital raising. The assets in Turkey formed the basis of the Company's float on the ASX in December 2004, and it will be pleasing to see these assets come into commercial fruition shortly. Edirne gas will become Otto's second revenue-generating asset after Galoc oil.

In the year ahead, I expect to see our offshore Philippines exploration portfolio farmed down and the Company's development portfolio progressing.

We have significantly repositioned our management team during 2009. Our new CEO, Paul Moore has some 27 years experience in all aspects of upstream E&P business with Shell International, Fletcher Challenge Energy, Santos Ltd and Woodside Energy Ltd. His production and project development experience will be particularly helpful for the Board to progress Otto's vision of becoming internationally recognised as one of the best mid tier oil and gas companies.

I am confident that under Paul Moore's leadership and with our motivated and experienced management team, 2010 will be an active and successful year for Otto Energy and its shareholders.

Rick Crabb
Non Executive Chairman

# CHIEF EXECUTIVE OFFICER'S LETTER

Dear Shareholders,

I am pleased to have joined Otto Energy in July 2009 and deliver my first annual report as the Company's Chief Executive Officer.

2009 was a difficult year with high volatility in the oil price and reliability problems at the Galoc Oil Field. Conversely, we experienced ongoing exploration successes in Turkey and are now underway with the development of the onshore shallow gas fields at Edirne.

Elsewhere, in Argentina and Italy, our wildcat exploration programme was unsuccessful in finding hydrocarbons. It is likely that we will exit Argentina. Our plans to continue exploring in the highly prospective Po Valley in Italy are still being formulated having consideration to the hydrocarbon potential, cost of exploration, the market for gas and in context of Otto's other business opportunities.

Since joining Otto, I have focussed on three aspects of the Company's business:

1. Ensuring good industry practices are applied to the maturation of the exploration, development and production opportunities within our existing asset portfolio;
2. Realignment of functional skills and priorities to match needs in the current climate and to deliver on the commercialisation of the existing asset base; and
3. Cost control; ensuring we deliver our business outcomes cost effectively.

Looking forward, I see three focus areas for delivering improved shareholder value, which I will continue to elaborate on during 2009/10.

First, our goal is to improve production operations and generate enhanced earnings in the Galoc field via hardware upgrades, sound reservoir management, effective contractor relationships, and where feasible, further appraisal and sequential development. In addition we will bring into production our first onshore gas development in Turkey during the first half of 2010.

Second, we aim to capture further onshore appraisal/development opportunities during 2010 to build production supplementary to Galoc and Edirne and prior to capital commitments on future appraisal and development of our offshore portfolio in the Philippines.

Third, the highly prospective exploration portfolio in the Philippines, both offshore Palawan and in the East Visayan Basin will be matured. Our goal is to farm down in all our licences in a manner which facilitates cost effective exploration of these blocks.

In summary, over the current financial year I am committed to focusing on growth via a measured approach to projects, sound execution over a tighter geography and a cost effective corporate structure.

Paul Moore
CEO

# COMPANY OVERVIEW

Otto Energy is an exploration and production company that listed on ASX in December 2004. The Company has a growing exploration, development and production portfolio consisting of the Galoc Field, a producing offshore oil field; the Edirne Gas Project an onshore near term gas development and a number of exciting exploration leads and drillable prospects.

Outlined below is a summary of the Company's assets and key metrics for the 2009 financial year.

| Licence/Permit | Location | Status |
|---|---|---|
| **Operated** | | |
| SC50 (Calauit) | Philippines - Offshore | Discovery |
| SC51 | Philippines – Offshore | Exploration |
| SC55 | Philippines – Offshore | Exploration |
| SC69 | Philippines - Offshore | Exploration |
| **Non-Operated** | | |
| SC14C (Galoc) | Philippines - Offshore | Production |
| Edirne | Turkey - Onshore | Development |
| Cento Bastiglia | Italy – Onshore | Exploration |
| Santa Rosa | Argentina - Onshore | Exploration |

| Key Metrics | Year ended 30 June 2009 |
|---|---|
| Net Operated acreage | 16,322km² |
| - Combined number of mapped prospects and leads | >40 |
| Net Non-Operated exploration acreage | 3,152km² |
| - Combined number of mapped prospects and leans | >25 |
| Total number of exploration and appraisal wells drilled | 5 |
| - Number of discoveries | 3 |
| Otto's share of Galoc production[1] | 0.42 mmboe |
| Proved Reserves[1] | 1.20 mmboe |
| Proved plus Probable Reserves[1] | 1.87 mmboe |
| 2C Contingent Resource[1] | 6.07 mmboe |

1. Please refer to Reserve and Contingent Resource Estimate on page 22 for further details in respect to these estimates.

A review of the Company's projects and operations is presented in the following pages. Ongoing operations and plans for projects potentially change dependant on market conditions and as new data becomes available. Updates on current activities are available from Otto's website www.ottoenergy.com and through the ASX announcement platform.

# PRODUCTION

## Service Contract 14C – Galoc Block

The Galoc Oil Field is located in Service Contract 14C, Galoc Sub Block, offshore northwest Palawan, in the Philippines. The field is located in a proven oil and gas fairway in a water depth of approximately 290 metres.

Gross oil production from the Galoc Field for the financial year totalled over 2.2 million barrels since first oil commenced on 9 October 2008. At the date of this report, the two wells were producing at around 11,000 barrels of oil per day (bopd) on a natural decline from initial production rates of 17,000 bopd. Oil production was offloaded and delivered to refineries across the Asia Pacific region generating gross revenues of approximately US$106 million for the financial year. GPC's share of the gross oil production revenue for the year was used largely to repay the non-recourse portion of the GPC project debt facility and to fund its share of operating costs. As a result no distributions were made by GPC to its shareholders (Otto and Vitol Group) during the financial year. Regular distributions are however expected from GPC in 2010 now that the GPC project debt facility has been fully repaid.

Production at the Galoc Field was interrupted a number of times during the year principally due to adverse weather conditions and subsequent damage to the mooring and riser system. A hold back mooring system was installed on the FPSO in February 2009 to improve the station-keeping of the vessel during adverse weather conditions. This has resulted in decreased operating expenditure through fuel cost savings; increased production uptime; and a simpler process for more controlled disconnections. Further remediation work is contemplated to establish optimal production uptime at the field.

The Galoc Joint Venture issued a formal "Declaration of Commerciality" in June 2009 following the successful Extended Well Test, which resulted in the field reverting to the conventional fiscal terms of the governing Service Contract.

# PRODUCTION (Cont'd)

Galoc Phase 1 production to date encourages the Operator and Joint Venture to consider a Phase 2 development, which could involve an additional two wells in the northern portion of the structure providing a boost to production and access to undeveloped reserves. Further detailed analysis is however required before any investment decision is made in respect to a Phase 2 development.

Otto increased its indirect interest in the Galoc Project by 0.50% to 18.78% (previously 18.28%) in July 2009 as a result of GPC acquiring an additional 1.55% working interest in SC14C from two of the Filipino minority interest partners. This increased GPC's working interest in Galoc Oil Field from 58.29% to 59.84%.

**Participating interests (as at 1/9/09) in SC14C – Galoc Block are:**

| Participant | Participating Interest % |
|---|---|
| Galoc Production Company W.L.L (GPC)<br>Owned by;<br>Vitol Group 68.62%<br>Otto Energy 31.38% | 59.84473 and Operator |
| Nido Petroleum Philippines Pty Ltd | 22.87952 |
| The Philodrill Corporation | 7.21495 |
| Oriental Petroleum & Minerals Corporation/Linapacan Oil Gas & Power Corporation | 7.78505 |
| Forum Energy Philippines Corporation | 2.27575 |

# DEVELOPMENT

## TURKEY Edirne Licence, Thrace Basin

Otto holds a 35% interest in the Edirne Licence in the Thrace Basin. The licence is operated by joint venture partners and Joint Operators, Petroleum Exploration Mediterranean Int. (PEMI) (55%) and local Turkish company Petraco (10%).

The Thrace Basin is located in the European part of Turkey, to the west of Istanbul and the Sea of Marmara. This Tertiary Basin onshore Turkey is the country's most productive onshore gas province. 3D seismic was acquired over the central part of the licence in mid 2007, which identified potential gas bearing structures.

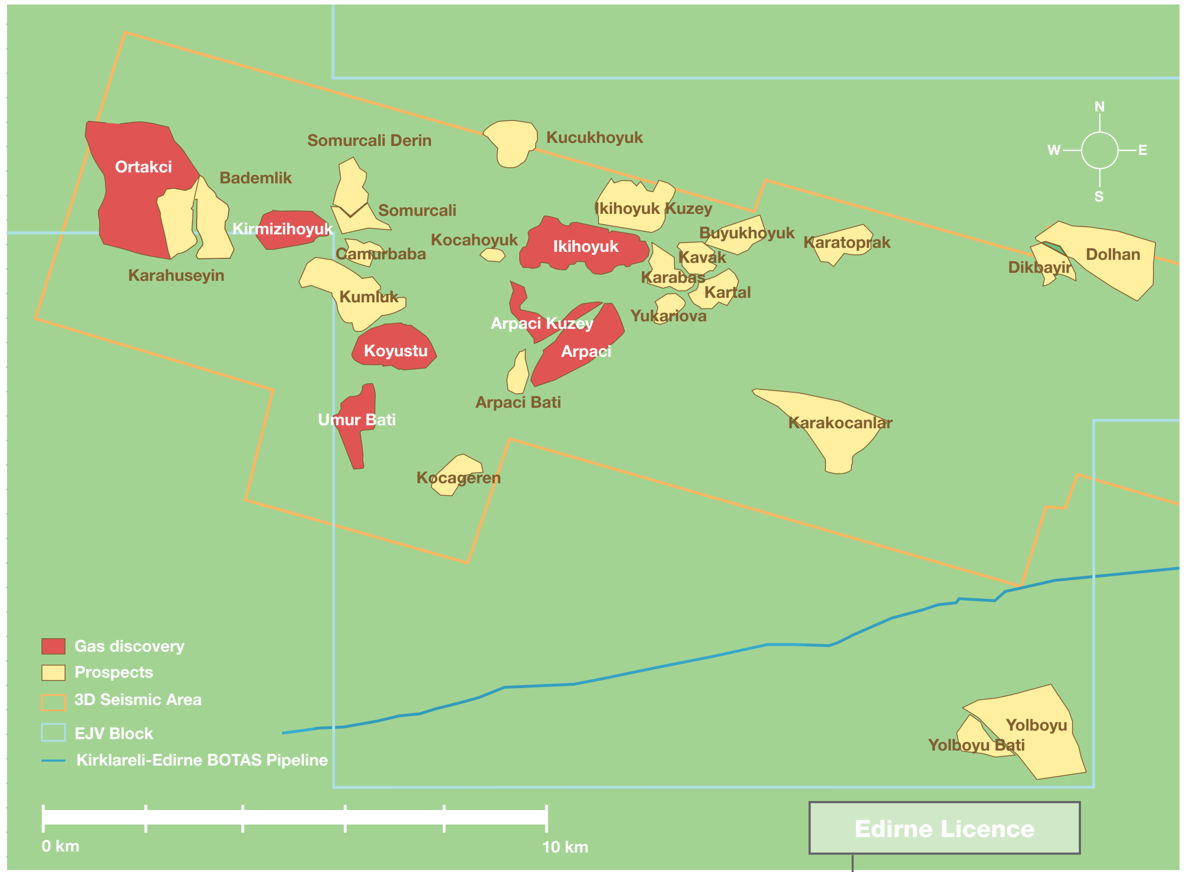
A total of eight gas discoveries have been made with a 100% success rate since Otto's original acquisition of 80% of the licence in 2004. In addition, two successful appraisal wells have been drilled, which have established deliverability of the reservoir for development.

The Edirne Joint Venture (EJV) is currently on track to monetise the reserves through the construction of a gas facility. PEMI have designed the gathering, treatment, processing and compression systems required to gather natural gas produced by the EJV and redeliver this for sale to a licensed end-user. PEMI are proposing to construct and operate facilities to provide for a minimum capacity of 14 Mmcf/d.

A Gas Sales Agreement is currently being negotiated by the EJV and will be in place before the commencement of production. First gas sales are currently expected during the first half of 2010.

**Edirne Block Participants:**

| | |
|---|---|
| Erdine Energy Limited (a 100% subsidiary of Otto Energy) | 35% |
| Petroleum Exploration Mediterranean Int. (a 100% subsidiary of TransAtlantic Petroleum via Incremental Petroleum) | 55% and Joint Operator |
| Petraco | 10% and Joint Operator |




| Well Name | Date Drilled | Total depth (mKB) | Flow Rate (Mmcf/d) |
|---|---|---|---|
| Kuzey Ikihoyuk-1 | 01 July 2009 | 389 | 0.42 |
| Ikihoyuk-2 | 12 June 2009 | 500 | 4.76 |
| Kirmizihoyuk-1 | 12 May 2009 | 500 | 4.26 |
| Arpaci-2A | 21 June 2008 | 525 | 0.98 |
| Ikihoyuk-1 | 26 April 2008 | 540 | 1.08 |
| Kuzey Arpaci-1 | 09 April 2008 | 540 | 2.4 |
| Ortakci-1 | 23 April 2008 | 542 | 2.53 |
| Koyustu-1 | 27 December 2006 | 617 | 0.6 |
| Arpaci-1 | 13 January 2006 | 509 | N/A |
| Bati Umur-1 | 8 December 2005 | 1052 | 0.8 |

# EXPLORATION & STATIC RESOURCES


## PHILIPPINES OFFSHORE PALAWAN BASIN

### Service Contract 55

SC55 covers an area of 9,000 km$^2$ in the southwest Palawan Basin. The block is located in water depths from 60m to 2,400m on a regional oil and gas fairway that extends from the productive Borneo offshore region in the southwest to the offshore Philippine production assets northwest of Palawan. Otto's Calauit and Calauit South oil discoveries (SC50) are the northern most known oil fields on this trend.

Palaeo-carbonate reefs of Oligocene to Early Miocene age are an established play type in the northwest Palawan Basin and these formations are also present in SC55. The Marantao structure is the largest identified prospect in SC55, of this proven play type, and is well delineated by modern, closely spaced 2D seismic. This prospect is analogous to the producing Malampaya Gas Field to the north and has potential prospective resources of several hundred million barrels of oil.

Miocene tectonic compression has created numerous structural traps which have been mapped at the Nido Limestone level. Thrust-fault closures also occur at levels where Miocene clastic reservoirs are likely to be present.

The Hawkeye Lead, identified on seismic acquired by Otto in 2007, is an example of this play type and has a direct-hydrocarbon-indicator (flat spot) strongly suggesting the presence of a gas cap. A number of oil fields along this proven hydrocarbon trend are overlain by a gas cap in the same producing reservoir.

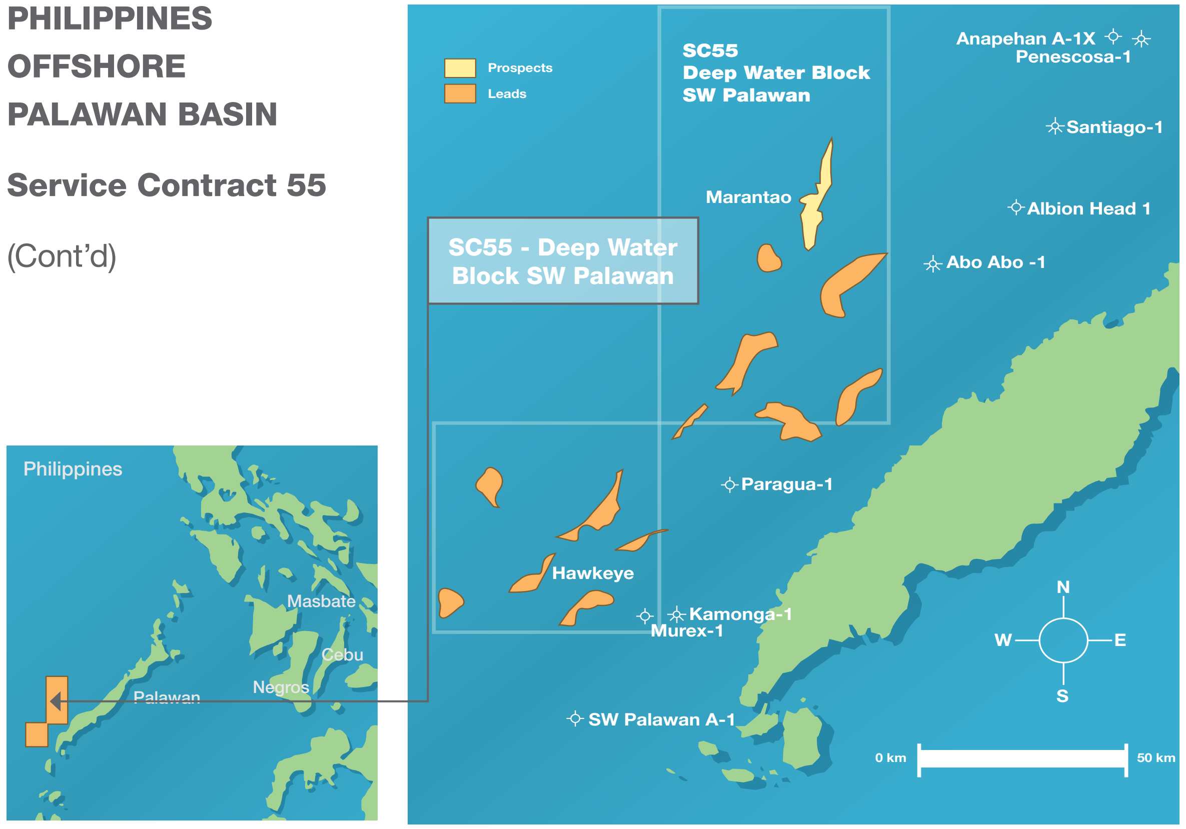
In addition, Miocene turbidites are interpreted in the basinal areas of SC55 and may form sizeable stratigraphic traps. Some drape closures have also been mapped at this level. Correlative reservoirs in offshore Sabah are excellent reservoirs with current production.

# EXPLORATION & STATIC RESOURCES (Cont'd)

## PHILIPPINES OFFSHORE PALAWAN BASIN

### Service Contract 55

(Cont'd)




The Department of Energy in the Philippines recently approved the request from the SC55 joint venture to revise the Work Programme for the current exploration sub-phase. The joint venture is contemplating a 3D seismic programme to mature the Hawkeye Lead and other leads prior to entering the next sub-phase in August 2010, which involves the drilling of one deep-water well.

Otto is seeking a partner to participate in the planned seismic programme and in subsequent drilling campaigns.

**SC55 Block Participants:**

| | |
|---|---|
| NorAsian Energy Limited (100% subsidiary of Otto) | 85% and Operator |
| TransAsia Oil and Energy Development Corporation | 15% (carried interest in first well) |

### Service Contract 50 – Calauit / Calauit South Oil Fields

SC50 contains the Calauit and Calauit South Oil Fields which were discovered in 1991 and 1992. The Calauit and Calauit South fields lie in shallow water depths that range from 50m to 100m and are situated at the northeast of the oil and gas prolific Palawan Basin.

During the year a site survey was undertaken of the proposed Calauit 2 drilling location and work continued on the commercial and economic review of appraisal and development options for the Calauit oil fields.

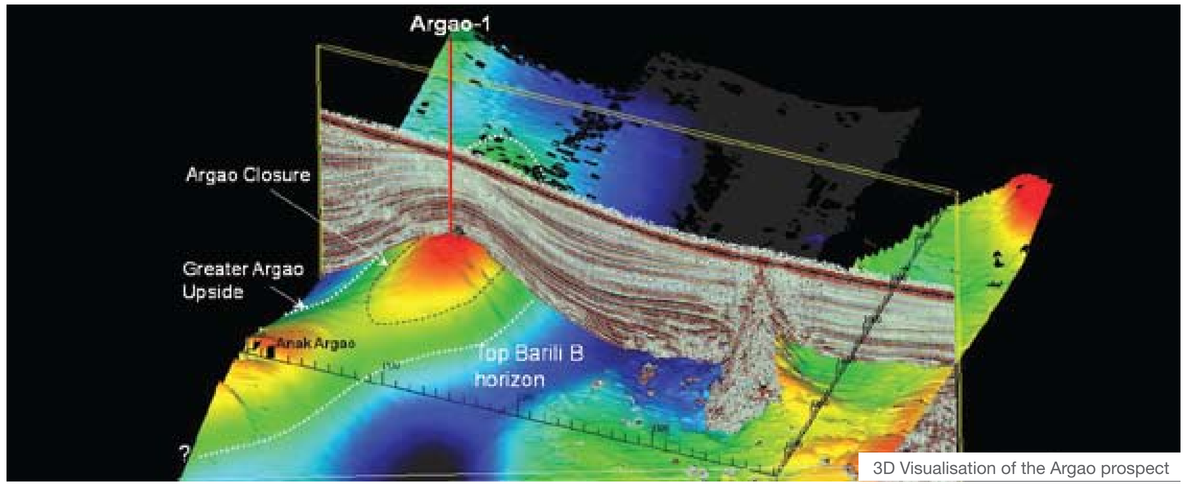
The Company was granted an extension to the drill commitment in the current sub-phase until March 2011 by the Philippines Department of Energy.

Otto/NorAsian is currently paying 100% for 99% beneficial interest in the block, carrying the Filipino partner through drilling of the first well.

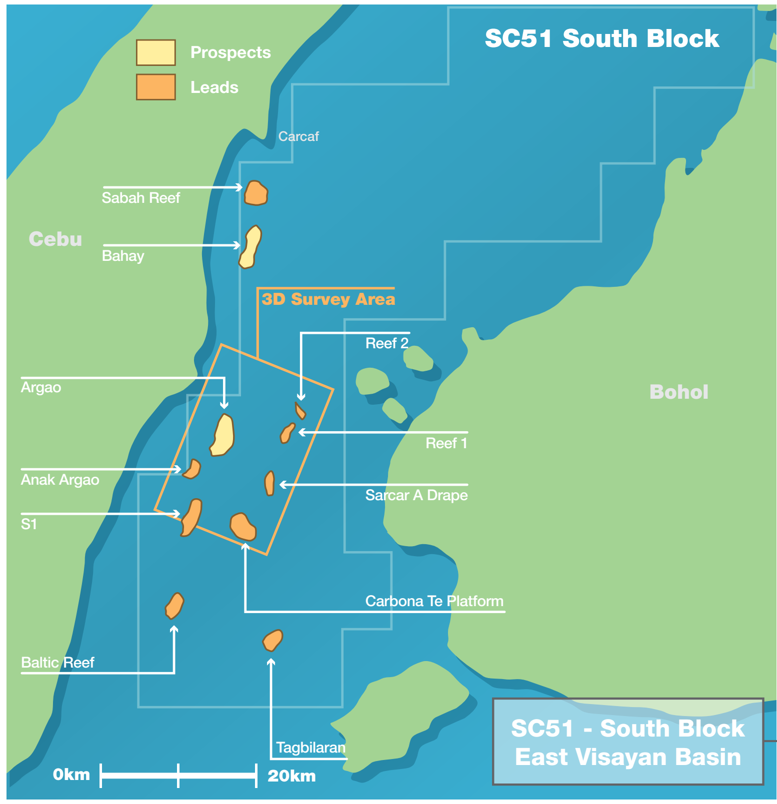
**SC50 Block Participants:**

| | |
|---|---|
| NorAsian Energy Limited (100% subsidiary of Otto) | 85% (Beneficial Interest 99%) and Operator |
| RGA Resources Inc | 15% (1% Overriding Royalty) |

# EXPLORATION & STATIC RESOURCES (Cont'd)

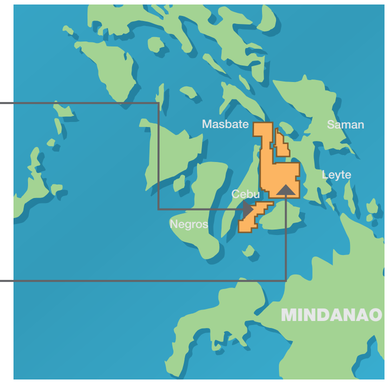


3D Visualisation of the Argao prospect




## SC51 Block Participants:

| | | |
|---|---|---|
| NorAsian Energy Limited (100% subsidiary of Otto) | 80% and Operator | |
| Alcorn Gold Resources Corporation | 9.32% | (carried interest through first well) |
| Trans Asia Oil and Energy Development Corporation | 6.67% | |
| PetroEnergy Resources Corporation | 4.01% | |




## PHILIPPINES
## EAST VISAYAN BASIN

### Service Contract 51

SC51 is situated in the East Visayan Basin in the central Philippines. The area consists of a northern and southern part with the two areas being separated by a distance of approximately 80km (of which the intervening area is SC69).

The large Argao and Bahay prospects are located in the south block with over 9 additional leads recently defined on 2D and 3D seismic.

During the past year Otto undertook preparatory site surveys of the proposed Argao 1 and Bahay 1 drilling locations. Environmental site assessments of these two locations were put on hold in October 2008 at the request of the Philippines Department of Energy and the Governor of Cebu whilst community and stakeholder consultation continued through to June 2009. The Philippines Department of Energy has extended the well commitment in the Service Contract to December 2010.

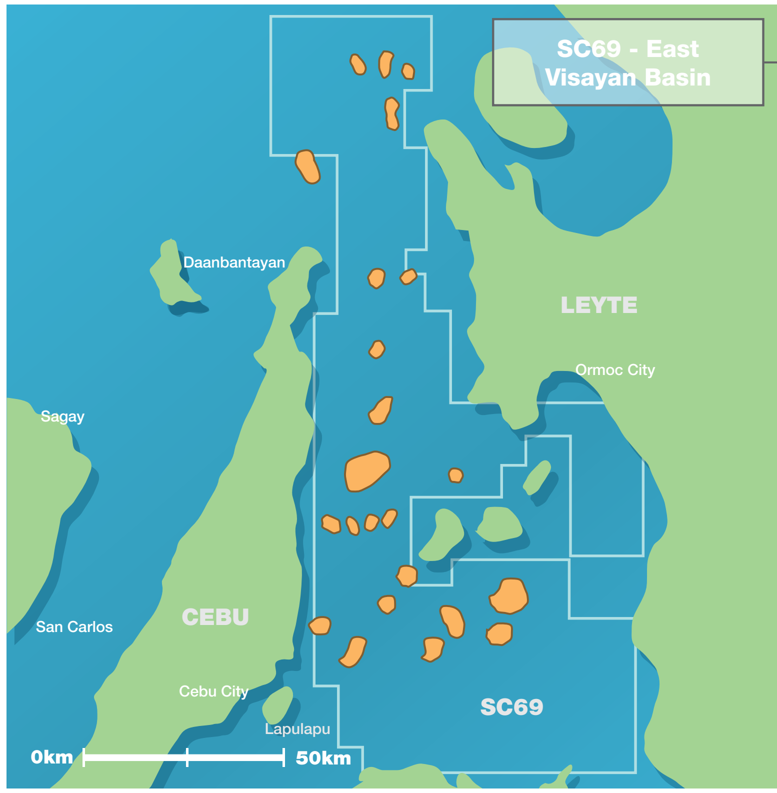
Otto is seeking farminees to earn an interest in SC51.

### Service Contract 69

SC69 is Otto's most recent Philippines offshore exploration licence and is located between the north and south blocks of SC51 offshore in the East Visayan Basin.

During the year, the Company has reprocessed approximately 2,700 km of vintage seismic data. Preliminary interpretation of the seismic data indicates a host of previously unidentified leads in this large block.

Primary exploration focus is on the Miocene/Pliocene reef play with potential for both oil and gas discoveries. Gas discoveries have been made offshore in Otto's adjacent SC51 licence (Villaba 1) and in several wells on the island of Cebu providing evidence for a working petroleum system in the basin.




## SC69 Block Participants:

| | |
|---|---|
| NorAsian Energy Limited (100% subsidiary of Otto) | 70% and Operator |
| Trans Asia Oil and Energy Development Corporation | 30% |

# EXPLORATION & STATIC RESOURCES (Cont'd)

## ITALY

### Cento - Bastiglia Exploration Permits

Otto Energy is earning its 50% working interest in the onshore Cento-Bastiglia Permits located near Bologna in the Po Valley region of northern Italy. Otto's joint venture partner and field Operator is Ascent Resources Plc.

The Po Valley is a well established hydrocarbon region for both oil and gas and the area is still considered highly prospective. The two adjacent Cento and Bastiglia Permits are surrounded by established hydrocarbon fields found on easily mapped structures in the 1960/70s. The permits are located between structural highs and the main trapping playtypes are porous channel and turbidite sands encased in source and sealing clays. Such traps are more difficult to locate, but are often very substantial in size. Several of such leads have been identified from previous seismic data.

Gazzata-1, the first exploration well for the joint venture, was drilled during May/June 2009. The well was drilled to a total depth of 2,840m and intersected a series of sand/shale sequences below 2,300 metres. Wireline logs confirmed the absence of commercial gas zones and the well was plugged and abandoned as a dry hole.

The Joint Venture is currently reviewing data from the Gazzata-1 well logs and pre-existing seismic with a view to ascertaining next steps for the future exploration programme.

**Cento-Bastiglia Permits Participants:**

| | |
|---|---|
| Otto Energy Ltd | Earning 50% |
| Ascent Resources Plc. | 50% and Operator |

## ARGENTINA

### The Santa Rosa Exploration Licence

The Santa Rosa Licence is located in the Cuyana Basin in the Province of Mendoza, Argentina. During the financial year Otto acquired a 32.48% shareholding in Cynthia Holdings Limited, which wholly owns Argentinean company Exploraciones Oromin SA (EOSA). EOSA holds 100% of the rights to explore and produce from the Santa Rosa block and is the Operator.

The exploration well "OLE.MD.SRE X-2001" was spudded on 15 July 2009 and reached a total depth of 1,270m in basement approximately 11 days later. Electric log evaluation confirmed that the well did not encounter hydrocarbons. The results indicate that the target reservoir zones are not present at this crestal well location.

EOSA is currently studying the well data to determine whether potential stratigraphic traps on the western and southern flank of the Santa Rosa dome warrant further investigation.

During the year Otto elected not to increase its shareholding in Cynthia Holdings Limited to 41.24%, a right it had under the original farmin agreement with Oromin. It is likely that Otto will undertake a country exit from Argentina in the 2009-10 financial year.

**Santa Rosa Licence Participants:**

| | |
|---|---|
| Exploraciones Oromin S.A. | 100% |
| **Owned (via shareholding in Cynthia Holdings Ltd) by;** | |
| Otto Energy | 32.48% |
| Oromin Explorations Ltd | 67.52% and Operator |

# RESERVES & CONTINGENT RESOURCES ESTIMATE

**OTTO PROVED (1P) RESERVES as at 30 June 2009**

**1P Reserves [2] (Otto share) by Area**

| | Crude Oil mmbbl | Sales Gas Bcf | Sales Gas mmboe | Total mmboe |
|---|---|---|---|---|
| Philippines - Galoc Field [5] | 0.93 | 0.00 | 0.00 | 0.93 |
| Turkey - Edirne Licence | 0.00 | 1.59 | 0.27 | 0.27 |
| TOTAL | 0.93 | 1.59 | 0.27 | 1.20 |

**OTTO PROVED AND PROBABLE (2P) RESERVES as at 30 June 2009**

**Proven plus Probable (2P) Reserves [3] (Otto share) by Project Area**

| | Crude Oil mmbbl | Sales Gas Bcf | Sales Gas mmboe | Total mmboe |
|---|---|---|---|---|
| Philippines - Galoc Field [5] | 1.46 | 0.00 | 0.00 | 1.46 |
| Turkey - Edirne Licence | 0.00 | 2.47 | 0.41 | 0.41 |
| TOTAL | 1.46 | 2.47 | 0.41 | 1.87 |

**OTTO CONTINGENT RESOURCES (2C) as at 30 June 2009**

**2C Resources [4] (Otto share) by Area**

| | Crude Oil mmbbl | Sales Gas Bcf | Sales Gas mmboe | Total mmboe |
|---|---|---|---|---|
| Philippines - Galoc Field [6] | 1.13 | 0.00 | 0.00 | 1.13 |
| Philippines - Calauit Field [6] | 4.85 | 0.00 | 0.00 | 4.85 |
| Turkey - Edirne Licence | 0.00 | 0.53 | 0.09 | 0.09 |
| TOTAL | 5.98 | 0.53 | 0.09 | 6.07 |

**MOVEMENT IN RESERVE AND RESOURCE CATEGORIES OVER THE PERIOD 30 JUNE 08 TO 30 JUNE O9**

**Otto's Reserves & Contingent Resources Summary**

| Galoc Field - SC14C (18.78%) | 30-Jun-08 | Production | Revisions & Exploration Success | Contingent Resources converted to Reserves | Acquisitions and Divestment | 30-Jun-09 |
|---|---|---|---|---|---|---|
| | mmboe | mmboe | mmboe | mmboe | mmboe | mmboe |
| 2P Reserves | 3.42 | 0.42 | -1.58 | 0.00 | 0.04 | 1.46 |
| 2C Contingent Resources | 0.00 | - | 1.10 | 0.00 | 0.03 | 1.13 |
| **Calauit Field - SC51 (85%)** | mmboe | mmboe | mmboe | mmboe | mmboe | mmboe |
| 2P Reserves | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| 2C Contingent Resources | 4.85 | - | 0.00 | 0.00 | 0.00 | 4.85 |
| **Edirne Gas Project (35%)** | mmboe | mmboe | mmboe | mmboe | mmboe | mmboe |
| 2P Reserves | 0.00 | 0.00 | 0.41 | 0.00 | 0.00 | 0.41 |
| 2C Contingent Resources | 0.00 | - | 0.09 | 0.00 | 0.00 | 0.09 |
| **All Project Areas** | mmboe | mmboe | mmboe | mmboe | mmboe | mmboe |
| 2P Reserves | 3.42 | 0.42 | -1.17 | 0.00 | 0.04 | 1.87 |
| 2C Contingent Resources | 4.85 | - | 1.19 | 0.00 | 0.03 | 6.07 |

## OTTO RESERVE ESTIMATES (30 JUNE, 2009)

Otto reports its petroleum reserve and resource estimates using definitions and guidelines published in the Society of Petroleum Engineers Inc./World Petroleum Congresses/American Association of Petroleum Geologists/Society of Petroleum Evaluation Engineers (SPE/WPC/AAPG/SPEE) Petroleum Resources Management System (March 2007).

In 2009, the Galoc 1P and 2P Reserves were independently audited by RISC (April, 2009). This audit was contracted by the Operator, the Galoc Production Company. Since then, Otto and the Operator have updated the reserve estimates of the Galoc Field with additional data available from down-hole pressure measurements in the two producing wells together with production data. Reserve and contingent resource estimates outlined above for the Galoc Field represent Otto estimates and not necessarily those of its joint venture partners.

Otto's reserve and contingent resource estimates for the gas fields in the Edirne licence in Turkey are based upon internal technical assessments incorporating results of the most recent drilling campaign in the Edirne licence.

Technical assessments to determine the 2C Contingent Resource estimates for the Calauit Field were undertaken by qualified in-house technical specialists.

Otto reports reserves net of the petroleum required for processing and transportation to the customer, and in the case of Service Contracts (such as the Philippines), net of the "Government Share". Reserves reported are based on, and accurately reflect, information compiled by full-time employees of the Company who have the requisite qualifications and experience prescribed by the ASX Listing Rules.

# RESERVES & CONTINGENT RESOURCES ESTIMATE (Cont'd)

## Movements in Reserve and Resource categories over the period 30 June 2008 to 30 June 2009

### Galoc

The Galoc gross 2P Reserve estimate at 30 June 2008, prior to production having commenced, was 23.4 mmstb. Of this, Otto assess that 18.7 mmstb is the "Contractor Share" (Gross) and 4.7 mmstb is the "Government Share" (Gross). As at 30 June 2009, Otto reports its effective working interest of the Contractor Share of the Reserves (2P = 1.46 mmstb).

2P Reserves have been reduced during the period as not all of the 2P Reserves reported in 2008 are now considered to be developed (-1.58 mmstb). However, work undertaken in-house during the period identifies (undeveloped) 2C Contingent Resources added as an upward revision (+1.1 mmstb). In addition, Otto's share of Galoc Reserves and Contingent Resources increased during the period due to the acquisition of part interests in Alcorn & PetroEnergy's working interests in the Galoc Field (0.07 mmstb).

### Calauit

Calauit 2C Contingent Resources remain unchanged during the period at 4.85 mmstb.

### Edirne Licence

As at 30 June 2008, Otto did not have any reported Reserves in the Edirne Licence. Additions to 2P Reserves during the period total 0.41 mmboe (2.47 Bcf) of gas. This 2P Reserve estimate is the arithmetic aggregation of the individual 2P Reserves of the following gas discoveries; Arpaci, Ikihoyuk, Kuzey Arpaci, Ortakci, Koyustu, Bati Umur. Additional 2C Contingent Resources of 0.09 mmboe (0.53 Bcf) are considered additions during the period as a result of the more recent Kirmizihoyuk and Kuzey Ikihoyuk gas discoveries. The resources of these two fields are considered contingent at this time as the results of the wells are very recent, studies are ongoing, and these wells are yet to be incorporated into the Edirne Gas Development Plan.

## Notes to the Reserves Statement:

1. Reserves are those quantities of petroleum anticipated to be commercially recoverable by application of development projects to known accumulations from a given date forward under defined conditions. Reserves must further satisfy four criteria: they must be discovered, recoverable, commercial, and remaining (as of the evaluation date) based on the development project(s) applied.
2. Proven (1P) reserves are those reserves that, to a high degree of certainty (90% confidence), are recoverable. There is relatively little risk associated with these reserves. Proven developed reserves are reserves that can be recovered from existing wells with existing infrastructure and operating methods. Proven undeveloped reserves require development.
3. Proven plus Probable (2P) reserves are those reserves that analysis of geological and engineering data suggests are more likely than not to be recoverable. There is at least a 50% probability that reserves recovered will exceed Proven plus Probable reserves.
4. Contingent Resources are those quantities of hydrocarbons which are estimated, on a given date, to be potentially recoverable from known accumulations, but which are not currently considered to be commercially recoverable. Contingent Resources may be of a significant size, but still have constraints to development. These constraints, preventing the booking of reserves, may relate to lack of gas marketing arrangements or to technical, environmental or political barriers. 2C Contingent Resources are where there is at least 50% probability that the quantities exceed this estimate. Contingent Resources do not always mature to Reserves and do not necessarily represent future Reserves bookings.
5. The Philippines "Government Share" of Galoc 1P and 2P Reserves has been deducted from Otto's indirect interest (18.78%).
6. The "Government Share" has not been determined for "2C Resources" as these resources are not subject to a development plan.
7. "mmbbl" means millions of barrels of oil at standard oilfield conditions of 14.696 psi (101.325kPa) and 60°Fahrenheit (15.56° Celsius).
8. "Bcf" means billions of cubic feet of gas at standard oilfield conditions of 14.696 psi (101.325kPa) and 60°Fahrenheit (15.56° Celsius).
9. "mmboe" means millions of barrels of oil equivalent. In common with international practice, dry gas volumes are converted to oil equivalent volumes via a constant conversions factor, for which Otto adopts 6 Bcf of dry gas to one mmboe.
10. Unless otherwise stated, Reserve and Resource estimates are net to Otto.

## Governance

The Reserve Statement has been compiled by Mr. Craig Martin, Otto's Chief Operating Officer, who is a full-time employee of the Company. Mr. Martin has more than 20 years of relevant experience and is qualified in accordance with the ASX Listing Rule 5.11. Mr. Martin has consented to the form and context that this statement appears.

# SUMMARY OF ASSETS

| Asset / Service Contract | OEL Working Interest | Joint Venture Partners | | Notes |
|---|---|---|---|---|
| **The Philippines** | | | | |
| SC50<br>Northwest Palawan – includes Calauit & Calauit South Oil Fields | 85% | RGA Resources Inc ("RGA") | 15% | Otto/NorAsian currently paying 100% for 99% beneficial interest.<br>There is a 1% Gross Overriding Royalty to RGA on Otto/NorAsian's share. |
| SC51<br>Exploration block, East Visayan Basin | 80% | Alcorn Gold Resources<br>TransAsia Oil & Energy<br>PetroEnergy | 9.32%<br>6.67%<br>4.01% | Otto/NorAsian carrying Filipino partners through drilling of first well.<br>There is a 1% Gross Overriding Royalty to RGA on Otto/NorAsian's share. |
| SC55<br>Exploration block, Southwest Palawan Basin | 85% | TransAsia Oil & Energy | 15% | Otto/NorAsian carrying Filipino partners through drilling of first well.<br>There is a 1% Gross Overriding Royalty to RGA on Otto/NorAsian's share.<br>TransAsia also has a right to acquire an additional 5% equity |
| SC69<br>Exploration block, East Visayan Basin | 70% | TransAsia Oil & Energy | 30% | Otto/NorAsian paying 70%<br>No royalties exist |
| SC14C<br>Galoc Block<br>Northwest Palawan | 18.77% indirect interest through a 31.38% share-holding in Galoc Production Company WLL (GPC) | GPC (Operator)<br>Nido Petroleum<br>Phil Co's | 59.84%<br>22.88%<br>17.3% | A subsidiary of the Vitol Group owns the remaining stake in GPC (68.62%). |
| **Turkey** | | | | |
| Edirne Licence | 35% | Petroleum Exploration Mediterranean Int. (PEMI) (Joint Operator)<br>Petraco Petroleum (Joint Operator) | 55%<br>10% | PEMI is a wholly owned subsidiary of Incremental Petroleum, which was acquired by TransAtlantic Petroleum in March 2009.<br>Otto carrying 3.5% of Petraco's costs refundable from production. |
| **Italy** | | | | |
| Cento-Bastiglia Licences | Earning 50% | Ascent Resources Plc (Operator) | 50% | |
| **Argentina** | | | | |
| Santa Rosa Licence | 32.48% holding in Cynthia Holdings Ltd, which owns 100% of the rights to the licence. | Oromin Explorations Ltd (as shareholder in Cynthia) | 67.52% | Cynthia Holdings Ltd. is a British Virgin Islands company that is jointly owned with Oromin Explorations Ltd. Exploraciones Oromin S.A. is a subsidiary of Cynthia Holdings Ltd. |

# ANNUAL FINANCIAL REPORT 2009

# DIRECTORS' REPORT

RUFINO BOMASANG
DIRECTOR
(NON - EXECUTIVE)

JAAP POLL
DIRECTOR
(NON - EXECUTIVE)

RICK CRABB
CHAIRMAN
(NON – EXECUTIVE)

IAN MACLIVER
DIRECTOR
(NON - EXECUTIVE)

JOHN JETTER
DIRECTOR
(NON – EXECUTIVE)

Your Directors present their report on the consolidated entity ("Otto Energy"), consisting of Otto Energy Limited ("the Company") and the entities it controlled at the end of, or during, the financial year ended 30 June 2009.

## Directors

The names of the Directors in office and at any time during, or since the end of the year are:

Mr Rick Crabb

Mr Rufino Bomasang

Mr John Jetter

Mr Ian Macliver

Dr Jaap Poll

Mr John Zadnik (Alternate Director for Rick Crabb)

Directors have been in office since the start of the financial year to the date of this report unless otherwise stated.

## Company Secretary

The following person held the position of Company Secretary at the end of the financial year:

Ms Emma McCormack.

## Principal Activities

The principal activities of the consolidated entity during the financial year were investment in oil and gas exploration and development in Turkey, the Philippines, Italy and Argentina.

No significant change in the nature of these activities occurred during the financial year.

## Operating Results

The consolidated loss of the consolidated entity for the financial year, after providing for income tax, amounted to $57,348,777 (2008: loss of $10,699,873). This result is after recognising an unrealised foreign exchange loss of $481,389 (2008: loss of $6,399,184).

## Dividends Paid or Recommended

The Directors recommend that no dividend be paid for the year ended 30 June 2009, nor have any amounts been paid or declared by way of dividend since the end of the previous financial year.

## Review of Operations

Otto Energy is an oil and gas exploration and production company with a growing exploration, development and production portfolio consisting of the Galoc Field a producing offshore oil field, the Edirne Gas Project an onshore near term gas development and a number of exciting exploration leads and drillable prospects. An overview of the of the Company's production, development and exploration operations is summarised below.

The Company appointed Mr Paul Moore as its Chief Executive Officer on 1 July 2009. Paul has extensive experience in the oil and gas industry with 27 years in operating oil and gas companies, including 17 years in executive management roles.

### Production

The Company has an 18.78% indirect interest in the Galoc Oil Field. This indirect interest is held via a 31.38% shareholding in the Galoc Production Company W.L.L. (GPC), the Operator, which holds 59.84% working interest in the field. The Galoc Oil Field is located offshore northwest Palawan, in the Philippines. The field is located in a proven oil and gas fairway in a water depth of approximately 290 metres.

The Galoc Oil Field has produced over 2.2 million barrels since it commenced oil production on 9 October 2008. At the time of this report, the two wells were producing at around 11,000 barrels of oil per day (bopd) on natural decline from initial production rates of 17,000 bopd. The field's oil production is supported by solution gas drive.

Production uptime at the Galoc Field during the year was adversely impacted by a combination of poor weather conditions and damage to the mooring and riser system. The FPSO and mooring were upgraded to better maintain station during typhoon and monsoon influence however further remediation work is still required to improve production uptime.

### Development

Otto Energy holds a 35% in the Edirne Licence in the Thrace Basin, located in the European part of Turkey, to the west of Istanbul and the Sea of Marmara. The Joint-Operators of the Edirne Licence are Petroleum Exploration Mediterranean Int. (PEMI) (55%) and local Turkish company Petraco (10%).

Since Otto's original acquisition of 80% of the licence in 2004, a total of eight gas discoveries have been made with a 100% success rate. In addition, two successful appraisal wells have been drilled, which have established deliverability of the reservoir for development.

The Edirne Joint Venture (EJV) is currently on track to monetise the reserves identified from this successful exploration campaign through the construction of a gas facility. PEMI have designed the gathering, treatment, processing and compression systems required to gather natural gas produced by the EJV and redeliver for sale such gas to a licensed end-user. PEMI are constructing and will operate facilities to provide for a minimum 14 Mmcf/d capacity.

A Gas Sales Agreement and a Gas Gathering and Processing Agreement are currently being negotiated and will be in place before commencement of production.

# DIRECTORS' REPORT (Cont'd)

## Review of Operations (Cont'd)

### Exploration

#### Philippines

The Company's exploration licenses in the Philippines comprise SC50, 51, 55 and 69. Revised work programmes and budgets for SC50, 51 and 55 were approved by the Philippines Department of Energy during the year which has allowed the Company to defer some of its major drilling commitments including the deep water well for SC55 which has been deferred until August 2011.

SC55 covers an area of 9,000 km$^2$ located in the southwest Palawan Basin and is considered to be one of the Company's most prospective licences. The block is located in water depths of 60m to 2,400m on a regional oil and gas fairway that extends from the productive Borneo offshore region in the southwest to the offshore Philippine production assets northwest of Palawan. Otto's Calauit and Calauit South oil discoveries are the northern most known oil fields on this trend.

SC50 contains the Calauit and Calauit South oil fields which lie in water depths of 50m to 100m in the northwest Palawan Basin. During the year a site survey was undertaken on the proposed Calauit 2 drilling location and work continued on the commercial and economic review of appraisal and development options for the Calauit oil fields.

During the past year Otto undertook preparatory site surveys of the proposed Argao 1 and Bahay 1 drilling locations in SC51. The Company also reprocessed 2,700 line-km of vintage seismic data from SC69, which was designed to validate over 20 leads identified within the block by previous operators.

#### Italy

Otto is earning a 50% working interest in the onshore Cento-Bastiglia Permits located near Bologna in the Po Valley region of northern Italy during the year. Otto's joint venture partner and field Operator is Ascent Resources Plc.

In May/June 2009 the first exploration well for the joint venture (Gazzata 1) was drilled. The Gazzata prospect had a seismic amplitude anomaly mapped on several seismic lines all displaying what was interpreted as a gas filled sand body with a common gas/water contact. The well was drilled to a total depth of 2,840m. Wireline logs confirmed the absence of commercial gas zones and the well was plugged and abandoned as a dry hole. Data from the Gazzata well logs and pre-existing seismic is currently being reviewed with a view to ascertaining next steps for the future exploration programme.

#### Argentina

During the financial year Otto earned a 32.48% shareholding in Cynthia Holdings Limited, which wholly owns Argentinean company Exploraciones Oromin SA (EOSA). EOSA holds 100% of the rights to explore and produce from the Santa Rosa block and is Operator. The Santa Rosa block is located in the Cuyana Basin in the Province of Mendoza, Argentina.

The first exploration well on the Santa Rosa block spudded on 15 July 2009 and reached a total depth of 1,270m. This exploration well however also proved unsuccessful with electric log evaluation confirming that the well did not encounter hydrocarbons.

## Financial Position

Otto Energy ended the 2009 financial year with a solid financial position with no debt and cash reserves $13.1 million.

The net assets of the consolidated entity have decreased by $6.8 million, from $106.6 million at 30 June 2008, to $99.8 million at 30 June 2009. The year over year change mainly reflects the increase in issued capital, net of share issue costs, the accounting loss of $57.3 million, a $1.8 million net change in share based payment reserves and $14.9 million net change in the foreign currency translation reserve.

The net loss for the year ended 30 June 2009 included non-cash impairment expense of $49.3 million. This impairment expense relates predominantly to a $34.8 million write down associated with the Company's investment in the Galoc Oil Field, which is now currently carried at $7.5 million. The impairment relates only to the Phase 1 operations at Galoc and is not reflective of the significant additional value expected to arise from a potential future Phase 2 expansion of the Galoc Field. Whilst technical and commercial fundamentals currently support a future potential stage two development this additional value cannot be considered when assessing the carrying value of the investment as the development is yet be fully evaluated and approved.

During the year the Company issued 593,530,089 shares:

- 578,530,089 shares in placements and on conversion of options, raising cash of $32.34 million (before share issue costs); and
- 15,000,000 shares as part of the consideration for the buy back of the 5% gross overriding royalty assessable on future production revenues generated from the Service Contract (SC) SC50, SC51, SC55 and any new Service Contracts.

The funds were principally used to repay the shareholder and Director loans drawn during the year, fund exploration wells in Italy and Argentina, continue development work in Turkey and for general working capital purposes.

The Directors believe the Group is in a strong and stable financial position to continue expanding and growing its current operations.

## Significant Changes in State Of Affairs

No significant changes in the consolidated entity's state of affairs occurred during the financial year.

## After Balance Date Events

On 9 July 2009, the company announced that Galoc Production Company W.L.L ("GPC") has entered into an agreement to acquire an additional 1.55% working interest in the Galoc oil field. The acquisition increases GPC's working interest in the Galoc oil field from 58.29% to 59.84% and as a result the company's indirect interest in GPC will increase by 0.49% to 18.77%. The acquisition follows the decision by GPC, to acquire the interests of minority partners of the joint venture. The cost to the company for its share will be approximately $500,000 (US $390,170) which will be paid via proceeds from Galoc production.

## Future Developments, Prospects and Business Strategies

To further improve the consolidated entity's financial position and maximise shareholders wealth, the following developments are intended to be implemented:

In the Philippines, Otto, through its wholly owned subsidiary NorAsian Energy, will continue with exploration programmes in each of its Service Contract areas. These programmes include where appropriate further seismic acquisition for interpretation and drilling. The Company will continue to seek farm-in partners to assists in funding the drilling programmes in SC50, SC51 and SC55. A Phase II development at the Galoc Oil Field is also being reviewed and matured by the Company and GPC. This may involve an additional two wells in the northern portion of the structure to boost production and access undeveloped reserves.

In Turkey, the Company is proceeding with the gas field development in the Edirne license area and first gas sales are expected during 2010.

The Company's investments in Italy and Argentina are in the process of being reviewed.

These developments are expected to assist in the achievement of the consolidated entity's short-term goals to create a successful oil company with early cash flow to fund its ongoing financial requirements with minimum equity dilution.

# DIRECTORS' REPORT (Cont'd)

## Information on Directors and Executives

| | |
|---|---|
| **Mr Rick Crabb** | - Chairman (Non Executive) |
| Qualifications | - BJuris (Hons); LLB; MBA |
| Experience | - Mr Rick Crabb holds degrees in law and business administration from the University of Western Australia. He practised as a solicitor from 1980 to 2004, specialising in resources, corporate and commercial, with considerable offshore experience. Mr Crabb now focuses on his public company directorships and investments. |
| Interest in Shares and Options | - 13,370,052 ordinary shares of Otto Energy Limited; options to acquire 1,500,000 ordinary shares and 625,000 performance shares. |
| Special Responsibilities | - Audit and Compliance |
| Directorships held in other listed entities | - During the past three years Mr Crabb's directorships in other listed entitles are as a current director of Royal Resources Ltd from 23 February 2004 to 11 August 2009, Golden Rim Resources Ltd from 22 August 2001, Ashburton Minerals Ltd from 1 September 1999, Paladin Energy Ltd from 8 February 1994, former director of Port Bouvard Ltd from 2 December 1996 to 23 April 2009 and Thundelarra Exploration Ltd from 8 September 2003 to 13 June 2007. |

| | |
|---|---|
| **Mr Rufino Bomasang** | - Director (Non Executive) |
| Qualifications | - BSc (Min.Eng), Master in Business Economics (Phil) |
| Experience | - Mr Bomasang is a mining engineer, having worked in recent years as an International Energy and Mining Consultant, focusing on the development of untapped indigenous energy resources in the Philippines. From 1996 to 2004 Mr Bomasang was President and CEO of Philippine National Oil Company-Exploration Corporation (PNOC-EC), where he was responsible for top level management of PNOC-EC's operations. Mr Bomasang previously worked with the United States Agency for International Development as an Energy Consultant, providing technical assistance to the Philippine Department of Energy and as Senior Advisor to the Department of Energy Gas Office. Mr Bomasang is currently Non Executive Chairman of NorAsian Energy Limited, a subsidiary of Otto Energy Limited. |
| Interest in Shares and Options | - Options to acquire 1,000,000 ordinary shares |
| Directorships held in other listed entities | - Mr Bomasang has not been a director of any other Australian listed entities in the past three years. |

| | |
|---|---|
| **Mr John Jetter** | - Director (Non Executive) |
| Qualifications | - B. Law, B. Econ, INSEAD |
| Experience | - Mr Jetter has extensive international finance and M&A experience being the former Managing Director, CEO and head of investment banking of JPMorgan in Germany and Austria, and a member of the European Advisory Council, JP Morgan London. He held various senior positions with JPMorgan throughout Europe, during which time he focused his attention on major corporate clients and advised on some of Europe's largest corporate transactions. He also held a number of other board positions including Chairman of the Board of Rodenstock AG, Germany, Deputy Chairman of the Board of European Business School and Chairman of the Finance Facility, Oestrich-Winkel, Germany. |
| Interest in Shares and Options | - 19,089,175 ordinary shares of Otto Energy Limited and options to acquire 6,000,000 ordinary shares. |
| Directorships held in other listed entities | - Mr Jetter has not been a director of any other Australian listed entities in the past three years. |

| | |
|---|---|
| **Mr Ian Macliver** | - Director (Non Executive) |
| Qualifications | - B.Com, CA, F Fin, MAICD |
| Experience | - Mr Macliver is managing director of Grange Consulting Group Pty Ltd which provides specialist corporate advisory services to both listed and unlisted companies. He has many years experience as a senior executive and director of both resource and industrial companies, with particular responsibility for capital raising and other corporate initiatives. Mr Macliver is a director of various listed and unlisted companies and is the Chairman of the Company's Audit and Compliance Committee. |
| Interest in Shares and Options | - 6,306,942 ordinary shares of Otto Energy Limited and options to acquire 3,500,000 ordinary shares |
| Special Responsibilities | - Audit and Compliance |
| Directorships held in other listed entities | - During the past three years Mr Macliver's directorships in other listed entities are current chairman of Stratatel Limited since July 2000, non-executive director of Mount Gibson Iron Limited since February 2001, Port Bouvard Limited since December 1994 and Empire Beer Group Limited since 23 May 2006 and former director of Bioprospect Limited from February 2000 to April 2007. |

# DIRECTORS' REPORT (Cont'd)

## Information on Directors and Executives (Cont'd)

| | |
|---|---|
| **Dr Jaap Poll** | - Director (Non Executive) |
| Qualifications | - BSc, MSc and PhD Geology |
| Experience | - Dr Jaap Poll is a geologist with a distinguished 40 year career in petroleum exploration and production management worldwide. He has a PhD in Structural Geology, is an Accredited Member of the American Association of Petroleum Geology (AAPG), a Distinguished Member of the Petroleum Exploration Society of Australia (PESA) and is an accredited arbitrator and mediator. Dr Poll has extensive work experience in the Middle East, Europe, Central and South America, Africa, Asia and Australia and is the founder of the company. |
| Interest in Shares and Options | - 13,544,206 ordinary shares of Otto Energy Limited, options to acquire 3,000,000 ordinary shares, 1,250,000 performance shares and 4000 converting performance shares. |
| Directorships held in other listed entities | - Dr Poll has not been a director of any other Australian listed entities in the past three years. |

| | |
|---|---|
| **Mr John Zadnik** | - Alternate Director for Mr Rick Crabb (Non Executive) |
| Qualifications | - Dip. Cart, Dip. Eng Surv, Dip. RE Management, Lic. Surv |
| Experience | - Mr Zadnik is a licensed cadastral, mining and engineering surveyor, real estate developer and project manager. Mr Zadnik has been involved in the mining industry for 40 years, including the formation and management of several listed and unlisted public companies in Australia and Canada. He has successfully managed his own group of companies for 40 years and is an experienced director. |
| Interest in Shares and Options | - 5,369,000 ordinary shares of Otto Energy Limited; options to acquire 500,000 ordinary shares and 625,000 performance shares. |
| Special Responsibilities | - Alternate Director for Mr Rick Crabb |
| Directorships held in other listed entities | - Mr Zadnik has not been a director of any other Australian listed entities in the past three years. |

| | |
|---|---|
| **Ms Emma McCormack** | - Company Secretary |
| Qualifications | - B.Com. CA. SA Fin |
| Experience | - Ms McCormack is a senior executive at Grange Consulting, where she specialises in providing corporate and strategic advice, due diligence investigations, corporate compliance and valuation advice. Ms McCormack has project managed the listing of a number of companies on ASX and has been involved in various private and seed capital raisings.<br><br>Prior to joining Grange Consulting, Ms McCormack was an executive at KPMG Corporate Finance where she was involved in a range of corporate advisory engagements gaining extensive experience in financial and strategic analysis, due diligence reviews, project financing and financial modelling.<br><br>Ms McCormack is a Chartered Accountant and senior associate of the Financial Services Institute of Australia. |
| Interest in Shares and Options | - 405,000 ordinary shares of Otto Energy Limited and options to acquire 500,000 ordinary shares. |

| Name | Position Held | Key Appointment Dates | Period in Office |
|---|---|---|---|
| Mr Rick Crabb | Non-Executive Chairman | Appointed 19 November 2004 | 4 yrs, 10 mths |
| Mr Rufino Bomasang | Non-Executive Director | Appointed 18 August 2006 | 3 yrs, 1mth |
| Mr John Jetter | Non- Executive Director | Appointed 12 December 2007 | 1 yr, 10 mths |
| Mr Ian Macliver | Non-Executive Director | Appointed 7 January 2004 | 5 yrs, 8 mths |
| Dr Jaap Poll | Non-Executive Director | Appointed 19 November 2004 | 4 yrs, 10 mths |
| Mr John Zadnik | Alternate Director for Mr Rick Crabb | Appointed 19 November 2004 | 4 yrs, 10 mths |
| Mr Alex Parks | Chief Executive Officer | Appointed 01 December 2006 (i) | 2 yrs, 9 mths |
| Mr Craig Martin | Chief Operating Officer | Appointed 01 February 2007 | 2 yrs, 7 mths |
| Ms Ida Holt | Chief Financial Officer | Appointed 01 January 2009 (i) | 8 mths |
| Mr Richard King | Commercial Manager | Appointed 28 July 2008 | 1 yr, 2 mths |
| Mr Stefan Kleffmann | Geoscience Manager | Appointed 01 April 2008 | 1 yr, 6 mths |
| Ms Emma McCormack | Company Secretary | Appointed 09 March 2007 | 2 yrs, 6 mths |

(i) Details of resignation dates can be found in section B of the remuneration report on page 38.

# DIRECTORS' REPORT (Cont'd)

## Remuneration Report

The remuneration report is set out under the following main headings:

A Principles used to determine the nature and amount of remuneration

B Details of remuneration

C Service agreements

D Share-based compensation

E Additional information

The information provided in this remuneration report has been audited as required under Section 308 (3) (c) of the Corporations Act 2001.

### A Principles used to determine the nature and amount of remuneration

The remuneration policy of Otto Energy Limited has been designed to align Director and Executives objectives with shareholder and business objectives. The Board of Otto Energy Limited believes the remuneration policy to be appropriate and effective in its ability to attract and retain the best Executives and Directors to run and manage the consolidated entity, as well as create goal congruence between Directors, Executives and shareholders.

The Board's policy for determining the nature and amount of remuneration for Board members and senior Executives of the Company is as follows:

Non executive Directors, executive Directors and senior executives receive a base salary (which is based on factors such as length of service and experience), which is calculated on a total cost basis and includes any FBT charges related to employee benefits including motor vehicles, as well as employer contributions to superannuation funds.

Executive Directors can be employed by the Company on a consultancy basis in conjunction with Board approval, with remuneration and terms stipulated in individual consultancy agreements.

The Board reviews Executive packages annually by reference to the Company's performance, Executive performance and comparable information from industry sectors and other listed companies in similar industries. In addition, external consultants may be used to provide analysis and advice to ensure the Directors and senior Executive's remuneration is competitive in the market place.

Directors and senior Executives receive a superannuation guarantee contribution required under the Australian superannuation guarantee legislation which is currently 9%. However, some individuals may choose to sacrifice a portion of their salary to increase payments towards superannuation.

All remuneration paid to Directors and Executives is valued at the cost to the Company and expensed. Shares issued to Directors and Executives as part of their remuneration are valued as the difference between the market price of the issued shares and the amount paid by the Director or Executive. Options over ordinary shares are valued using the Black-Scholes methodology.

The Board policy is to remunerate Non-executive Directors at market rates for comparable companies based upon time, commitment and responsibilities. Non executive remuneration is reviewed annually, based on market practice, duties and accountability. Independent external advice is sought when required. The maximum aggregate amount of fees that can be paid to non executive Directors is subject to approval by shareholders at the Annual General Meeting.

Fees for Non-executive Directors are not linked to the performance of the consolidated entity. Non-executive Directors do not receive any retirement benefits other than superannuation. The Non-executive Directors are not required to hold any shares in the Company under the Constitution of the Company; however, to align Directors' interests with shareholder interests, the Directors are encouraged to hold shares in the Company.

The Board believes that it has implemented suitable practices and procedures that are appropriate for an organisation of this size and maturity.

#### Base Salary

Base salary may include a combination of cash and prescribed non-financial benefits at the Executive's discretion.

Executives are offered a competitive base pay that comprises the fixed component of pay and rewards. Base pay for executives is reviewed annually to ensure the Executives' pay is competitive with the market. An Executive's pay is also reviewed on promotion. There are no guaranteed base pay increases included in any Executives' contracts.

#### Bonuses

Bonuses to Directors and Executives are paid based upon unspecified performance criteria as determined by the Board from time to time.

#### Remuneration Committee

During the year ended 30 June 2009, the consolidated entity did not have a separately established nomination or remuneration committee. Considering the current size of the consolidated entity and the number of Directors, the Board are of the view that these functions can be efficiently performed with full Board participation.

#### Remuneration Structure

In accordance with best practice corporate governance, the structure of non executive Director and senior manager remuneration is separate and distinct.

#### Directors' Remuneration

The Non-executive Directors are entitled to receive directors' fees of amounts determined by the shareholders of the Company at the Annual General Meeting. The Non-executive Directors of the Company are entitled to receive directors' fees in such amounts (as determined by the Directors) in aggregate not to exceed $500,000 (approved at January 2008 EGM), to be divided among non executive Directors as the Directors may agree and in the absence of agreement then equally, until otherwise determined by shareholders at the Annual General Meeting.

The Directors have resolved that Non-executive Directors' fees based in Australia are $50,000 per annum (inclusive of superannuation) for each Non-executive Director and $75,000 per annum (inclusive of superannuation) for the Non-executive Chairman. Non executive Directors may also be remunerated for additional specialised services performed at the request of the Board and reimbursed for reasonable expense incurred by Directors on Company business.

#### Executive Director and Key Management Personnel Remuneration

The Company aims to reward Executives with a level and mix of remuneration commensurate with their position and responsibilities within the Company and so as to:

- Reward Executives for Company performance;
- Align the interest of Executives with those of shareholders; and
- Ensure total remuneration is competitive by market standards.

# DIRECTORS' REPORT (Cont'd)

## Remuneration Report (Cont'd)

### Company Performance, Shareholder Wealth, Directors and Executives Remuneration

There is no direct link between Company performance, shareholder wealth and remuneration.

The table below shows the total revenue, losses and earnings per share for the previous 5 years:

| | 2005 $ | 2006 $ | 2007 $ | 2008 $ | 2009 $ |
|---|---|---|---|---|---|
| Revenue and other income | 174,024 | 171,567 | 107,432 | 4,193,006 | 2,600,078 |
| Net Loss | (430,197) | (1,501,857) | (2,797,839) | (10,699,873) | (57,348,777) |
| Earnings/(loss) per share (cents) | (1.71) | (2.92) | (2.19) | (3.12) | (10.06) |

### B Details of remuneration

**Amounts of remuneration**

Details of the remuneration of the Directors, the key management personnel of the Group (as defined in AASB 124 *Related Party Disclosures*) and specified Executives of Otto Energy Limited and its controlled entities are set out in the following tables.

The key management personnel of the Group are the directors of Otto Energy Limited (see page 35 above).

In addition, the following persons must be disclosed under the Corporations Act 2001 as they are key management personnel:

| | | |
|---|---|---|
| Mr Alex Parks | Chief Executive Officer | Appointed 01 December 2006 |
| Mr Craig Martin | Chief Operating Officer | Appointed 01 February 2007 |
| Ms Ida Holt | Chief Financial Officer | Appointed 01 January 2009 |
| Mr Richard King | Commercial Manager | Appointed 28 July 2008 |
| Mr Stefan Kleffmann | Geoscience Manager | Appointed 01 April 2008 |

**Changes during and since year end**

Mr Paul Moore was appointed to the position of Chief Executive Officer on the 1 July 2009. Mr Alex Parks resigned from the position of Chief Executive officer effective from 30 June 2009. Ms Ida Holt resigned from the position of Chief Financial Officer effective from 28 August 2009.

| 30 June 2009 Group and Company | Short-term Employee Benefits | | | Post Employ-ment | Long-Term Benefits | | Share-Based Payments | Total | % Perfor-mance Related |
|---|---|---|---|---|---|---|---|---|---|
| | Salary & Fees | Cash Bonus | Non Monetary | Super-annuation Pensions | Long Service Leave | Termination benefits | Options | | |
| Directors | $ | $ | $ | $ | $ | | $ | $ | % |
| Mr R Crabb | 45,872 | 75,000 | 5,250 | 4,128 | - | - | 107,490 | 237,740 | 32% |
| Dr J Poll | 150,000 | - | 5,250 | - | - | - | 93,882 | 249,132 | - |
| Mr I Macliver | 43,248 | - | 5,250 | 3,892 | - | - | 143,320 | 195,710 | - |
| Mr J Zadnik | 22,936 | - | 5,250 | 2,064 | - | - | 35,830 | 66,080 | - |
| Mr R Bomasang | 82,496 | - | 5,250 | - | - | - | 16,180 | 103,926 | - |
| Mr J Jetter | 62,560 | - | 5,250 | - | - | - | - | 67,810 | - |
| | 407,112 | 75,000 | 31,500 | 10,084 | - | - | 396,702 | 920,398 | 32% |
| Other Key Management Personnel | | | | | | | | | |
| Mr A Parks | 331,255 | - | - | 29,813 | - | 308,860 | 252,707 | 922,635 | - |
| Mr C Martin | 247,706 | - | - | 22,294 | - | - | 103,679 | 373,679 | - |
| Ms I Holt | 125,000 | - | - | 11,250 | - | - | - | 136,250 | - |
| Mr Richard King | 230,875 | - | - | 20,778 | - | - | 320,833 | 572,486 | - |
| Mr Stefan Kleffmann | 230,941 | - | - | 20,784 | - | - | 285,071 | 536,796 | - |
| | 1,165,777 | - | - | 104,919 | - | 308,860 | 962,290 | 2,541,846 | - |

The above amounts representing options granted as part of remuneration are calculated in accordance with AASB 2 Share Based Payments. AASB 2 requires that the expense associated with a share based payment is calculated at issue date and then subsequently amortised over the option vesting period. Once the share based payment has been calculated it is not able to be adjusted. As such the option expense noted above is based upon historical calculations made during a time when the share price of the company was significantly higher than its current level. Due to the impact of the global financial crisis it is management's belief that the true intrinsic value of the options issued to Directors and Other Key Management Personnel is significantly lower than the number presented above.

| 30 June 2008 Group and Company | Short-term Employee Benefits | | | Post Employment | Long-Term Benefits | Share-Based Payments | Total | % Perfor-mance Related |
|---|---|---|---|---|---|---|---|---|
| 30 June 2008 | Salary & Fees | Cash Bonus | Non Monetary | Super-annuation Pensions | Long Service Leave | Options | | |
| Directors | $ | $ | $ | $ | $ | $ | $ | % |
| Mr R Crabb | 45,500 | - | 5,250 | 4,095 | - | 76,779 | 131,624 | - |
| Dr J Poll | 150,000 | 50,000 | 5,250 | - | - | 225,656 | 430,906 | - |
| Mr I Macliver | 45,500 | - | 5,250 | 4,095 | - | 102,371 | 157,216 | - |
| Mr J Zadnik | 22,750 | - | 5,250 | 2,048 | - | 25,595 | 55,643 | - |
| Mr R Bomasang | 53,571 | - | 5,250 | - | - | 60,959 | 119,780 | - |
| Mr J Jetter | 27,083 | - | 5,250 | - | - | 737,074 | 769,407 | - |
| | 344,404 | 50,000 | 31,500 | 10,238 | - | 1,228,434 | 1,664,576 | - |
| Other Key Management Personnel | | | | | | | | |
| Mr A Parks | 282,314 | 100,000 | - | 25,408 | - | 468,711 | 876,433 | - |
| Mr C Martin | 222,577 | 100,000 | - | 28,289 | - | 183,464 | 534,330 | - |
| Mr B Elsholz | 135,520 | 27,500 | - | 12,196 | - | 101,792 | 277,008 | - |
| | 640,411 | 227,500 | - | 65,893 | - | 753,967 | 1,687,771 | - |
| Executives | | | | | | | | |
| Ms E McCormack | - | - | - | - | - | 40,833 | 40,833 | - |
| | - | - | - | - | - | 40,833 | 40,833 | - |

# DIRECTORS' REPORT (Cont'd)

## Remuneration Report (Cont'd)

The relative proportions of remuneration that are linked to performance and those that are fixed are as follows:

| Name | Fixed Remuneration | | At Risk – Short Term Incentive | | At Risk – Long Term Incentive | |
|---|---|---|---|---|---|---|
| | 2009 | 2008 | 2009 | 2008 | 2009 | 2008 |
| **Directors** | | | | | | |
| Mr R Crabb | 55% | 42% | - | - | 45% | 58% |
| Dr J Poll | 62% | 36% | - | - | 38% | 52% |
| Mr I Macliver | 27% | 35% | - | - | 73% | 65% |
| Mr J Zadnik | 46% | 54% | - | - | 54% | 46% |
| Mr R Bomasang | 84% | 49% | - | - | 16% | 51% |
| Mr J Jetter | 100% | 3% | - | - | - | 97% |
| **Other Key Management Personnel** | | | | | | |
| Mr A Parks | 73% | 35% | - | - | 27% | 53% |
| Mr C Martin | 74% | 47% | - | - | 26% | 34% |
| Ms I Holt | 100% | - | - | - | - | - |
| Mr R King | 44% | - | - | - | 56% | 44% |
| Mr S Kleffmann | 48% | - | - | - | 52% | - |

### C Service agreements

On appointment to the Board, all Non-executive directors enter into a service agreement with the company in the form of a letter of appointment. The letter summarises the Board polices and terms, including compensation, relevant to the office of Director.

Remuneration and other terms of employment for the Chief Executive Officer and other key management personnel are formalised in service agreements. Each of these agreements provide for the provision of performance-related conditions and other major provisions of the agreements relating to remuneration are set out below.

Remuneration and other terms of employment for Dr Jaap Poll (Non Executive Director) are formalised in a consultancy agreement. The major provisions of the agreement relating to remuneration are set out below.

Dr Jaap Poll, Non Executive Director - Consultancy Agreement with Dormley Pty Ltd

- Term of Agreement – The Agreement commenced on 1 October 2004 and continues until either party gives 3 months written notice of termination or is otherwise terminated in accordance with the Consultancy Agreement.
- Remuneration $150,000 per annum plus GST payable monthly.
- Payment of termination of the Agreement without cause – 3 months fee plus GST, subject to the requirements of ASX Listing Rule 10.19.

Remuneration and other terms of employment for Executives of the Company are formalised in an employment agreement. Major provisions of the Executives' agreements relating to remuneration are set out below.

#### Mr Alex Parks, Chief Executive Officer – Employment Agreement

- Term of Agreement – The Agreement commenced on 01 December 2006 and continues until either party gives 3 months written notice of termination or is otherwise terminated in accordance with the Employment Agreement.
- Remuneration $345,000 per annum inclusive of superannuation payable monthly.
- Payment of termination of Agreement without cause – 9 months remuneration.

#### Mr Craig Martin, Chief Operating Officer – Employment Agreement

- Term of Agreement – The Agreement commenced on 01 February 2007 and continues until the Company gives 3 months written notice of termination (2 months notice by the Executive) or is otherwise terminated in accordance with the Employment Agreement.
- Remuneration $270,000 per annum inclusive of superannuation payable monthly.
- Payment of termination of Agreement without cause – 4 months remuneration.

#### Ms Ida Holt, Chief Financial Officer – Employment Agreement

- Term of Agreement – The Agreement commenced on 01 January 2009 and continues until the Company gives 2 months written notice of termination (2 months notice by the Executive) or is otherwise terminated in accordance with the Employment Agreement.
- Remuneration $272,500 per annum inclusive of superannuation payable monthly.
- Payment of termination of Agreement without cause – 2 months remuneration.

#### Mr Richard King, Commercial Manager – Employment Agreement

- Term of Agreement – The Agreement commenced on 28 July 2008 and continues until the employee gives 2 months written notice of termination (6 months notice by the Executive) or is otherwise terminated in accordance with the Employment Agreement.
- Remuneration $270,000 per annum inclusive of superannuation payable monthly.

#### Mr Stefan Kleffmann, Geoscience Manager – Employment Agreement

- Term of Agreement – The Agreement commenced on 01 January 2009 and continues until the Company gives 2 months written notice of termination (2 months notice by the Executive) or is otherwise terminated in accordance with the Employment Agreement.
- Remuneration $250,000 per annum inclusive of superannuation payable monthly.

# DIRECTORS' REPORT (Cont'd)

## Remuneration Report (Cont'd)

### D Share-based compensation

**Options**

Options are issued to Directors and Executives as part of their remuneration. The options are issued to the majority of Directors and Executives of Otto Energy Limited and its subsidiaries to increase goal congruence between Executives, Directors and shareholders.

The terms and conditions of each grant of options affecting remuneration in the previous, current or future reporting periods are as follows:

| Grant Date | Date vested and exercisable | Expiry Date | Exercise Price | Value per option at grant date |
|---|---|---|---|---|
| 27 September 2005 | 27 September 2005 | 01 December 2007 | $0.25 | $0.14 |
| 27 September 2005 | 20 October 2007 | 01 December 2007 | $0.30 | $0.13 |
| 08 May 2007 | 08 May 2008 | 29 May 2011 | $0.20 | $0.11 |
| 08 May 2007 | 08 November 2008 | 29 May 2011 | $0.30 | $0.08 |
| 08 May 2007 | 08 May 2009 | 29 May 2011 | $0.40 | $0.06 |
| 17 December 2007 | 17 December 2008 | 17 December 2010 | $0.30 | $0.14 |
| 29 January 2008 | 29 January 2009 | 29 January 2011 | $0.30 | $0.12 |
| 01 August 2008 | 01 August 2009 | 01 August 2012 | $0.60 | $0.14 |

Options granted under the plan carry no dividend or voting rights.

Details of options over ordinary shares in the Company provided as remuneration to each Director of Otto Energy Limited and each of the key management personnel of the parent entity and the Group are set out below. When exercisable each option is convertible into one ordinary share of Otto Energy Limited. Further information on the options is set out in note 29 to the financial statements.

| | Number of options granted during the year | | Number of options vested during the year | |
|---|---|---|---|---|
| **Directors** | **2009** | **2008** | **2009(i)** | **2008** |
| Mr R Crabb | - | 1,500,000 | 1,500,000 | - |
| Dr J Poll | - | 1,000,000 | 2,000,000 | 1,000,000 |
| Mr I Macliver | - | 2,000,000 | 2,000,000 | - |
| Mr J Zadnik | - | 500,000 | 500,000 | - |
| Mr R Bomasang | - | - | 666,666 | 333,334 |
| Mr J Jetter | - | 6,000,000 | - | 6,000,000 |
| **Other Key Management Personnel** | | | | |
| Mr A Parks | - | 3,500,000 | 4,500,000 | 1,000,000 |
| Mr C Martin | - | 1,500,000 | 1,833,300 | 333,400 |
| Ms I Holt | - | - | - | - |
| Mr R King | 2,500,000 | - | - | - |
| Mr S Kleffmann | - | 1,500,000 | - | 1,500,000 |

(i)The options expense recorded for the 2009 financial year is equal to the amortisation of the total calculated options expense from grant date to vesting date and does not necessarily reflect the value of options granted during the year.

The assessed fair value at grant date of options granted to the individuals is allocated equally over the period from grant date to vesting date, and the amount is included in the remuneration tables above. Fair values at grant date are independently determined using a Black-Scholes option pricing model that takes into account the exercise price, the term of the option, the share price at grant date and expected price volatility of the underlying share, the expected dividend yield and the risk-free interest rate for the term of the option.

The model inputs for options granted during the year ended 30 June 2009 included:

Options are granted for no consideration and vest 1 year from issue date and are subject to a vesting price condition until expiry date.

| Grant date | 01 August 2008 |
|---|---|
| Exercise price | $0.60 |
| Expiry date | 01 August 2012 |
| Share price at grant date | $0.34 |
| Expected volatility | 65% |
| Expected dividend yield | Nil |
| Risk free rate | 6.06% |

**Shares provided on exercise of remuneration of options**

Details of ordinary shares in the Company provided as a result of the exercise of remuneration options to each director of Otto Energy Limited and other key management personnel of the group are set out below:

| | Date of exercise of options | Amount paid per share | Number of ordinary shares issued on exercise of options during the year | |
|---|---|---|---|---|
| **Directors** | | **$** | **2009** | **2008** |
| Mr R Crabb | - | - | - | - |
| Dr J Poll | - | - | - | 1,000,000 |
| Mr I Macliver | - | - | - | - |
| Mr J Zadnik | - | - | - | - |
| Mr R Bomasang | - | - | - | - |
| Mr J Jetter | - | - | - | - |
| **Other Key Management Personnel** | | | | |
| Mr A Parks | - | - | - | - |
| Mr C Martin | - | - | - | - |
| Ms I Holt | - | - | - | - |
| Mr R King | - | - | - | - |
| Mr S Kleffmann | - | - | - | - |

# DIRECTORS' REPORT (Cont'd)

## Remuneration Report (Cont'd)

### E Additional information

**Details of remuneration: cash bonuses and options**

Options are issued to Directors and executives as part of their remuneration. The options are used to attract and retain suitably experienced Directors and are incentives to increase long term shareholder wealth. These are issued to the majority of Directors and executives of Otto Energy Limited to increase goal congruence between executives, Directors and shareholders. The options are subject to vesting conditions and will not vest (and become exercisable) if the vesting conditions are not satisfied, hence the minimum value of the option yet to vest is nil. The maximum value of the options yet to vest has been determined as the amount of the grant date fair value of the options that is yet to be expensed.

| | Options | | | | | | Cash Bonus | |
|---|---|---|---|---|---|---|---|---|
| | Year Granted | Vested | Forfeited | Financial year in which options may vest | Minimum total value of grant yet to vest | Maximum total value of grant yet to vest | Paid | Forfeited |
| Directors | | % | % | | $ | $ | % | % |
| Mr R Crabb | 2008 | 100 | - | 2009 | nil | nil | 100% | - |
| Dr J Poll | 2005 | - | 100 | 2005 | nil | nil | - | - |
| | | 100 | - | 2007 | nil | nil | - | - |
| | 2007 | 100 | - | 2008 | nil | nil | - | - |
| | | 100 | - | 2009 | nil | nil | - | - |
| | 2008 | 100 | - | 2009 | nil | nil | - | - |
| Mr I Macliver | 2008 | 100 | - | 2009 | nil | nil | - | - |
| Mr J Zadnik | 2008 | 100 | - | 2009 | nil | nil | - | - |
| Mr R Bomasang | 2007 | 100 | - | 2008 | nil | nil | - | - |
| | | 100 | - | 2009 | nil | nil | - | - |
| Mr J Jetter | 2008 | 100 | - | 2008 | nil | nil | - | - |
| Other Key Management Personnel | | | | | | | | |
| Mr A Parks | 2007 | 100 | - | 2008 | nil | nil | - | - |
| | | 50 | 50(i) | 2009 | nil | nil | - | - |
| | 2008 | 100 | - | 2009 | nil | nil | - | - |
| Mr C Martin | 2007 | 100 | - | 2008 | nil | nil | - | - |
| | | 100 | - | 2009 | nil | nil | - | - |
| | 2008 | 100 | - | 2009 | nil | nil | - | - |
| Mr B Elsholz | 2007 | 100 | - | 2008 | nil | nil | - | - |
| | | 100 | - | 2009 | nil | nil | - | - |
| | 2008 | 100 | - | 2009 | nil | nil | - | - |
| Mr R King | 2008 | - | - | 2009 | nil | 29,167 | - | - |
| Mr S Kleffmann | 2008 | 100 | - | 2008 | nil | nil | - | - |

(i) Forfeited options

Options were forfeited upon the cessation of Alex Park's employment with the company on 30 June 2009.

| | Options Granted as part of Remuneration | Total Remuneration Represented by Options | Exercise price per option | Options Exercised | Options Lapsed |
|---|---|---|---|---|---|
| Directors | $ | % | $ | $ | $ |
| Mr R Crabb | 107,490 | 45% | - | - | - |
| Dr J Poll | 93,882 | 38% | - | - | - |
| Mr I Macliver | 143,320 | 73% | - | - | - |
| Mr J Zadnik | 35,830 | 54% | - | - | - |
| Mr R Bomasang | 16,180 | 16% | - | - | - |
| Mr J Jetter | - | - | - | - | - |
| | 396,702 | - | - | - | - |
| Other Key Management Personnel | $ | % | $ | $ | $ |
| Mr A Parks | 252,707 | 27% | - | - | - |
| Mr C Martin | 103,679 | 28% | - | - | - |
| Ms I Holt | - | - | - | - | - |
| Mr R King | 320,833 | 56% | - | - | - |
| Mr S Kleffmann | 285,071 | 52% | - | - | - |
| | 962,290 | - | - | - | - |

End of the audited remuneration report

## Meetings of Directors

During the financial year, 16 meetings of Directors and 2 meetings of the Audit and Compliance Committee were held. Attendances by each Director during the year were as follows:

| | Board Meetings | | Audit & Compliance Committee | |
|---|---|---|---|---|
| Director | Number eligible to attend | Number attended | Number eligible to attend | Number attended |
| Mr R Crabb | 16 | 15 | 2 | 2 |
| Dr J Poll | 16 | 14 | - | - |
| Mr I Macliver | 16 | 15 | 2 | 2 |
| Mr J Jetter | 16 | 15 | - | - |
| Mr R Bomasang | 16 | 16 | - | - |
| Mr J Zadnik (Alternate) | 16 | 13 | - | - |

# DIRECTORS' REPORT (Cont'd)

## Indemnifying Officers or Auditor

During the financial year the Company paid premiums to insure the Directors against certain liabilities arising out of their conduct while acting as an officer of the Company. The Company paid premiums to insure each of the Directors against liabilities for costs and expenses incurred by them in defending any legal proceedings arising out of their conduct while acting in the capacity as Director of the Company, other than conduct involving a wilful breach of duty in relation to the Company. Under the terms and conditions of the insurance contract the amount of the premium paid cannot be disclosed.

## Options

At the date of this report details of the unissued ordinary shares of Otto Energy Limited under option, are as follows:

| Date of Expiry | Exercise Price | Number Under Option |
|---|---|---|
| 30/11/2009 | $0.34 | 8,000,000 |
| 03/07/2010 | $0.05 | 61,855,350 |
| 15/12/2010 | $0.60 | 2,000,000 |
| 17/12/2010 | $0.30 | 8,250,000 |
| 25/01/2011 | $0.30 | 11,000,000 |
| 29/05/2011 | $0.20 | 4,083,400 |
| 29/05/2011 | $0.30 | 4,333,300 |
| 29/05/2011 | $0.40 | 2,333,300 |
| 10/04/2012 | $0.35 | 2,000,000 |
| 01/08/2012 | $0.60 | 2,500,000 |
| 08/09/2012 | $0.12 | 6,000,000 |
| 30/06/2014 | $0.12 | 7,500,000 |
| | | 119,855,350 |

## Shares issued on the exercise of options

The following ordinary shares of Otto Energy Limited were issued during the year ended 30 June 2009 on the exercise of options granted under the employee share option plan. No amounts were unpaid on any of the shares.

| Date options granted | Issue price of shares | Number of shares issued. |
|---|---|---|
| 29/05/2007 | $0.20 | 250,000 |

## Environmental Regulation and Performance

So far as the Directors are aware, there have been no breaches of environmental conditions of the Company's exploration licences. Procedures are adopted for each exploration programme to ensure that environmental conditions of the Company's tenements are met.

### Carbon Emissions

The National Greenhouse and Energy Reporting Act 2007 (NGER) is currently subject to finalisation by the Australian Parliament with implementation due in 2010/2011. The legislation sets forth the requirements of Otto Energy under the Carbon Pollution Reduction Scheme (CPRS). As the legislation is not yet finalised, the Directors are unable to reliably quantify the potential future impact of both direct and indirect costs related to this scheme. As such any costs associated with the CPRS have not been taken into account when preparing budgets, forecasts and/or valuation models for measurement of recognised amounts.

## Proceedings on Behalf of Company

No person has applied for Leave of Court to bring proceedings on behalf of the Company or 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 any part of those proceedings.

The Company was not a party to any such proceedings during the year.

## Corporate Governance

In recognising the need for the highest standards of corporate behaviour and accountability, the Directors of Otto Energy Limited support and have adhered to the principles of Corporate Governance. The Company's corporate governance statement is contained in the Corporate Governance section of the Financial Report.

## Non-Audit Services

The Board of Directors, in accordance with advice from the Audit and Compliance Committee, is satisfied that the provision of non-audit services during the year is compatible with the general standard of independence for auditors imposed by the Corporations Act 2001 (Cth). The Directors are satisfied that the services disclosed below did not compromise the external auditor's independence for the following reasons:

- all non-audit services are reviewed and approved by the Audit and Compliance Committee prior to commencement to ensure they do not adversely affect the integrity and objectivity of the auditor; and
- the nature of the services provided do not compromise the general principles relating to auditor independence as set out in the Institute of Chartered Accountants in Australia and APES 110 Code of Ethics for Professional Accountants.

The total fees for non-audit services paid to the external auditors related entity BDO Kendalls Corporate Tax (WA) Pty Ltd for taxation services is $10,360 for the year ended 30 June 2009 (2008:$10,050).

## Auditors Independence Declaration

The auditor's independence declaration as required under Section S307C of the Corporations Act 2001 (Cth) for the year ended 30 June 2009 has been received and can be found on page 48 of the Directors' report.

Signed in accordance with a resolution of the Board of Directors.

**Mr I Macliver**

**Director**

**23 September 2009**

# AUDITORS' INDEPENDENCE DECLARATION

BDO Kendalls

BDO Kendalls Audit & Assurance (WA) Pty Ltd
128 Hay Street
SUBIACO WA 6008
PO Box 700
WEST PERTH WA 6872
Phone 61 8 9380 8400
Fax 61 8 9380 8499
aa.perth@bdo.com.au
www.bdo.com.au

ABN 79 112 284 787

23 September 2009

The Directors
Otto Energy Limited
32 Delhi Street
WEST PERTH WA 6005

Dear Sirs,

**DECLARATION OF INDEPENDENCE BY BRAD MCVEIGH TO THE DIRECTORS OF OTTO ENERGY LIMITED**

As lead auditor of Otto Energy Limited for the year ended 30 June 2009, I declare that, to the best of my knowledge and belief, there have been no contraventions of:

- the auditor independence requirements of the Corporations Act 2001 in relation to the audit; and
- any applicable code of professional conduct in relation to the audit.

This declaration is in respect of Otto Energy Limited and the entities it controlled during the period.

**Brad McVeigh**
Director

BDO Kendalls

**BDO Kendalls Audit & Assurance (WA) Pty Ltd**
Perth, Western Australia



# INCOME STATEMENTS

## Income Statements
## For the Year Ended 30 June 2009

| | Note | Economic Entity | | Parent Entity | |
|---|---|---|---|---|---|
| | | 2009 $ | 2008 $ | 2009 $ | 2008 $ |
| **Revenue from continuing operations** | 5 | 1,871,849 | 854,632 | 56,068 | 136,333 |
| Other income | 6 | 728,229 | 3,338,374 | 728,229 | - |
| Employee benefits expense | | (3,558,608) | (2,163,304) | (3,083,858) | (1,835,118) |
| Share based payment expense | 7 | (1,724,501) | (2,553,245) | (1,724,501) | (2,268,575) |
| Finance costs | 7 | (658,058) | (1,834) | (655,933) | (213) |
| Depreciation expense | 7 | (175,392) | (72,535) | (115,722) | (59,539) |
| Impairment expense | 7 | (49,431,593) | - | (59,128,084) | - |
| Other expenses | 7 | (3,716,774) | (2,250,073) | (2,645,271) | (2,169,762) |
| Capitalised costs written off | | (192,839) | (26,861) | (64,091) | - |
| Unrealised foreign exchange gain/(loss) | | (481,389) | (6,399,184) | 13,313,669 | (6,399,184) |
| Write back of prior year provision | | - | - | - | 441,722 |
| Share of net profits/(losses) of associates | 25 | - | (843,611) | - | - |
| **Loss before income tax** | | (57,339,076) | (10,117,641) | (53,319,494) | (12,154,336) |
| Income tax expense from continuing operations | 8 | (9,701) | (582,232) | - | - |
| **Loss attributable to equity holders of Otto Energy Limited** | | (57,348,777) | (10,699,873) | (53,319,494) | (12,154,336) |

| **Earnings Per Share** | | Cents | Cents |
|---|---|---|---|
| Basic loss per share | 28 | (10.06) | (3.12) |
| Diluted loss per share | 28 | n/a | n/a |

The above income statements should be read in conjunction with the accompanying notes.

# BALANCE SHEETS

## Balance Sheets
## As At 30 June 2009

| | Note | Economic Entity | | Parent Entity | |
|---|---|---|---|---|---|
| | | 2009 $ | 2008 $ | 2009 $ | 2008 $ |
| **ASSETS** | | | | | |
| **CURRENT ASSETS** | | | | | |
| Cash and cash equivalents | 9 | 13,061,710 | 5,033,862 | 11,912,122 | 2,915,725 |
| Trade and other receivables | 10 | 707,061 | 19,198,014 | 446,206 | 9,102,869 |
| Other current assets | 13 | 55,788 | 102,315 | 15,867 | 66,951 |
| **TOTAL CURRENT ASSETS** | | 13,824,559 | 24,334,191 | 12,374,195 | 12,085,545 |
| **NON-CURRENT ASSETS** | | | | | |
| Trade and other receivables | 10 | 39,737,289 | 15,820,825 | 80,055,766 | 82,004,187 |
| Financial assets | 11(a) | - | - | 1,500,250 | 8,586,721 |
| Intangible assets | 11(b) | 7,542,044 | 35,425,041 | - | - |
| Property, plant and equipment | 12 | 378,962 | 345,849 | 179,105 | 196,842 |
| Other non-current assets | 13 | 44,798,882 | 31,821,586 | - | 4,049,932 |
| Investments in Associate | 25 | - | - | - | - |
| **TOTAL NON-CURRENT ASSETS** | | 92,457,177 | 83,413,301 | 81,735,121 | 94,837,682 |
| **TOTAL ASSETS** | | 106,281,736 | 107,747,492 | 94,109,316 | 106,923,227 |
| **CURRENT LIABILITIES** | | | | | |
| Trade and other payables | 14 | 6,382,760 | 1,054,616 | 5,467,114 | 637,346 |
| **TOTAL CURRENT LIABILITIES** | | 6,382,760 | 1,054,616 | 5,467,114 | 637,346 |
| **NON-CURRENT LIABILITIES** | | | | | |
| Trade and other payables | 14 | - | 24,265 | - | - |
| Provisions | 15 | 55,915 | 46,802 | - | - |
| **TOTAL NON-CURRENT LIABILITIES** | | 55,915 | 71,067 | - | - |
| **TOTAL LIABILITIES** | | 6,438,675 | 1,125,683 | 5,467,114 | 637,346 |
| **NET ASSETS** | | 99,843,060 | 106,621,809 | 88,642,202 | 106,285,881 |
| **EQUITY** | | | | | |
| Contributed equity | 16 | 151,932,731 | 118,064,437 | 151,932,731 | 118,064,437 |
| Reserves | 17 | 20,693,710 | 3,991,976 | 6,985,195 | 5,177,674 |
| Accumulated losses | 17 | (72,783,381) | (15,434,604) | (70,275,724) | (16,956,230) |
| **TOTAL EQUITY** | | 99,843,060 | 106,621,809 | 88,642,202 | 106,285,881 |

The above balance sheets should be read in conjunction with the accompanying notes.

# STATEMENTS OF CHANGES IN EQUITY

## Statements of Changes in Equity
## For the Year Ended 30 June 2009

| | Note | Economic Entity | | Parent Entity | |
|---|---|---|---|---|---|
| | | 2009 $ | 2008 $ | 2009 $ | 2008 $ |
| **Total equity at the beginning of the financial year** | | 106,621,809 | 23,790,954 | 106,285,881 | 23,790,954 |
| Translation of foreign currency on controlled entities | | 14,894,213 | (1,118,535) | - | - |
| **Net income and expenses recognised directly in equity** | | 14,894,213 | (1,118,535) | - | - |
| Loss for the year | | (57,348,777) | (10,699,873) | (53,319,494) | (12,154,336) |
| **Total recognised income and expense for the year** | | (42,454,564) | (11,818,408) | (53,319,494) | (12,154,336) |
| Transactions with equity holders in their capacity with equity holders | | | | | |
| - Contribution of equity, net of transaction costs | 16 | 33,868,294 | 90,672,018 | 33,868,294 | 90,672,018 |
| - Issue of options | 29c | 83,019 | 1,424,000 | 83,019 | 1,424,000 |
| - Share based payments | 29c | 1,724,502 | 2,553,245 | 1,724,502 | 2,553,245 |
| **Total equity at the end of the financial year** | | 99,843,060 | 106,621,809 | 88,642,202 | 106,285,881 |

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

# CASH FLOW STATEMENTS

## Cash Flow Statements
## For the Year Ended 30 June 2009

| | Note | Economic Entity 2009 $ | Economic Entity 2008 $ | Parent Entity 2009 $ | Parent Entity 2008 $ |
|---|---|---|---|---|---|
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | | | | |
| Payments for exploration and evaluation | | (12,839,394) | (13,219,662) | (53,501) | (4,045,623) |
| Payments to suppliers and employees | | (6,700,626) | (4,108,091) | (5,209,301) | (3,896,997) |
| Interest received | | 773,896 | 441,539 | 55,214 | 136,334 |
| Interest and other costs of finance paid | | (658,058) | (1,834) | (648,183) | (214) |
| Income Tax Expense | | (9,701) | (582,232) | - | - |
| Foreign exchange gain | | - | 12,357 | - | - |
| Other Income | | 2,042,231 | 1,848 | 588,367 | - |
| Net cash used in operating activities | 27(a) | (17,391,652) | (17,456,075) | (5,267,404) | (7,806,500) |
| **CASH FLOWS FROM INVESTING ACTIVITIES** | | | | | |
| Purchase of property, plant and equipment | | (174,129) | (320,198) | (97,984) | (211,177) |
| Proceeds on sale of licence interest | | - | 5,381,553 | - | - |
| Payment for purchase of subsidiary, net of cash acquired | 23 | - | - | (99) | - |
| Payment for acquisition of unlisted investments | 23 | - | (58,515,913) | - | - |
| Loan to associated company | | (12,503,267) | (10,030,740) | (896,761) | - |
| Payment for purchase of investment in associate | | (2,116,680) | - | (2,116,680) | - |
| Net cash used in investing activities | | (14,794,076) | (63,485,298) | (3,111,524) | (211,177) |
| **CASH FLOWS FROM FINANCING ACTIVITIES** | | | | | |
| Proceeds from issue of shares | | 40,395,504 | 84,900,051 | 40,395,504 | 84,900,051 |
| Payment of share issue costs | | (2,568,571) | (3,728,958) | (2,568,571) | (3,728,958) |
| Loans from related parties | | 1,530,000 | - | 1,530,000 | - |
| Repayment of loans from related parties | | (1,183,420) | | (1,183,420) | - |
| Proceeds from borrowings | | - | 36,398 | - | - |
| Repayment of borrowings | | (6,165) | (1,976) | - | - |
| Loan to employees | | (100,000) | | (100,000) | |
| Loans to subsidiaries | | - | - | (22,299,782) | (72,047,862) |
| Net cash provided by financing activities | | 38,067,348 | 81,205,515 | 15,773,731 | 9,123,231 |
| Net (decrease)/ increase in cash held | | 5,881,620 | 264,142 | 7,394,803 | 1,105,554 |
| Cash at beginning of financial year | | 5,033,862 | 5,191,230 | 2,915,725 | 1,810,171 |
| Effect of exchange rate changes on the balances of cash held in foreign currencies at the beginning and end of the financial year | | 2,146,228 | (421,510) | 1,601,595 | - |
| Cash at end of financial year | 9 | 13,061,710 | 5,033,862 | 11,912,123 | 2,915,725 |

The accompanying notes form part of these financial statements.

# NOTES TO THE FINANCIAL STATEMENTS

## Statement of Significant Accounting Policies

The financial report is a general purpose financial report that has been prepared in accordance with Australian Accounting Standards, Australian Accounting Interpretations, other authoritative pronouncements of the Australian Accounting Standards Board and the *Corporations Act 2001 (Cth).*

The financial report covers the consolidated entity of Otto Energy Limited and controlled entities, and Otto Energy Limited as an individual parent entity. Otto Energy Limited is a listed public company, incorporated and domiciled in Australia.

The following is a summary of the material accounting policies adopted by the consolidated entity in the preparation of the financial report. The accounting policies have been consistently applied, unless otherwise stated.

### Basis of Preparation

#### Going Concern
The ability of the consolidated entity to continue as a going concern, develop its exploration assets, commercialise its various projects, and continue its operations is dependent upon both continuing production from the Galoc Oil Field (Service Contract 14c) and the market price of oil remaining at current levels. Should production levels from the Galoc Oil Field be lower than forecast, or if the market price of oil reaches lower than expected levels, the group will be required to seek additional funding through debt, equity or other means to continue its activities.

#### Compliance with IFRS
Australian Accounting Standards include Australian equivalents to International Financial Reporting Standards ("AIFRS"). Compliance with AIFRS ensures that the consolidated financial report of Otto Energy Limited complies with IFRS.

#### Historical cost convention
The financial report has been prepared on an accruals basis and is based on historical costs modified by the revaluation of selected non-current assets, and financial assets and financial liabilities for which the fair value basis of accounting has been applied.

#### Critical accounting estimates
The preparation of the financial statements in conformity with AIFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving higher degree of judgement or complexity, or areas where assumptions or estimates are significant to the financial statements are referenced in note 3.

#### Carbon Emissions
The National Greenhouse and Energy Reporting Act 2007 (NGER) is currently subject to finalisation by the Australian Parliament with implementation due in 2010/2011. The legislation sets forth the requirements of Otto Energy under the Carbon Pollution Reduction Scheme (CPRS). As the legislation is not yet finalised, the directors are unable to reliably quantify the potential future impact of both direct and indirect costs related to this scheme. As such any costs associated with the CPRS have not been taken into account when preparing budgets, forecasts and/or valuation models for measurement of recognised amounts.

# NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

## 1. Statement of Significant Accounting Policies (Cont'd)

### Accounting Policies

**a) Principles of Consolidation**

A controlled entity is any entity Otto Energy Limited has the power to control the financial and operating policies so as to obtain benefits from its activities. A list of controlled entities is contained in Note 24 to the financial statements. All controlled entities have a financial year-ending on 30 June.

All inter-company balances and transactions between entities in the consolidated entity, including any unrealised profits or losses, have been eliminated on consolidation. Accounting policies of subsidiaries have been modified where necessary to ensure consistency with those policies applied by the parent entity.

Where controlled entities have entered or left the consolidated entity during the year, their operating results have been included/excluded from the date control was obtained or until the date control ceased.

Minority interests in the equity and results of controlled entities are shown as a separate item in the consolidated financial report.

**b) Income Tax**

The charge for current income tax expense is based on the result for the year adjusted for any non-assessable or disallowed items. It is calculated using tax rates that have been enacted or are substantively enacted by the balance sheet date.

Deferred tax is accounted for using the balance sheet liability method in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. No deferred income tax will be recognised from the initial recognition of an asset or liability, excluding a business combination, where there is no effect on accounting or taxable profit or loss.

Deferred tax is calculated at the tax rates that are expected to apply to the period when the asset is realised or liability is settled. Deferred tax is credited in the income statement except where it relates to items that may be credited directly to equity, in which case the deferred tax is adjusted directly against equity.

Deferred income tax assets are recognised to the extent that it is probable that future tax profits will be available against which deductible temporary differences can be utilised.

The amount of benefits brought to account or which may be realised in the future is based on the assumption that no adverse change will occur in income taxation legislation and the anticipation that the consolidated entity will derive sufficient future assessable income to enable the benefit to be realised and comply with the conditions of deductibility imposed by the law.

**c) Plant and Equipment**

Each class of plant and equipment is carried at cost or fair value less, where applicable, any accumulated depreciation and impairment losses.

The carrying amount of plant and equipment is reviewed annually by Directors to ensure it is not in excess of the recoverable amount of these assets. The recoverable amount is assessed on the basis of the expected net cash flows which will be received from the assets' employment and subsequent disposal. The expected net cash flows have been discounted to their present values in determining recoverable amounts.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the group and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

Depreciation

The depreciable amount of all fixed assets including capitalised leased assets is depreciated on a straight-line basis over their useful lives to the consolidated entity commencing from the time the asset is held ready for use. Leasehold improvements are depreciated over the shorter of either the unexpired period of the lease or the estimated useful lives of the improvements.

The depreciation rates used for each class of depreciable asset are:

| Class of Fixed Asset | Depreciation Rate |
|---|---|
| Plant and equipment | 20% |
| Computer equipment | 40% |
| Computer software | 40% |

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposals are determined by comparing proceeds with the carrying amount at the time of disposal and are included in the income statement. When revalued assets are sold, amounts included in the revaluation reserve relating to that asset are transferred to retained earnings.

**d) Exploration and Development Expenditure**

Exploration, evaluation and development expenditure incurred is accumulated in respect of each identifiable area of interest. These 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 that 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.

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.

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.

Costs of site restoration are provided over the life of the facility from when exploration commences and are included in the costs of that stage. Site restoration costs include the dismantling and removal of mining plant, equipment and building structures, waste removal, and rehabilitation of the site in accordance with clauses of the mining permits. Such costs have been determined using estimates of future costs, current legal requirements and technology on an undiscounted basis.

Any changes in the estimates for the costs are accounted on a prospective basis. In determining the costs of site restoration, there is uncertainty regarding the nature and extent of the restoration due to community expectations and future legislation. Accordingly the costs have been determined on the basis that the restoration will be completed within one year of abandoning the site.

# NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

## 1. Statement of Significant Accounting Policies (Cont'd)

### e) Financial Instruments

Recognition
Financial instruments are initially measured at cost on trade date, which includes transaction costs, when the related contractual rights or obligations exist. Subsequent to initial recognition these instruments are measured as set out below.

Financial assets at fair value through profit and loss
A financial asset is classified in this category if acquired principally for the purpose of selling in the short term or if so designated by management and within the requirements of AASB 139: Recognition and Measurement of Financial Instruments. Derivatives are also categorised as held for trading unless they are designated as hedges. Realised and unrealised gains and losses arising from changes in the fair value of these assets are included in the income statement in the period which they arise.

Loans and receivables
Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and are stated at amortised cost using the effective interest rate method.

Available-for-sale financial assets
Available-for-sale financial assets include any financial assets not included in the above categories. Available-for-sale financial assets are reflected at fair value. Unrealised gains and losses arising from changes in fair value are taken directly to equity.

Fair value
Fair value is determined based on current bid prices for all quoted investments. Valuation techniques are applied to determine the fair value for all unlisted securities, including recent arm's length transactions, reference to similar instruments and option pricing models.

Impairment
At each reporting date, the Group assesses whether there is objective evidence that a financial instrument has been impaired. In the case of available-for-sale financial instruments, a prolonged decline in the value of the instrument is considered to determine whether impairment has arisen. Impairment losses are recognised in the income statement.

### f) Impairment of Assets

At each reporting date, the Group reviews the carrying values of its tangible and intangible assets to determine whether there is any indication that those assets have been impaired. If such an indication exists, the recoverable amount of the asset, being the higher of the asset's fair value less costs to sell and value in use, is compared to the assets carrying value. Any excess of the assets carrying value over its recoverable amount is expensed to the income statement.

Impairment testing is performed annually for goodwill and intangible assets with indefinite lives.

Where it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs.

### g) Foreign Currency Transactions and Balances

Functional and presentation currency
The functional currency of each of the Group's entities is measured using the currency of the primary economic environment in which that entity operates. The consolidated financial statements are presented in Australian dollars which is the parent entity's functional and presentation currency.

Transaction and balances
Foreign currency transactions are translated into functional currency using the exchange rates prevailing at the date of the transaction. Foreign currency monetary items are translated at the year-end exchange rate. Non-monetary items measured at historical cost continue to be carried at the exchange rate at the date of the transaction. Non-monetary items measured at fair value are reported at the exchange rate at the date when fair values were determined.

Exchange differences arising on the translation of monetary items are recognised in the income statement, except where deferred in equity as a qualifying cash flow or net investment hedge.

Exchange differences arising on the translation of non-monetary items are recognised directly in equity to the extent that the gain or loss is directly recognised in equity; otherwise the exchange difference is recognised in the income statement.

Group companies
The financial results and position of foreign operations whose functional currency is different from the Group's presentation currency are translated as follows:

- assets and liabilities are translated at year-end exchange rates prevailing at that reporting date;
- income and expenses are translated at average exchange rates for the period; and
- retained profits are translated at the exchange rates prevailing at the date of the transaction.

Exchange differences arising on translation of foreign operations are transferred directly to the Group's foreign currency translation reserve in the balance sheet. These differences are recognised in the income statement in the period in which the operation is disposed.

### h) Employee Benefits

(i) Wages and salaries and Annual leave
Provision is made for the Company's liability for employee benefits arising from services rendered by employees to balance date. Employee benefits that are expected to be settled within one year have been measured at the amounts expected to be paid when the liability is settled, plus related on-costs. Employee benefits payable later than one year have been measured at the present value of the estimated future cash outflows to be made for those benefits.

# NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

## 1. Statement of Significant Accounting Policies (Cont'd)

### h) Employee Benefits (Cont'd)

(ii) Share-based payments

Share-based payments compensation benefits are provided to employees via the employee share option plan. Information relating to this scheme is set out in note 29.

The fair value of options granted under the employee share option plan is recognised as an employee benefit expense with a corresponding increase in equity. The fair value is measured at grant date and recognised over the period during which employees become unconditionally entitled to the options.

The fair value at grant date is independently determined using a Black-Scholes option pricing model which takes into account the exercise price volatility of the underlying share, the expected dividend yield and the risk free interest rate for the term if the option.

The fair value of the options granted is adjusted to reflect market vesting conditions, but excludes the impact of any non-market vesting conditions. Non-market vesting conditions are included in assumptions about the number of options that's expected to become exercisable. The employee benefit expense recognised each period takes into account the most recent estimate. The impact on the revision to original estimates, if any, is recognised in the income statement with a corresponding adjustment to equity.

(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 or 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.

### i) Provisions

Provisions are recognised when the Group has a legal or constructive obligation, as a result of past events, for which it is probable that an outflow of economic benefits will result and that outflow can be reliably measured.

### j) Cash and Cash Equivalents

Cash and cash equivalents includes cash on hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less, and bank overdrafts. Bank overdrafts are shown within short-term borrowings in current liabilities on the balance sheet.

### k) Revenue

Revenue from the sale of goods is recognised when goods are delivered to a designated named place Freight on Board. Interest revenue is recognised on a proportional basis taking into account the interest rates applicable to the financial assets. Dividend revenue is recognised when the right to receive a dividend has been established. Dividends received from associates are accounted for in accordance with the equity method of accounting. All revenue is stated net of the amount of goods and services tax (GST).

### l) Business Combinations

The purchase method of accounting is used to account for all business combinations, including business combinations involving entities or businesses under common control, regardless of whether equity instruments or other assets are acquired. Cost is measured as the fair value of the assets given, equity instruments issued or liabilities incurred or assumed at the date of exchange plus costs directly attributable to the acquisition. Where equity instruments are issued in an acquisition, the fair value of the instruments is their published market price as at the date of exchange unless, in rare circumstances, it can be demonstrated that the published price at the date of exchange is an unreliable indicator of fair value and that other evidence and valuation methods provide a more reliable measure of fair value. Transaction costs arising on the issue of equity instruments are recognised directly in equity.

Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the Group's share of the fair value of the identifiable net assets of the subsidiary acquired, the difference is recognised directly in the income statement, but only after a reassessment of the identification and measurement of the net assets acquired.

Where settlement of any part of cash consideration is deferred, the amounts payable in the future are discounted to their present value as at the date of exchange. The discount rate used is the entity's incremental borrowing rate, being the rate at which a similar borrowing could be obtained from an independent financier under comparable terms and conditions.

Goodwill and intangible assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment, or more frequently if events or changes in circumstances indicate that they might be impaired. Other assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use.

For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows which are largely independent of the cash inflows from other assets or groups of assets (cash-generating units). Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

### m) Fair Value

The fair value of financial assets and financial liabilities must be estimated for recognition and measurement or for disclosure purposes. The fair value of financial instruments traded in active markets (such as publicly traded derivatives, and trading and available-for-sale securities) is based on quoted market prices at the balance sheet date. The quoted market price used for financial assets held by the Group is the current bid price.

The fair value of financial instruments that are not traded in an active market (for example, over-the-counter derivatives) is determined using valuation techniques. The Group uses a variety of methods and makes assumptions that are based on market conditions existing at each balance date. Quoted market prices or dealer quotes for similar instruments are used for long-term debt instruments held.

Other techniques, such as estimated discounted cash flows, are used to determine fair value for the remaining financial instruments. The fair value of interest rate swaps is calculated as the present value of the estimated future cash flows. The fair value of forward exchange contracts is determined using forward exchange market rates at the balance sheet date.

The carrying value less impairment provision of trade receivables and payables are assumed to approximate their fair values due to their short-term nature. 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.

# NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

## 1. Statement of Significant Accounting Policies (Cont'd)

**n) Goods and Services Tax (GST)**
Revenues, expenses and assets are recognised net of the amount of GST, except where the amount of GST incurred is not recoverable from the Australian Tax Office. In these circumstances the GST is recognised as part of the cost of acquisition of the asset or as part of an item of the expense. Receivables and payables in the balance sheet are shown inclusive of GST.

Cash flows are presented in the cash flow statement on a gross basis, except for the GST component of investing and financing activities, which are disclosed as operating cash flows.

**o) Comparative Figures**
When required by Accounting Standards, comparative figures have been adjusted to conform to changes in presentation for the current financial year.

**p) Segment Reporting**
A business segment is identified for a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different to those of other business segments. A geographical segment is identified when products or services are provided within a particular economic environment subject to risks and returns that are different from those of segments operating in other economic environments.

**q) Trade and Other Receivables**
Trade receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. Trade receivables are generally due for settlement within 30 days.

Collectability of trade receivables is reviewed on an ongoing basis. Debts which are known to be uncollectable are written off by reducing the carrying amount directly.

**r) 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 are unpaid. The amounts are unsecured and are usually paid within 30 days of recognition.

**s) Contributed Equity**
Ordinary shares are classified as equity. Mandatorily redeemable preference shares are classified as liabilities.

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds. Incremental costs directly attributable to the issue of new shares or options for the acquisition of a business are not included in the cost of the acquisition as part of the purchase consideration.

If the entity reacquires its own equity instruments, for example as a result of a share buy-back, those instruments are deducted from equity and the associated shares are cancelled. No gain or loss is recognised in the profit or loss and the consideration paid including any directly attributable incremental costs (net of income taxes) is recognised directly in equity.

**t) Equity settled share-based payment**
If the equity instruments granted vest immediately, the counterparty is not required to complete a specified period of service before becoming unconditionally entitled to those equity instruments. In the absence of evidence to the contrary, the entity shall presume that services rendered by the counterparty as consideration for the equity instruments have been received. In this case, on grant date the entity shall recognise the services received in full, with a corresponding increase in equity.

If the equity instruments granted do not vest until the counterparty completes a specified period of service, the entity shall presume that the services to be rendered by the counterparty as consideration for those equity instruments will be received in the future, during the vesting period. The entity shall account for those services as they are rendered by the counterparty during the vesting period, with a corresponding increase in equity.

For transactions measured by reference to the fair value of the equity instruments granted, an entity shall measure the fair value of equity instruments granted at the measurement date, based on market prices if available, taking into account the terms and conditions upon which those equity instruments were granted. If market prices are not available, the entity shall estimate the fair value of the equity instruments granted using a valuation technique to estimate what the price of those equity instruments would have been on the measurement date in an arm's length transaction between knowledgeable, willing parties.

## 2. Financial Risk Management

### Overview
The Company and Group have exposure to the following risks from their use of financial instruments:

a) credit risk;

b) liquidity risk;

c) market risk; and

d) currency risk

This note presents information about the Company's and Group's exposure to each of the above risks, their objectives, policies and processes for measuring and managing risk, and the management of capital.

The Board of Directors has overall responsibility for the establishment and oversight of the risk management framework. Management monitors and manages the financial risks relating to the operations of the Group through regular reviews of the risks to which the Group is subject to. The Group's financial instruments consist mainly of deposits with banks, accounts receivable and payable and loans to and from subsidiaries.

**a) Credit risk**
Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's receivables from customers and investment securities. For the Company it arises from receivables due from subsidiaries.

All cash balances held at banks are held at internationally recognised institutions. The majority of receivables are immaterial to the Group. Given this the credit quality of financial assets that are neither past due nor impaired can be assessed by reference to historical information of default rates. The credit quality of financial assets that are neither past due nor impaired can be assessed by reference to external credit ratings.

The maximum exposure to credit risk is the carrying amount of the financial assets of cash and trade and other receivables to the value of $52,410,685 (group) and $92,414,094 (parent).

# NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

## 2. Financial Risk Management (Cont'd)

### a) Credit risk (Cont'd)

Financial assets that are neither past due nor impaired are as follows:

| | Consolidated | | Parent | |
|---|---|---|---|---|
| | 2009 | 2008 | 2009 | 2008 |
| | $ | $ | $ | $ |
| **Trade and other receivables – counterparties without external credit rating** | | | | |
| Financial assets with no defaults in past | 606,207 | 19,198,064 | 345,352 | 9,102,869 |
| Financial assets with no history (new) | 100,854 | - | 100,854 | - |
| Financial assets with some defaults (intercompany receivables) | 39,737,289 | - | 80,055,766 | 82,004,187 |
| **Total trade and other receivables** | 40,444,350 | 19,198,064 | 80,501,972 | 91,107,056 |
| **Cash and cash equivalents** | | | | |
| AA S&P credit rating | 13,061,701 | 5,033,862 | 11,912,122 | 2,915,725 |

### b) Liquidity risk

Prudent liquidity risk management implies maintaining sufficient cash and cash equivalents, combined with the availability of funding. The Group manages liquidity risk by continuously monitoring forecast and actual cash flows and matching the maturity profiles of financial assets and liabilities.

As at reporting date the Group had sufficient cash reserves to meet its current requirements. The Group therefore had no credit standby facilities or arrangements for further funding in place.

*Maturities of financial liabilities*

The tables below analyse the Group's and the Company'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 As at 30 June 2009 | Weighted average interest rate | Less than 6 months | 6-12 months | Between 1-2 years | Between 2-5 years | Over 5 years | Total contractual cashflows | Carrying Amounts |
|---|---|---|---|---|---|---|---|---|
| **Non derivatives** | | | | | | | | |
| Non-interest bearing | - | 6,344,813 | - | - | - | - | 6,344,813 | 6,344,813 |
| Variable rate | - | - | - | - | - | - | - | - |
| Fixed rate | 5.05% | 15,412 | 12,844 | - | - | - | 28,256 | 28,256 |

| Group As at 30 June 2008 | Weighted average interest rate | Less than 6 months | 6-12 months | Between 1-2 years | Between 2-5 years | Over 5 years | Total contractual cashflows | Carrying Amounts |
|---|---|---|---|---|---|---|---|---|
| **Non derivatives** | | | | | | | | |
| Non-interest bearing | - | 1,044,459 | - | - | - | - | 1,044,459 | 1,044,459 |
| Variable rate | - | - | - | - | - | - | - | - |
| Fixed rate | 5.05% | 6,522 | 6,522 | 13,044 | 11,957 | - | 38,045 | 34,421 |

| Parent As at 30 June 2009 | Less than 6 months | 6-12 months | Between 1-2 years | Between 2-5 years | Over 5 years | Total contractual cashflows | Carrying Amounts |
|---|---|---|---|---|---|---|---|
| **Non derivatives** | | | | | | | |
| Non-interest bearing | 5,467,114 | - | - | - | - | 5,467,114 | 5,467,114 |
| Variable rate | - | - | - | - | - | - | - |
| Fixed rate | - | - | - | - | - | - | - |

| Parent As at 30 June 2008 | Less than 6 months | 6-12 months | Between 1-2 years | Between 2-5 years | Over 5 years | Total contractual cashflows | Carrying Amounts |
|---|---|---|---|---|---|---|---|
| **Non derivatives** | | | | | | | |
| Non-interest bearing | 637,346 | - | - | - | - | 637,346 | 637,346 |
| Variable rate | - | - | - | - | - | - | - |
| Fixed rate | - | - | - | - | - | - | - |

### c) Market risk

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

*Currency risk*

The Group is exposed to currency risk on investments, purchases and borrowings that are denominated in a currency other than the respective functional currencies of Group entities, primarily the Australian dollar ("AUD"), but also the United States Dollar ("USD"). The currencies in which these transactions primarily are denominated are AUD and USD.

The Group has not entered into any derivative financial instruments to hedge such transactions and anticipated future receipts or payments that are denominated in a foreign currency.

Group's investments in its subsidiaries are not hedged as those currency positions are considered to be long term in nature.

*Exposure to currency risk*

The consolidated entity's operations in Turkey and the Philippines are conducted using US Dollars. Operating assets and liabilities are denominated in US Dollars and translated to Australian Dollars at balance sheet dates.

# NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

## 2. Financial Risk Management (Cont'd)

### c) Market risk (Cont'd)

Exposure to foreign currency risk at balance date was as follows, based on notional amounts:

| Group | 30 June 2009 | 30 June 2008 |
|---|---|---|
| | USD | USD |
| Trade Receivables | 31,972,104 | 10,095,145 |
| Secured bank loans | 22,741 | 10,157 |
| Trade Payables | 112,223 | 407,113 |
| Gross balance sheet exposure | 32,107,068 | 10,512,415 |
| **Company** | | |
| Secured bank loans | 22,741 | - |
| Intercompany receivables | 85,530,204 | - |
| Gross balance sheet exposure | 85,552,945 | - |

In 2009 no forward exchange contracts were entered into (2008: nil).

*Sensitivity Analysis*

A 10 percent strengthening of the Australian dollar against the following currencies at 30 June would have increased (decreased) equity and profit or loss by the amounts shown below. This analysis assumes that all other variables, in particular interest rates, remain constant. The analysis is performed on the same basis for 2008 and 2009. Management believe a 10% sensitivity rate to be reasonable based upon an assessment of current and expected market conditions.

| | Economic Entity | | Parent Entity | |
|---|---|---|---|---|
| | Equity | Profit or loss | Equity | Profit or loss |
| **30 June 2009** | | | | |
| USD | (7,225,449) | 3,038,005 | (8,119,384) | 3,625,869 |
| **30 June 2008** | | | | |
| USD | (9,319,715) | 872,001 | (9,290,352) | 990,534 |

A 10 percent weakening of the Australian dollar against the above currencies at 30 June would have had the equal but opposite effect on the above currencies to the amounts shown above, on the basis that all other variables remain constant.

*Cash flow and fair value at interest rate risk*

The Company's only interest rate risk arises from cash and cash equivalents held. Term deposits and current accounts held with variable interest rates expose the Company to cash flow interest rate risk. As shown in the table below a 50 basis points ("bps") strengthening at 30 June would have increased profit or loss and equity by the amounts shown below. Management have assessed the risk of a decrease in interest rates to be low and as such no sensitivity analysis has been provided. This conclusion is based upon an assessment of current and future market conditions.

| | | | +50bps |
|---|---|---|---|
| | Carrying Amount | Equity | Profit or loss |
| | | | |
| Economic Entity | 13,061,710 | 65,308 | 65,308 |
| Parent Entity | 11,912,122 | 59,560 | 59,560 |

### d) Fair value estimation

The Directors consider that the carrying amount of financial assets and financial liabilities recorded in the financial statements approximate their fair values.

## 3. Critical Accounting Estimates

The Directors evaluate estimates and judgements incorporated into the financial report based on historical knowledge and best available current information. Estimates assume a reasonable expectation of future events and are based on current trends and economic data, obtained both externally and within the Company. Please refer to the relevant note, where estimates and assumptions that have a significant risk of causing material adjustment to the carrying amounts of assets and liabilities within the next financial year, have been disclosed:

- Estimated impairment of goodwill and reserve estimates (refer note 11(b))
- Rehabilitation provision (refer note 15)
- Recoverability of exploration expenditure (refer note 13)
- Reserve estimates (refer to note 11(b))
- Income taxes (refer note 8)
- Share based payment expense (refer note 29)

## 4. Segment Reporting

### Primary Reporting – Business Segments

The consolidated entity currently operates wholly within the oil and gas exploration sector.

### Secondary Reporting – Geographical Segments

| | Segment Revenues from External Customers | | Segment Liabilities | | Carrying Amount of Segment Assets | | Acquisitions of Non Current Segment Assets | |
|---|---|---|---|---|---|---|---|---|
| | 2009 $ | 2008 $ | 2009 $ | 2008 $ | 2009 $ | 2008 $ | 2009 $ | 2008 $ |
| **Geographical Location:** | | | | | | | | |
| Australia | - | - | 1,205,439 | 637,346 | 641,178 | 9,366,662 | 97,985 | 155,756 |
| Turkey | 21,451 | 106,180 | 791,258 | 46,802 | 10,438,118 | 6,599,787 | 2,805,805 | 514,878 |
| Philippines | 1,794,330 | 503,361 | 180,270 | 441,535 | 82,140,619 | 82,706,256 | 5,996,388 | 56,866,000 |
| Argentina | - | - | - | - | - | 25,896 | 2,240,783 | 13,446 |
| Italy | - | - | 4,261,708 | - | 114 | 4,024,036 | 7,370,759 | 4,024,036 |
| Unallocated segment | 56,068 | 245,091 | - | - | 13,061,707 | 5,024,855 | 61,091 | - |
| | 1,871,849 | 854,632 | 6,438,675 | 1,125,683 | 106,281,736 | 107,747,492 | 18,572,811 | 61,574,116 |

# NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

## 4. Segment Reporting (Cont'd)

### Accounting Policies

Segment revenues and expenses are those directly attributable to the segments and include any joint revenue and expenses where a reasonable basis of allocation exists. Segment assets include all assets used by a segment and consist principally of receivables, plant and equipment, exploration expenditure capitalised net of accumulated depreciation and amortisation. While most such assets can be directly attributed to individual segments, the carrying amount of certain assets used jointly by two or more segments is allocated to the segments on a reasonable basis. Segment liabilities consist principally of payables, employee benefits and accrued expenses. Segment assets and liabilities do not include deferred income taxes.

### Geographical Segments

The consolidated entity's head office is located in Australia, with exploration work carried out in Turkey, the Philippines, Italy and Argentina.

## 5. Revenue

| | Economic Entity | | Parent Entity | |
|---|---|---|---|---|
| | 2009 $ | 2008 $ | 2009 $ | 2008 $ |
| Operating activities | | | | |
| - interest received (other) | 169,574 | 550,296 | 56,068 | 136,333 |
| - interest received from associates | 1,702,275 | 304,336 | - | - |
| Total revenue from continuing operations | 1,871,849 | 854,632 | 56,068 | 136,333 |

## 6. Other Income

| | Economic Entity | | Parent Entity | |
|---|---|---|---|---|
| | 2009 $ | 2008 $ | 2009 $ | 2008 $ |
| Foreign exchange gains | - | 12,357 | - | - |
| Profit on sale of licence interests | - | 3,324,169 | - | - |
| Other income | 728,229 | 1,848 | 728,229 | - |
| | 728,229 | 3,338,374 | 728,229 | - |

## 7. Expenses

| | | Economic Entity | | Parent Entity | |
|---|---|---|---|---|---|
| | Note | 2009 $ | 2008 $ | 2009 $ | 2008 $ |
| Share based payment expense | | 1,724,501 | 2,553,245 | 1,724,501 | 2,268,575 |
| | | | | | |
| *Finance Costs* | | | | | |
| Interest and finance charges | | 658,058 | 1,834 | 655,933 | 213 |
| | | | | | |
| *Depreciation* | | | | | |
| Plant and equipment | 12 | 165,729 | 71,175 | 115,722 | 59,539 |
| Motor Vehicles | 12 | 9,663 | 1,360 | - | - |
| | | 175,392 | 72,535 | 115,722 | 59,539 |
| *Impairment Expenses*[i] | | | | | |
| Impairment of loans receivable | 10 | 896,761 | - | 49,774,933 | - |
| Impairment of investments | 11a | - | - | 7,086,471 | - |
| Impairment of goodwill | 11b | 34,871,412 | - | - | - |
| Impairment of exploration assets | 13a | 11,396,740 | - | - | - |
| Impairment of investment in associate | 25 | 2,266,680 | - | 2,266,680 | - |
| | | 49,431,593 | - | 59,128,084 | - |
| | | | | | |
| [i]Refer to relevant notes for further details on impairment expenses. | | | | | |
| *Other Expenses* | | | | | |
| General administration | | 1,965,065 | 618,908 | 1,516,338 | 1,008,328 |
| Travel and accommodation expenses | | 714,512 | 385,723 | 630,238 | 307,631 |
| Consultant expenses | | 1,037,197 | 1,245,442 | 498,695 | 853,803 |
| | | 3,716,774 | 2,250,073 | 2,645,271 | 2,169,762 |

# NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

## 8. Income Tax Expense

| | Economic Entity | | Parent Entity | |
|---|---|---|---|---|
| | 2009 $ | 2008 $ | 2009 $ | 2008 $ |
| a) The components of tax expense comprise: | | | | |
| - Current tax | 9,107 | 582,232 | - | - |
| - Deferred tax | - | - | - | - |
| | 9,107 | 582,232 | - | - |
| b) The prima facie tax on the result from ordinary activities before income tax is reconciled to the income tax as follows: | | | | |
| Prime facie tax payable on the result from ordinary activities before income tax at 30% (2008: 30%) | | | | |
| - economic entity | (17,528,176) | (3,209,961) | - | - |
| - parent entity | - | - | (15,995,848) | (3,646,301) |
| | (17,528,176) | (3,209,961) | (15,995,848) | (3,646,301) |
| Add tax effect of: | | | | |
| - other non-allowable items | 1,906,384 | 995,154 | 18,696,377 | 862,637 |
| | (15,621,792) | (2,214,807) | 2,700,529 | (2,783,664) |
| Less tax effect of: | | | | |
| - issue costs charged to equity | - | (33,635) | - | (33,635) |
| Deferred tax asset not previously recognised now brought into account | - | | (2,700,529) | - |
| Benefits of tax losses and other timing differences not brought to account | 15,621,792 | 2,830,674 | - | 2,817,299 |
| Income tax attributable | - | 582,232 | - | - |
| c) Deferred tax balances not brought to account, the benefits of which will only be realised if the conditions for deductibility set out in Note 1(b) occur. | | | | |
| - temporary differences | 2,902,525 | 1,991,004 | 2,902,525 | 1,991,004 |
| - tax losses: revenue | 3,896,933 | 2,096,022 | 3,896,933 | 1,666,926 |
| - tax losses: foreign | 18,828,177 | 229,963 | - | 229,963 |
| | 25,627,635 | 4,316,989 | 6,799,458 | 3,887,893 |
| Offset against deferred tax liabilities recognised | (2,074,346) | - | (2,074,346) | - |
| Deferred tax assets not brought to account | 23,553,289 | 4,316,989 | 4,725,112 | 3,887,893 |
| d) Deferred tax liabilities | | | | |
| Timing differences | 2,074,346 | - | 2,074,346 | - |
| Offsets by Deferred Tax Assets recognised | (2,074,346) | - | (2,074,346) | - |
| | - | - | - | - |

e) The Deferred Tax Asset not brought to account for 2009 year will only be obtained if:

i. the Company derives future assessable income of a nature and of an amount sufficient to enable the benefit to be realised;
ii. the Company continues to comply with the conditions of deductibility imposed by tax legislation; and
iii. the Company is able to meet the continuity of ownership and/or continuity off business tests

## 9. Cash and Cash Equivalents

| | Economic Entity | | Parent Entity | |
|---|---|---|---|---|
| | 2009 $ | 2008 $ | 2009 $ | 2008 $ |
| Cash at bank and in hand | 12,552,065 | 3,348,138 | 11,745,734 | 2,801,225 |
| Short-term bank deposits | 509,645 | 1,685,724 | 166,388 | 114,500 |
| | 13,061,710 | 5,033,862 | 11,912,122 | 2,915,725 |

The effective interest rate on short-term bank deposits was 6.39% (2008: 5.18%). The above balances reconcile to cash at the end of the financial year as shown in the Statement of Cash Flows. Further information on fair values and interest rate risk are set out in Note 2.

## 10. Trade and Other Receivables

| CURRENT | Note | | | | |
|---|---|---|---|---|---|
| Other receivables | | 400,717 | 19,050,218 | 139,862 | 8,955,073 |
| Employee Loan | | 100,854 | - | 100,854 | - |
| Goods and services tax | | 205,490 | 147,796 | 205,490 | 147,796 |
| | | 707,061 | 19,198,014 | 446,206 | 9,102,869 |
| **NON-CURRENT** | | | | | |
| Wholly-owned entities | | - | - | 129,830,699 | 82,004,187 |
| Associates (i) | | 40,623,530 | 15,814,075 | - | - |
| Provision for impairment (ii) | 7 | (896,761) | - | (49,774,933) | - |
| Other receivables | | 10,520 | 6,750 | - | - |
| | | 39,737,289 | 15,820,825 | 80,055,766 | 82,004,187 |

Further information relating to fair values and interest rate risk are set out in Note 2.

(i) Loan conditions:

The loan bears interest of three percent above LIBOR rate compounded quarterly and is repayable within 5 years from the date of the initial loan. In 2009, The Group has provided USD $15,444,146 in total support to the financing party and additional loan to GPC, and recognised interest income of USD $1,254,853 that was capitalised as part of the loan balance.

(ii) Impaired receivables:

Loans to wholly-owned entities and loans to associate entities have been tested for impairment, in total an impairment loss of $49,774,933 has been recognised of which $48,878,172 relates to the Company's loan receivable with Norasian Energy Limited and Otto Energy (Europe) Limited and $896,761 related to loans to an associate entity Cynthia Holdings Limited. Management consider this portion of the loan not to be recoverable by reference to the carrying value of the net assets of Norasian Energy Limited, Otto Energy (Europe) Limited and the abandonment of exploration activities in Argentina.

(iii) Past due but not impaired:

As of 30 June 2009, there were no trade and other receivables past due but not impaired with the exception of loans to wholly-owned entities and loans to associates (refer note 10(ii)). All other trade and other receivables are not impaired or not past due based on management's assessment.

# NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

## 11. (a) Other Financial Assets

| | Note | Economic Entity | | Parent Entity | |
|---|---|---|---|---|---|
| | | 2009 $ | 2008 $ | 2009 $ | 2008 $ |
| Other financial assets | | - | - | 1,500,250 | 8,586,721 |
| | | - | - | 1,500,250 | 8,586,721 |
| Less non-current portion | | - | - | (1,500,250) | (8,586,721) |
| Current portion | | - | - | - | - |
| **Other Financial Assets comprise:** | | | | | |
| Unlisted investments, at cost | | | | | |
| Shares in controlled entities | | - | - | 8,586,721 | 8,586,721 |
| Impairment of investments | 7 | - | - | (7,086,471) | - |
| | | - | - | 1,500,250 | 8,586,721 |

Other financial assets comprise investments in the ordinary share capital of various entities. There are no fixed returns or fixed maturity date attached to these investments. The fair value of unlisted other financial assets cannot be reliably measured as variability in the range of reasonable fair value estimates is significant. As a result, all unlisted investments are reflected at cost. Further information on fair values and interest rate risk are set out in Note 2.

(i) Impairment charge:
An impairment expense was recognised on the Company's investment in Norasian Energy Limited ("NEL") of $7,086,471. The Company considered the investment to be impaired as the NEL consolidated balance sheet was in net deficiency of $37,206,908 after accounting for intercompany loans payable of $111,134,175.

## 11. (b) Intangible Assets

| | Note | Economic Entity | | Parent Entity | |
|---|---|---|---|---|---|
| | | 2009 $ | 2008 $ | 2009 $ | 2008 $ |
| Goodwill on acquisition of controlled entities | 23 | 7,542,044 | 35,425,041 | - | - |
| Balance at the beginning of the year | | 35,425,041 | - | - | - |
| Additions – acquisition | | - | 35,425,041 | - | - |
| Amortisation charge | | - | - | - | - |
| Impairment expense | 7 | (34,871,412) | - | - | - |
| Exchange differences (i) | | 6,988,415 | - | - | - |
| Balance and net book value at the end of year | | 7,542,044 | 35,425,041 | - | - |

(i) Exchange differences:
The goodwill on acquisition balance is held in the wholly owned subsidiary, NorAsian Energy Limited, which has a functional currency of USD, whereas the parent entity has a functional currency of AUD dollars. As a result, foreign exchange differences arise based upon movements in AUD and USD currencies and the recognition of goodwill on consolidation and the conversion to presentational currency. The exchange differences arising upon translation are recognised through the foreign currency translation reserve.

(ii) Impairment test for Goodwill:
The Goodwill is held within the Norasian Energy Limited group which is attributable to the acquisition of Colag BVI Limited (formerly Cape Energy Philippines SA) and Colag UK Limited (formerly Team Oil Limited) which each hold a 15.69% ownership interest in the Galoc Production Company W.L.L ("GPC").
The recoverable amount of the goodwill is determined based on value-in-use calculations.
These calculations are based upon discounted cash flow forecasts covering a five year period.

(iii) The key assumptions and inputs used in the value-in-use model for the Galoc oil field were:

Discount rate: 15%

Oil price: US$60/barrel

Up time: 85% per annum
(75% during typhoon season periods and 95% during non typhoon- season periods.)

(iv) Impact on possible changes in key assumptions:

**Oil price per barrel**

Should the oil price utilised increase to US$65/barrel this would result reduction to impairment expense of approximately $6m. Alternatively if US$55/barrel was used this would have resulted in an increase in the impairment expense by approximately $7m.

**Percentage of production "up time and down time"**

The percentage "up time" and "down time" was not considered a key assumption as a change in these variables would simply defer cash flows from period to period and would unlikely result in a material change to the total cash flows of the project.

**Reserve estimates**

Otto reports its petroleum reserve and resource estimates using definitions and guidelines published in the Society of Petroleum Engineers Inc./World Petroleum Congresses/American Association of Petroleum Geologists/Society of Petroleum Evaluation Engineers Petroleum Resources Management System (March 2007) The estimated quantities of proven plus probably hydrocarbon reserves utilised by the Company within the value-in-use calculation are integral to the calculation of impairment model. Estimated reserve quantities are based upon interpretation of geological and geophysical models and assessments of technical and commercial feasibility. These assessments require assumptions to be made regarding future development, production costs, commodity prices, exchange rates and fiscal regimes. The assessment of reserves may change from period to period based upon on changes in economic assumptions.

(v) Impairment charge:
The value-in-use model calculates the recoverable amount of the goodwill in the Norasian Energy Limited group relating to their indirect interest in the Galoc oil field to be $46,409,046. After adjusting for loans to associates of $38,631,403, the recoverable amount exceeded the carrying value of goodwill at 30 June 2009 and an impairment loss of $34,871,412 was recognised against goodwill within the Norasian Energy Limited group.

(vi) Managements assessment of impairment:
The impairment loss above has been determined in accordance with the requirements of AASB 136 *Impairment of Assets.* AASB 136 limits the nature of the cash flows that can be included within the discounted cash flow model to only those that can be generated by the asset in its current state. As such the current value-in-use calculations exclude any estimated future cash inflows or outflows expected to arise from future expansion plans or from enhancing the asset's performance. It is the opinion of management that had the cash flows arising from future expansion plans been included within the discounted cash flow forecasts, the value in use calculation would have supported the carrying value of the investment at balance date.

# NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

## 12. Property Plant and Equipment

| | Economic Entity | | Parent Entity | |
|---|---|---|---|---|
| | 2009 $ | 2008 $ | 2009 $ | 2008 $ |
| At cost | 668,419 | 460,721 | 386,202 | 288,218 |
| Accumulated depreciation | (289,457) | (114,872) | (207,097) | (91,376) |
| | 378,962 | 345,849 | 179,105 | 196,842 |

| Consolidated Entity: | Plant and Equipment $ | Motor Vehicles $ | Total $ |
|---|---|---|---|
| **Year Ended 30 June 2008** | | | |
| Balance at the beginning of year | 94,068 | - | 94,068 |
| Additions | 283,875 | 40,441 | 324,316 |
| Disposals | - | - | - |
| Depreciation expense | (71,175) | (1,360) | (72,535) |
| Carrying amount at the end of year | 306,768 | 39,081 | 345,849 |
| **Year Ended 30 June 2009** | | | |
| Balance at the beginning of year | 306,768 | 39,081 | 345,849 |
| Additions | 174,129 | - | 174,129 |
| Disposals | - | - | - |
| Depreciation expense | (165,729) | (9,663) | (175,392) |
| Exchange differences (i) | 26,767 | 7,609 | 34,376 |
| Carrying amount at the end of year | 341,935 | 37,027 | 378,962 |

(i) Exchange differences:
A portion of the property, plant and equipment balance is held in the wholly owned subsidiary, NorAsian Energy Limited, which has a functional currency of USD, whereas the parent entity has a functional currency of AUD. As a result, foreign exchange differences arise based upon movements in AUD and USD currencies and the recognition of property, plant and equipment on consolidation and the conversion to presentational currency. The exchange differences are recognised through the foreign currency translation reserve.

| Parent Entity: | Plant and Equipment $ | Total $ |
|---|---|---|
| **Year Ended 30 June 2008** | | |
| Balance at the beginning of year | 41,086 | 41,086 |
| Additions | 215,296 | 215,295 |
| Disposals | - | - |
| Revaluation increments/(decrements) | - | - |
| Depreciation expense | (59,539) | (59,539) |
| Carrying amount at the end of year | 196,842 | 196,842 |
| **Year Ended 30 June 2009** | | |
| Balance at the beginning of year | 196,842 | 196,842 |
| Additions | 97,985 | 97,985 |
| Disposals | - | - |
| Revaluation increments/(decrements) | - | - |
| Depreciation expense | (115,722) | (115,722) |
| Carrying amount at the end of year | 179,105 | 179,105 |

## 13. Other Assets

| | Economic Entity | | Parent Entity | |
|---|---|---|---|---|
| | 2009 $ | 2008 $ | 2009 $ | 2008 $ |
| **CURRENT** | | | | |
| Prepayments | 55,788 | 102,315 | 15,867 | 66,951 |
| **NON-CURRENT** | | | | |
| Capitalised exploration and evaluation expenditure | 44,798,882 | 31,821,586 | - | 4,049,932 |

The recoverability of the carrying amount of exploration assets is dependent on the successful development and commercial exploitation or sale of the respective mining tenements. Amortisation of the costs carried forward for the development phase is not being charged pending the commencement of production.

Capitalised costs amounting to $12,839,394 (2008:$ 13,219,662) have been included in cash flows from operating activities in the Cash Flow Statement.

### a) Movements in Carrying Amounts

Movement in the carrying amounts for exploration expenditure capitalised between the beginning and the end of the current financial year.

| | Other Assets $ |
|---|---|
| **Economic Entity:** | |
| Balance at the beginning of year | 31,821,586 |
| Additions | 18,524,826 |
| Disposals | - |
| Transfers to investments in associate | (2,266,679) |
| Impairment expense (i) | (11,394,795) |
| Capitalised costs written off | (191,836) |
| Exchange differences (ii) | 8,305,780 |
| Amortisation expense | - |
| Carrying amount at the end of year | 44,798,882 |

(i) Impairment charge:
An impairment expense was recognised in Otto Energy (Europe) Limited of $11,394,795 relating to exploration expenditure in it's wholly owned Italian subsidiary Otto Energy (Italy) S.r.L in relation to the Cento-Bastiglia permits. As announced to the market on the 16 June 2009 the Company has abandoned all exploration activities in the license area as drilling results to date indicate the lack of a commercial reserve.

(ii) Exchange differences:
A portion of the other assets balance is held in the wholly owned subsidiary, NorAsian Energy Limited, which has a functional currency of USD, whereas the parent entity has a functional currency of AUD. As a result, foreign exchange differences arise based upon movements in AUD and USD currencies and the recognition of other assets on consolidation and the conversion to presentational currency. The exchange differences are recognised through the foreign currency translation reserve.

# NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

## 13. Other Assets (Cont'd)

| Parent Entity: | Other Assets $ |
|---|---|
| Balance at the beginning of year | 4,049,932 |
| Additions | 5,708,054 |
| Disposals | - |
| Transfer to subsidiary | (7,427,216) |
| Capitalised costs written off | (64,091) |
| Impairment expense | (2,266,679) |
| Amortisation expense | - |
| Carrying amount at the end of year | - |

## 14. Trade and Other Payables

| | Economic Entity | | Parent Entity | |
|---|---|---|---|---|
| | 2009 $ | 2008 $ | 2009 $ | 2008 $ |
| CURRENT | | | | |
| Unsecured liabilities | | | | |
| Trade payables | 929,325 | 658,137 | 466,077 | 251,024 |
| Sundry payables and accrued expenses(i) | 5,453,435 | 396,479 | 5,001,037 | 386,322 |
| | 6,382,760 | 1,054,616 | 5,467,114 | 637,346 |
| NON-CURRENT | | | | |
| Trade payables | - | 24,265 | - | - |
| | - | 24,265 | - | - |

Further information on fair values and interest rate risk are set out in Note 2.

(i) Amounts not expected to be settled within the next 12 months:

Other payables include accruals for annual leave. The entire obligation is presented as current, since the Group does not have an unconditional right to defer settlement. However, based on past experience, the Group does not expect all employees to take the full amount of accrued leave within the next 12 months. The amounts disclosed below reflect leave that is not expected to be taken with the next 12 months.

| | Economic Entity | | Parent Entity | |
|---|---|---|---|---|
| | 2009 $ | 2008 $ | 2009 $ | 2008 $ |
| Non-current obligation | 68,434 | 34,724 | 68,434 | 34,724 |

## 15. Provisions

| | Economic Entity | | Parent Entity | |
|---|---|---|---|---|
| | 2009 $ | 2008 $ | 2009 $ | 2008 $ |
| NON-CURRENT | | | | |
| Provision for restoration | 55,915 | 46,802 | - | - |
| | 55,915 | 46,802 | - | - |

## 16. Contributed Equity

| | Economic Entity | | Parent Entity | |
|---|---|---|---|---|
| | 2009 $ | 2008 $ | 2009 $ | 2008 $ |
| 1,070,184,721 (2008: 476,654,632) fully paid ordinary shares | 151,932,731 | 118,064,437 | 151,932,731 | 118,064,437 |

### a) Ordinary Share Capital

| | Issue Price. | No. | No. | $ | $ |
|---|---|---|---|---|---|
| At the beginning of year | | 476,654,632 | 172,903,994 | 118,064,437 | 27,392,420 |
| Shares issued during year | | | 303,750,638 | | 94,490,498 |
| - 04 July 2008 | 0.39 | 769,231 | | 300,000 | |
| - 14 July 2008 | 0.20 | 250,000 | | 50,000 | |
| - 10 October 2008 | 0.305 | 15,000,000 | | 4,575,000 | |
| - 27 March 2009 | 0.07 | 73,901,079 | | 5,173,076 | |
| - 14 May 2009 | 0.05 | 324,782,353 | | 16,239,118 | |
| - 18 May 2009 | 0.05 | 100,148,854 | | 5,007,443 | |
| - 18 May 2009 | 0.07 | 61,000,000 | | 4,270,000 | |
| - 18 May 2009 | 0.081 | 5,000,000 | | 405,000 | |
| - 03 June 2009 | 0.07 | 11,428,572 | | 800,000 | |
| - 29 June 2009 | 0.08 | 1,250,000 | | 100,000 | |
| Transaction Costs | | | | (3,051,343) | (3,818,481) |
| | | 1,070,184,721 | 476,654,632 | 151,932,731 | 118,064,437 |

i. Ordinary shares entitle the holder to participate in dividends and the proceeds on winding up of the Company in proportion to the number and amount 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. The ordinary shares have no par value and the company does not have a limited amount of authorised capital.

### b) Options

ii. For information relating to share options issued to Directors during the financial year, refer to Note 29.

### Capital risk management

The Company's objectives when managing capital are to safeguard their ability to continue as a going concern, so that they can continue to provide returns to shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital. In order to maintain or adjust the capital structure, the Company may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt.

| Consolidated | Note | 2009 $ | 2008 $ |
|---|---|---|---|
| Total borrowings | | - | - |
| Less: cash and cash equivalents | 9 | (13,061,710) | (5,033,862) |
| Net debt | | - | - |
| Total equity | | 98,757,386 | 106,621,809 |
| Total capital | | 98,757,386 | 106,621,809 |

The Group does not currently have any external debt facilities as these were repaid during the year.

# NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

## 17. Reserves and Accumulated Losses

| | Economic Entity | | Parent Entity | |
|---|---|---|---|---|
| | 2009 $ | 2008 $ | 2009 $ | 2008 $ |
| **RESERVES** | | | | |
| Foreign Currency Translation Reserve | 13,711,017 | (1,185,698) | - | - |
| Share Based Payment Reserve | 4,656,926 | 2,932,424 | 4,656,926 | 2,932,424 |
| Option Reserve | 2,328,269 | 2,245,250 | 2,328,269 | 2,245,250 |
| | 20,696,212 | 3,991,976 | 6,985,195 | 5,177,674 |
| **ACCUMULATED LOSSES** | | | | |
| Accumulated Losses | (72,783,381) | (15,434,604) | (70,275,724) | (16,956,230) |
| | (72,783,381) | (15,434,604) | (70,275,724) | (16,956,230) |

| | Economic Entity | | Parent Entity | |
|---|---|---|---|---|
| | 2009 | 2008 $ | 2009 | 2008 $ |
| **Foreign Currency Translation Reserve** | | | | |
| Balance at beginning of year | (1,185,698) | (67,163) | - | - |
| Currency translation differences arising during the year | 14,896,715 | (1,118,535) | - | - |
| As at end of year | 13,711,017 | (1,185,698) | - | - |
| **Share Based Payments Reserve** | | | | |
| Balance at beginning of year | 2,932,424 | 379,179 | 2,932,424 | 379,179 |
| Share-based payments | 1,724,502 | 2,553,245 | 1,724,502 | 2,553,245 |
| As at end of year | 4,656,926 | 2,932,424 | 4,656,926 | 2,932,424 |
| **Option Reserve** | | | | |
| Balance at beginning of year | 2,245,250 | 821,250 | 2,245,250 | 821,250 |
| Option expense | 83,019 | 1,424,000 | 83,019 | 1,424,000 |
| As at end of year | 2,328,269 | 2,245,250 | 2,328,269 | 2,245,250 |
| **Accumulated Losses** | | | | |
| Balance at beginning of year | (15,434,604) | (4,734,732) | (16,956,230) | (4,801,895) |
| Loss for the year | (57,348,777) | (10,699,872) | (53,319,494) | (12,154,336) |
| As at end of year | (72,783,381) | (15,434,604) | (70,275,724) | (16,956,230) |

### a) Foreign Currency Translation Reserve

The foreign currency translation reserve records exchange differences arising on translation of foreign controlled subsidiaries.

### b) Option Reserve

The option reserve records the value attributed to the Otto Energy Limited options issued as part of the purchase consideration paid to acquire subsidiary entities.

### c) Share Based Payments Reserve

The share based payment reserve records equity based compensation granted to employees.

## 18. Key Management Personnel Disclosures

### a) Key management personnel compensation

| | Economic Entity | | Parent Entity | |
|---|---|---|---|---|
| | 2009 $ | 2008 $ | 2009 $ | 2008 $ |
| Short -term employee benefits | 1,679,389 | 1,293,815 | 1,679,389 | 1,293,815 |
| Post-employment benefits | 115,003 | 76,131 | 115,003 | 76,131 |
| Termination benefits | 308,860 | - | 308,860 | - |
| Share-based payments | 1,358,992 | 2,023,234 | 1,358,992 | 2,023,234 |
| | 3,462,244 | 3,393,180 | 3,462,244 | 3,393,180 |

Detailed remuneration disclosures are provided in sections A-C of the audited remuneration report on pages 36 to 45.

### b) Equity instrument disclosures relating to key management personnel

i. Options provided as remuneration and shares issued on exercise of such options

Details of options provided as remuneration and shares issued on the exercise of such options, together with terms and conditions of the options, can be found in section D of the remuneration report on pages 42-43.

ii. Option holdings

The number of options over ordinary shares in the Company, held during the financial year by the Directors and Executives of Otto Energy Limited, including their personally related parties, are set out below.

| 2009 | Balance at Start of Year | Granted During the Year as Compensation | Exercised During the Year | Other Changes During the Year | Balance at End of Year | Vested and Exercisable at End of Year |
|---|---|---|---|---|---|---|
| **Directors** | | | | | | |
| Mr R Crabb | 1,500,000 | - | - | - | 1,500,000 | 1,500,000 |
| Dr J Poll (i) | 3,000,000 | - | - | - | 3,000,000 | 3,000,000 |
| Mr I Macliver(ii) | 1,500,000 | - | - | 2,000,000 | 3,500,000 | 3,500,000 |
| Mr J Zadnik(iii) | 500,000 | - | - | - | 500,000 | 500,000 |
| Mr R Bomasang (iv) | 1,000,000 | - | - | - | 1,000,000 | 666,667 |
| Mr J Jetter (v) | 6,000,000 | - | - | - | 6,000,000 | 6,000,000 |
| | 13,500,000 | - | - | 2,000,000 | 15,500,000 | 15,166,667 |
| **Other Key Management Personnel** | | | | | | |
| Mr A Parks (vi) | 6,500,000 | - | - | - | 6,500,000 | 5,500,000 |
| Mr C Martin (vii) | 2,500,000 | - | - | - | 2,500,000 | 2,166,700 |
| Ms I Holt | - | - | - | - | - | - |
| Mr R King | - | 2,500,000 | - | - | 2,500,000 | - |
| Mr S Kleffmann | - | - | - | 1,500,000 | 1,500,000 | - |
| | 9,000,000 | 2,500,000 | - | 1,500,000 | 13,000,000 | 7,666,700 |

# NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

## 18. Key Management Personnel Compensation (Cont'd)

### b) Equity instrument disclosures relating to key management personnel (Cont'd)

i. Dr J Poll held 1,000,000 plan options under the ESOP which have a vesting date of 31 May 2008
Dr J Poll held 1,000,000 plan options under the ESOP which have a vesting date of 30 November 2008
Dr J Poll held 1,000,000 plan options under the ESOP which have a vesting date of 29 January 2009

ii. Mr I Macliver held 1,000,000 plan options under the ESOP which have a vesting date of 29 January 2009
Mr I Macliver transferred 500,000 plan options to a non director related entity.
Mr I Macliver, through a director related entity received 2,000,000 options in consideration for corporate advisory services.

iii. Mr J Zadnik held 500,000 plan options under the ESOP which have a vesting date of 29 January 2009

iv. Mr R Bomasang held 333,334 plan options under the ESOP which have a vesting date of 31 May 2008
Mr R Bomasang held 333,333 plan options under the ESOP which have a vesting date of 30 November 2008
Mr R Bomasang held 333,333 plan options under the ESOP which have a vesting date of 31 May 2009

v. Mr J Jetter held 6,000,000 plan options under the ESOP which were not subject to an escrow period

vi. Mr A Parks held 1,000,000 plan options under the ESOP which have a vesting date of 31 May 2008
Mr A Parks held 1,000,000 plan options under the ESOP which have a vesting date of 30 November 2008
Mr A Parks held 1,000,000 plan options under the ESOP which have a vesting date of 31 May 2009
Mr A Parks held 3,500,000 plan options under the ESOP which have a vesting date of 31 December 2008

vii. Mr C Martin held 333,400 plan options under the ESOP which have a vesting date of 31 May 2008
Mr C Martin held 333,300 plan options under the ESOP which have a vesting date of 30 November 2008
Mr C Martin held 333,300 plan options under the ESOP which have a vesting date of 31 May 2009
Mr C Martin held 1,500,000 plan options under the ESOP which have a vesting date of 31 December 2008

| 2008 | Balance at Start of Year | Granted During the Year as Compensation | Exercised During the Year | Other Changes During the Year | Balance at End of Year | Vested and Exercisable at End of Year |
|---|---|---|---|---|---|---|
| Directors | | | | | | |
| Mr R Crabb | - | 1,500,000 | - | - | 1,500,000 | - |
| Dr J Poll (i) | 4,000,000 | 1,000,000 | (1,000,000) | (1,000,000) | 3,000,000 | 1,000,000 |
| Mr I Macliver(ii) | - | 2,000,000 | - | (500,000) | 1,500,000 | - |
| Mr J Zadnik(iii) | - | 500,000 | - | - | 500,000 | - |
| Mr R Bomasang (iv) | 1,000,000 | - | - | - | 1,000,000 | 333,334 |
| Mr J Jetter (v) | - | 6,000,000 | - | - | 6,000,000 | 6,000,000 |
| | 5,000,000 | 11,000,000 | (1,000,000) | (1,500,000) | 13,500,000 | 7,333,334 |
| Other Key Management Personnel | | | | | | |
| Mr A Parks (vi) | 3,000,000 | 3,500,000 | - | - | 6,500,000 | 1,000,000 |
| Mr C Martin (vii) | 1,000,000 | 1,500,000 | - | - | 2,500,000 | 333,400 |
| Mr B Elsholz (viii) | 1,000,000 | 500,000 | - | - | 1,500,000 | 333,333 |
| | 5,000,000 | 5,500,000 | - | - | 10,500,000 | 1,666,733 |

viii. Dr J Poll held 1,000,000 plan options under the ESOP which have a vesting date of 31 May 2008
Dr J Poll held 1,000,000 plan options under the ESOP which have a vesting date of 30 November 2008
Dr J Poll held 1,000,000 plan options under the ESOP which have a vesting date of 29 January 2009

ix. Mr I Macliver held 2,000,000 plan options under the ESOP which have a vesting date of 29 January 2009
Mr I Macliver transferred 500,000 plan options to a non director related entity

x. Mr J Zadnik held 500,000 plan options under the ESOP which have a vesting date of 29 January 2009

xi. Mr R Bomasang held 333,334 plan options under the ESOP which have a vesting date of 31 May 2008
Mr R Bomasang held 333,333 plan options under the ESOP which have a vesting date of 30 November 2008
Mr R Bomasang held 333,333 plan options under the ESOP which have a vesting date of 31 May 2009

xii. Mr J Jetter held 6,000,000 plan options under the ESOP which were not subject to an escrow period

xiii. Mr A Parks held 1,000,000 plan options under the ESOP which have a vesting date of 31 May 2008
Mr A Parks held 1,000,000 plan options under the ESOP which have a vesting date of 30 November 2008
Mr A Parks held 1,000,000 plan options under the ESOP which have a vesting date of 31 May 2009
Mr A Parks held 3,500,000 plan options under the ESOP which have a vesting date of 31 December 2008

xiv. Mr C Martin held 333,400 plan options under the ESOP which have a vesting date of 31 May 2008
Mr C Martin held 333,300 plan options under the ESOP which have a vesting date of 30 November 2008
Mr C Martin held 333,300 plan options under the ESOP which have a vesting date of 31 May 2009
Mr C Martin held 1,500,000 plan options under the ESOP which have a vesting date of 31 December 2008

xv. Mr B Elsholz held 333,333 plan options under the ESOP which have a vesting date of 31 May 2008
Mr B Elsholz held 333,333 plan options under the ESOP which have a vesting date of 30 November 2008
Mr B Elsholz held 333,334 plan options under the ESOP which have a vesting date of 31 May 2009
Mr B Elsholz held 500,000 plan options under the ESOP which have a vesting date of 31 December 2008

iii. Shareholdings

The numbers of shares in the Company held during the financial year by each Director and Executive of Otto Energy Limited, including their personally related parties, are set out below:

| 2009 | Balance at Start of Year | Granted During the Year as Compensation | Received During the Year on the Exercise of Options | Other Changes During Year | Balance at End of Year |
|---|---|---|---|---|---|
| Directors | | | | | |
| Mr R Crabb | 5,500,397 | - | - | 7,869,655 | 13,370,052 |
| Mr J Poll | 7,011,290 | - | - | 6,532,916 | 13,544,206 |
| Mr I Macliver | 3,994,737 | - | - | 2,312,205 | 6,306,942 |
| Mr J Zadnik | 3,068,000 | - | - | 2,301,000 | 5,369,000 |
| Mr R Bomasang | - | - | - | - | - |
| Mr J Jetter | 5,800,000 | - | - | 13,289,175 | 19,089,175 |
| | 25,374,424 | - | - | 31,304,951 | 57,679,375 |
| Other Key Management Personnel | | | | | |
| Mr A Parks | - | - | - | - | - |
| Mr C Martin | 1,800,000 | - | - | 1,800,000 | 1,800,000 |
| Ms I Holt | - | - | - | - | - |
| Mr R King | - | - | - | - | - |
| Mr S Kleffmann | - | - | - | - | - |
| | 1,800,000 | - | - | 1,800,000 | 1,800,000 |

# NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

## 18. Key Management Personnel Compensation (Cont'd)

### b) Equity instrument disclosures relating to key management personnel (Cont'd)

| 2008 | Balance at Start of Year | Granted During the Year as Compensation | Received During the Year on the Exercise of Options | Other Changes During Year | Balance at End of Year |
|---|---|---|---|---|---|
| **Directors** | | | | | |
| Mr R Crabb | 5,500,397 | - | - | - | 5,500,397 |
| Mr J Poll | 6,349,500 | - | 1,000,000 | (338,210) | 7,011,290 |
| Mr I Macliver | 3,994,737 | - | - | - | 3,994,737 |
| Mr J Zadnik | 3,064,500 | - | - | 3,500 | 3,068,000 |
| Mr R Bomasang | - | - | - | - | - |
| Mr J Jetter | - | - | - | 5,800,000 | 5,800,000 |
| | 18,909,134 | - | 1,000,000 | 5,465,290 | 25,374,424 |
| **Other Key Management Personnel** | | | | | |
| Mr A Parks | - | - | - | - | - |
| Mr C Martin | 1,800,000 | - | - | - | 1,800,000 |
| Mr B Elsholz | - | - | - | - | - |
| | 1,800,000 | - | - | - | 1,800,000 |

| Performance Shares 2009 | Balance at Start of Year | Granted During the Year as Compensation | Received During the Year on the Exercise of Options | Other Changes During Year | Balance at End of Year |
|---|---|---|---|---|---|
| **Directors** | | | | | |
| Mr R Crabb | 625,000 | - | - | - | 625,000 |
| Mr J Poll | 1,250,000 | - | - | 4,000 | 1,254,000 |
| Mr I Macliver | - | - | - | - | - |
| Mr D Riekie | - | - | - | - | - |
| Mr J Zadnik | 625,000 | - | - | - | 625,000 |
| Mr R Bomasang | - | - | - | - | - |
| Mr J Jetter | - | - | - | - | - |
| | 2,500,000 | - | - | 4,000 | 2,504,000 |
| **Other Key Management Personnel** | | | - | - | - |
| Mr A Parks | - | - | - | - | - |
| Mr C Martin | - | - | - | - | - |
| Ms I Holt | - | - | - | - | - |
| Mr R King | - | - | - | - | - |
| Mr S Kleffmann | - | - | - | - | - |
| | - | - | - | - | - |

| Performance Shares 2008 | Balance at Start of Year | Granted During the Year as Compensation | Received During the Year on the Exercise of Options | Other Changes During Year | Balance at End of Year |
|---|---|---|---|---|---|
| **Directors** | | | | | |
| Mr R Crabb | 625,000 | - | - | - | 625,000 |
| Mr J Poll | 1,250,000 | - | - | - | 1,250,000 |
| Mr I Macliver | - | - | - | - | - |
| Mr D Riekie | - | - | - | - | - |
| Mr J Zadnik | 625,000 | - | - | - | 625,000 |
| Mr R Bomasang | - | - | - | - | - |
| Mr J Jetter | - | - | - | - | - |
| | 2,500,000 | - | - | - | 2,500,000 |
| **Other Key Management Personnel** | | | | | |
| Mr A Parks | - | - | - | - | - |
| Mr C Martin | - | - | - | - | - |
| Mr B Elsholz | - | - | - | - | - |
| | - | - | - | - | - |

### c) Loans to key management personnel

Details of loans made to other key management personnel of the Group, including their personally related parties, are set out below.

(i) Aggregates for key management personnel

| Group | Balance at the start of the year | Interest payable for year | Interest not charged | Balance at the end of the year | Number in Group at the end of the year |
|---|---|---|---|---|---|
| | $ | $ | $ | $ | |
| 2009 | - | 855 | - | 100,855 | 1 |
| 2008 | - | - | - | - | - |

(ii) Individuals with loans above $100,000 during the financial year.

Mr Alex Parks currently owes the company $100,000 plus accrued interest costs. The loan is repayable on or before 30 June 2010 and is subject to 6.5% interest per annum. Mr Parks is not considered a key management person at 30 June 2009 under *AASB 124 Related Party Disclosures* as he resigned effective from this date, however in the interest of transparency management have elected to disclose this information.

## 19. Auditors' Remuneration

| | Economic Entity | | Parent Entity | |
|---|---|---|---|---|
| | 2009 $ | 2008 $ | 2009 $ | 2008 $ |
| a) Audit Services -<br>BDO Kendalls Audit & Assurance (WA) Pty Ltd: | | | | |
| - Audit and review of financial reports<br>- Non-BDO Kendalls Audit & Assurance (WA) Pty Ltd | 79,850<br>- | 80,328<br>- | 79,850<br>- | 80,328<br>- |
| b) Non-Audit Services<br>BDO Kendalls Corporate Tax (WA) Pty Ltd:<br>- Taxation services | 10,360 | 10,050 | 10,360 | 10,050 |
| | 90,210 | 90,378 | 90,210 | 90,378 |

# NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

## 20. Contingent Liabilities and Contingent Assets

### Legal Proceeding

NorAsian Energy Limited ("NorAsian"), a wholly owned subsidiary of Otto Energy Limited, was one of the three respondents to a petition made by a local non-government organisation regarding the validity of the environmental permit issued to the Company by the Philippine Department of Environment and Natural Resources (DENR). The Permit (Certificate of Non-Coverage) allowed for the carrying out of 2D and 3D seismic acquisition in the Cebu-Bohol Straits for SC51. The Company was acknowledged by all parties to have fully complied with all permitting requirements before and during the survey.

In a decision issued by the court presiding over the case on August 15, 2008, the petition was dismissed for lack of merit as it is violative of the applicable law and settled jurisprudence. The Petitioners filed an appeal before the Cebu City Court of Appeals to the decision of the lower court. On July 29, 2009, the Court of Appeals dismissed the petition for lack of jurisdiction over the case.

### Contingent Recourse Commitments

The Group, through Colag UK and Colag BVI, shall provide loans up to a maximum amount of USD 12,470,000 as Contingent Recourse commitments and Sponsor Equity Completion Support commitments to the financing party of the Facility Agreement between GPC and a foreign bank. As of June 30, 2009, the Group has provided USD 24,658,935.

## 21. Commitments

| | Economic Entity | | Parent Entity | |
|---|---|---|---|---|
| | 2009 $ | 2008 $ | 2009 $ | 2008 $ |
| **a) Exploration expenditure**<br>**Committed expenditures in accordance with farm-in agreements.** | | | | |
| No longer than 1 year | 5,133,538 | 3,960,000 | 2,848,475 | - |
| Longer than 1 year and no longer than 5 years | 33,548,708 | - | - | - |
| Longer than 5 years | 3,727,634 | - | - | - |
| | 42,409,880 | 3,960,000 | 2,848,475 | - |

| | Economic Entity | | Parent Entity | |
|---|---|---|---|---|
| | 2009 $ | 2008 $ | 2009 $ | 2008 $ |
| **b) Non-cancellable operating leases**<br>**The Group leases corporate offices under non-cancellable operating leases expiring with 3 years.**<br>**The leases have varying terms, escalation terms and renewal rights. On renewal, the terms of the leases may be renegotiated.** | | | | |
| No longer than 1 year | 274,112 | - | 274,112 | - |
| Longer than 1 year and no longer than 5 years | 680,197 | - | 680,197 | - |
| Longer than 5 years | - | - | - | - |
| | 954,309 | - | 954,309 | - |

## 22. Related Party Transactions

Transactions between related parties are on normal commercial terms and conditions no more favourable than those available to other parties unless otherwise stated.

| | Economic Entity | | Parent Entity | |
|---|---|---|---|---|
| | 2009 $ | 2008 $ | 2009 $ | 2008 $ |
| **Key Management Personnel** | | | | |
| Consulting fees paid to Dormley Pty Ltd, a company in which Dr Poll is a Director. | 137,500 | 137,500 | 137,500 | 137,500 |
| Share based payments (ordinary shares issued) to Dormley Pty Ltd, a company in which Dr Poll is a Director, for the facilitation of the investment in the Santa Rosa project in Argentina. | 150,000 | - | 150,000 | - |
| Rent paid to Zadnik Holdings Pty Ltd, a company in which Mr Zadnik is a Director, for the provision of office space. | - | 58,764 | - | 58,764 |
| Consulting fees paid to Grange Consulting Group Pty Ltd, a company in which Mr Macliver is a Director, for the provision of corporate advisory, company secretarial and associated services. | 204,750 | 159,712 | 204,750 | 159,712 |
| Consulting and placement fees paid to Max Capital Pty Ltd, a company in which Mr Macliver is a Director, for the provision of capital raising services. | 404,910 | 733,425 | 404,910 | 733,425 |
| Share based payments (options issued) to Max Capital Pty Ltd for consulting and placement fees, a company in which Mr Macliver is a Director, for the provision of capital raising services. | 11,388 | - | 11,388 | - |
| Interest paid on loans from Directors (Messrs: Mr Crabb, Mr Macliver, Mr Jetter and Mr Poll). The total loans advanced from the Directors to the company were $1,530,000 and are fully repaid at 30 June 2009. Per the terms of the loan agreement interest was payable at 12% per annum. The terms of the loan were approved by the Board and considered commercial and on an arms length basis. | 26,051 | - | 26,051 | - |
| Advances to GPC, amounts to USD9,000 as at 30 June 2008. The advances are due and payable upon commercial production of GPC's exploration licences. | - | 9,360 | - | - |
| Outstanding loans receivable from GPC amounting to USD31,972,104 as at 30 June 2009. The loan bears interest of 3% above LIBOR rate, compounded annually, and is repayable within 5 years from the date of the initial loan. Refer note 10 for further information. | 39,726,769 | 15,814,075 | - | - |

# NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

## 23. Business Combination

On 18 May 2009, Otto Energy (Europe) Limited, a wholly owned subsidiary of Otto Energy Limited, acquired 100% of the issued capital of Otto Energy (Italy) S.r.L (formerly Sidelia 4 S.r.L).

Since acquisition Otto Energy (Italy) S.r.L has incurred $11,394,795 in net losses for the Group for the period 18 May 2009 to 30 June 2009 which is represented by the impairment write-down of the capitalised exploration.

Details of the net assets acquired and goodwill are as follows:

| Purchase Consideration | $ |
|---|---|
| -Cash Paid | 20,822 |
| Total purchase consideration | 20,822 |
| Fair Value of net identifiable assets acquired (refer below) | 20,822 |
| Goodwill | - |

| The assets and liabilities arising from the acquisition are as follows: | Carrying Amount $ | Fair Value $ |
|---|---|---|
| Cash and cash equivalents | 20,723 | 20,723 |
| Other receivables | 117 | 117 |
| Payables | (18) | (18) |
| Intangibles-exploration expenses | 3,690 | - |
| Net identifiable assets acquired | 24,512 | 20,822 |

| | 2009 |
|---|---|
| Outflow of cash to acquire controlled entities, net cash acquired | |
| Cash consideration | 20,822 |
| Less: Balances acquired | (20,723) |
| Cash paid on acquisition | 99 |

### Prior Year Business Combinations: 2008

On 14 December 2007, NorAsian Energy Limited, a wholly owned subsidiary of Otto Energy Limited, acquired 100% of the issued capital of Colag BVI Limited (formerly Cape Energy Philippines SA) and Colag UK Limited (formerly Team Oil Limited). Otto acquired the two single asset companies; Colag UK Limited and Colag BVI Limited, who each owned a 15.69% interest in Galoc Production Company W.L.L ("GPC"). At the completion of the acquisition Otto had a 31.38% shareholding in GPC which holds a 58.29% working interest in the Galoc Oil Field. Otto has thereby acquired an 18.28% indirect interest in the Galoc Oil Field development project in the Philippines. GPC is the operator of the Galoc Oil Field development project in SC14c, offshore Philippines.

The acquired businesses Colag UK Limited and Colag BVI Limited have contributed AUD $464,635 in revenues and AUD $412,452 in profits to the net profit and loss of the Group for the period from 14 December 2007 to 30 June 2008.

Details of the net assets acquired and goodwill are as follows:

| Purchase Consideration | $ |
|---|---|
| -Cash Paid | 58,515,913 |
| -Non cash consideration – equity issued | 2,062,000 |
| Total purchase consideration | 60,577,913 |
| | |
| Fair Value of net identifiable assets acquired (refer below) | 20,961,045 |
| Goodwill at acquisition date 14 December 2007 | 39,616,868 |
| Foreign exchange movement | (4,191,827) |
| Goodwill at 30 June 2008 (refer Note 11 (b)) | 35,425,041 |

| The assets and liabilities arising from the acquisition are as follows: | Carrying Amount $ | Fair Value $ |
|---|---|---|
| Cash and cash equivalents | - | - |
| Deposits and loans receivable | 21,101,161 | 21,101,161 |
| Payables | (140,116) | (140,116) |
| Investment in associate | - | - |
| Net identifiable assets acquired | 20,961,045 | 20,961,045 |

| The assets and liabilities arising from the acquisition are as follows: | 2008 $ |
|---|---|
| Outflow of cash to acquire controlled entities, net cash acquired | |
| Cash consideration | 58,515,913 |
| Less: Balances acquired | - |
| Cash paid on acquisition | 58,515,913 |

## 24. Controlled Entities

| | Country of Incorporation | Percentage Owned (%)* 2009 | 2008 |
|---|---|---|---|
| **PARENT ENTITY:** | | | |
| Otto Energy Limited | Australia | 100 | 100 |
| **ULTIMATE PARENT ENTITY:** | | | |
| Otto Energy Limited | Australia | 100 | 100 |
| **SUBSIDIARIES OF OTTO ENERGY LTD:** | | | |
| Edirne Energy Ltd | Turkey | 100 | 100 |
| Ottoman (Philippines) Pty Ltd | Australia | 100 | 100 |
| NorAsian Energy Limited | Bermuda | 100 | 100 |
| NorAsian Energy Phils. Inc. | Philippines | 100 | 100 |
| Colag UK Limited | United Kingdom | 100 | 100 |
| Colag (BVI) Limited | British Virgin Islands | 100 | 100 |
| Otto Energy (Europe) Limited | United Kingdom | 100 | - |
| Otto Energy (Italy) S.r.L *(formerly Sidelia 4 S.r.L)* | Italy | 100 | - |
| **ASSOCIATE OF OTTO ENERGY LTD:** | | | |
| Galoc Production Company W.L.L | Bahrain | 31.38 | 31.38 |
| Cynthia Holdings Limited | British Virgin Islands | 32.48 | - |

*The proportion of ownership interest is equal to the proportion of voting power held

# NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

## 25. Investments in Associates

| | Economic Entity 2009 $ | Economic Entity 2008 $ |
|---|---|---|
| a) Movements in carrying amounts | | |
| Carrying amount at the beginning of the financial year | - | - |
| Investment acquired | 2,266,680 | - |
| Impairment expense | (2,266,680) | |
| Revaluation | - | 843,611 |
| Share of profits/(losses) after income tax | - | (843,611) |
| Dividends received/receivable | - | - |
| Carrying amount at the end of the financial year | - | - |

b) Summarised financial information of associates

The Group's share of the results of its principal associate and its aggregated assets (including goodwill) and liabilities are as follows:

| | Ownership Interest % | Group's Share of: Assets $ | Liabilities $ | Revenues $ | Net Profit/(Loss) $ |
|---|---|---|---|---|---|
| **2009** | | | | | |
| Galoc Production Company W.L.L | 31.38 | 39,938,750 | 33,585,027 | 1,304,918 | 107,106 |
| Cynthia Holdings Limited | 32.48 | 1,902,680 | - | - | - |
| **2008** | | | | | |
| Galoc Production Company W.L.L | 31.38 | 36,214,303 | 37,493,935 | - | (988,382) |

| | Economic Entity 2009 $ | Economic Entity 2008 $ |
|---|---|---|
| c) Fair value of investments in associate | | |
| Galoc Production Company W.L.L | - | - |
| Cynthia Holdings Limited | - | - |
| d) Contingent liabilities of associates | | |
| Share of contingent liabilities incurred jointly with other investors | | |
| Contingent liabilities relating to liabilities of the associate for which the Company is severally liable. In 2009 this is no longer applicable as the Company's share of the project finance debt facility relating to it's investment in Galoc Production Company W.L.L have been fully repaid during the year. | - | 9,583,763 |
| | - | 9,583,763 |

## 26. Events After the Balance Sheet Date

On 9 July 2009, the company announced that GPC has entered into an agreement to acquire an additional 1.55% working interest in the Galoc oil field. The acquisition increases GPC's working interest in the Galoc oil field from 58.29% to 59.84% and as a result the company's indirect interest in GPC will increase by 0.49% to 18.78%. The acquisition follows the decision by GPC, to acquire the interests of minority partners of the joint venture. The cost to the company for its share will be approximately $500,000 (USD 390,170) which will be paid via proceeds from Galoc production.

## 27. Cash Flow Information

| | Economic Entity 2009 $ | Economic Entity 2008 $ | Parent Entity 2009 $ | Parent Entity 2008 $ |
|---|---|---|---|---|
| **a) Reconciliation of Cash Flow from Operations with Loss after Income Tax** | | | | |
| Loss after income tax | (58,436,953) | (10,699,873) | (53,319,494) | (12,154,336) |
| Non-cash flows in loss | | | | |
| - Depreciation | 175,392 | 72,535 | 115,722 | 59,539 |
| - Impairment expense | 49,431,593 | - | 59,128,084 | - |
| - Exploration costs | (12,839,394) | (13,219,662) | (53,501) | (4,045,623) |
| - Unrealised foreign exchange gain / (loss) | 481,389 | 6,399,184 | (13,313,669) | 6,399,184 |
| - Share options expensed | - | 2,553,245 | - | - |
| - Share based payments | 1,724,501 | - | 1,724,501 | 2,268,575 |
| -Provision for write down / (write back) of receivables | - | - | - | (441,722) |
| - Share of net loss of associate | - | 843,611 | - | - |
| - Write off exploration expenditures capitalised | 194,836 | 26,861 | 64,091 | - |
| - Profit on sale of licence interests | - | (3,324,169) | - | - |
| Changes in assets and liabilities, net of the effects of purchase and disposal subsidiaries | | | | |
| - (Increase)/decrease in other receivables | 1,324,608 | (340,165) | (195,686) | (129,589) |
| - (Increase)/decrease in prepayments | 46,527 | (33,930) | 51,084 | (25,837) |
| - Increase/(decrease) in trade payables and accruals | 505,849 | 266,288 | 531,464 | 263,309 |
| Net cash outflow from operations | (17,391,652) | (17,456,075) | (5,267,404) | (7,806,500) |

| | Economic Entity 2009 $ | Economic Entity 2008 $ | Parent Entity 2009 $ | Parent Entity 2008 $ |
|---|---|---|---|---|
| **b) Non Cash investing and financing activities** | | | | |
| 1. Issue of Otto securities as the non cash component of the purchase consideration paid to acquire subsidiaries. | | | | |
| - 2,000,000 ordinary shares at deemed price of 31.9 cents each | - | 638,000 | - | 638,000 |
| - 8,000,000 options expiring at 30 November 2009 at deemed price of 18 cents each | - | 1,424,000 | - | 1,424,000 |
| 2. Stage one non cash consideration for MEPS right termination through issue of Otto securities. | 4,575,000 | - | 4,575,000 | - |
| 3.Issue of Otto securities as the non cash component of the investment in associate. | 150,000 | - | 150,000 | - |
| 4. Conversion of shareholder loans to Otto securities at deemed price of $0.05 each. | 10,220,843 | - | 10,220,843 | - |
| 5. Conversion of director loans to Otto securities at deemed price of $0.05 each. | 346,281 | - | 346,581 | - |
| | 15,292,124 | 2,062,000 | 15,292,124 | 2,062,000 |

# NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

## 28. Earnings Per Share

| | Economic Entity | |
|---|---|---|
| | 2009 $ | 2008 $ |
| a) Reconciliation of earnings to profit or loss | | |
| - Loss | (57,348,777) | (10,699,873) |
| - Earnings used to calculate basic EPS | (57,348,777) | (10,699,873) |
| b) Weighted average number of ordinary shares outstanding during the year used in calculating basic EPS | No. 569,942,406 | No. 341,622,631 |

The Company's potential ordinary shares, being it's options granted, are not considered dilutive as the conversion of these options would result in a decrease in the net loss per share.

## 29. Share-Based Payments

### (a) Employee share option plan

The establishment of the Employee Share Option Plan was approved by general meeting. The Employee Option Plan is designed to provide long term incentives for senior managers and employees to deliver long term shareholder returns. Under the plan, participants are granted options based on the business meeting certain growth and acquisition targets. Participation in the plan is at the Board's discretion and no individual has a contractual right to participate in the plan or to receive any guaranteed benefits.

An option may only be exercised after that option has vested and any other conditions imposed by the Board on exercise are satisfied. Options are granted under the plan for no consideration. Options granted under the plan carry no dividend or voting rights.

When exercisable, shares allotted pursuant to the exercise of options will be allotted following receipt of all the relevant documents and payments and will rank equally with all other shares. The exercise price of options is based on the weighted average price at which the Company's shares are traded on the Australian Securities Exchange during the five trading days immediately before the options are granted.

| Grant Date | Expiry Date | Exercise Price | Balance at start of the year | Granted during the year | Exercised during the year | Forfeited during the year | Balance at end of the year | Vested and exercisable at end of the year |
|---|---|---|---|---|---|---|---|---|
| | | | Number | Number | Number | Number | Number | Number |
| 08 May 2007 | 29 May 2011 | $0.20 | 4,333,400 | - | (250,000) | - | 4,083,400 | 4,083,400 |
| 08 May 2007 | 29 May 2011 | $0.30 | 4,333,300 | - | - | - | 4,333,300 | 4,333,300 |
| 08 May 2007 | 29 May 2011 | $0.40 | 3,333,300 | - | - | - | 3,333,300 | - |
| 17 Dec 2007 | 17 Dec 2010 | $0.30 | 8,250,000 | - | - | - | 8,250,000 | 8,250,000 |
| 25 Jan 2008 | 25 Jan 2011 | $0.30 | 11,000,000 | - | - | - | 11,000,000 | 11,000,000 |
| 10 Apr 2008 | 10 Apr 2012 | $0.35 | 2,000,000 | - | - | - | 2,000,000 | - |
| 01 Aug 2008 | 01 Aug 2012 | $0.60 | - | 2,500,000 | - | - | 2,500,000 | - |
| Total | | | 33,250,000 | 2,500,000 | (250,000) | - | 35,500,000 | 27,666,700 |
| Weighted average exercise price | | | $0.30 | $0.60 | $0.20 | - | $0.32 | $0.29 |

No options expired during the periods covered by the above tables. The weighted average remaining contractual life of share options outstanding at the end of the year was 2 years.

The above amounts representing options granted as part of remuneration are calculated in accordance with AASB 2 Share Based Payments. AASB 2 requires that the expense associated with a share based payment is calculated at issue date and then subsequently amortised over the option vesting period. Once the share based payment has been calculated it is not able to be adjusted. As such the option expense noted above is based upon historical calculations made during a time when the share price of the company was significantly higher than its current level. Due to the impact of the global financial crisis it is management's belief that the true intrinsic value of the options issued to Directors and Other Key Management Personnel is significantly lower than the number presented above.

### (b) Options: Consultants and Advisors

| Grant Date | Expiry Date | Exercise Price | Balance at start of the year | Granted during the year | Exercised during the year | Forfeited during the year | Balance at end of the year | Vested and exercisable at end of the year |
|---|---|---|---|---|---|---|---|---|
| | | | Number | Number | Number | Number | Number | Number |
| 14 Dec 2007 | 30 Nov 2009 | $0.34 | 4,000,000 | - | - | - | 4,000,000 | 4,000,000 |
| 14 Dec 2007 | 30 Nov 2009 | $0.34 | 4,000,000 | - | - | - | 4,000,000 | 4,000,000 |
| 15 Dec 2008 | 15 Dec 2010 | $0.60 | - | 2,000,000 | - | - | 2,000,000 | 2,000,000 |
| 23 Jun 2009 | 03 Jul 2010 | $0.05 | - | 61,855,350 | - | - | 61,855,350 | 61,855,350 |
| Total | | | 8,000,000 | 63,855,350 | - | - | 71,855,350 | 71,855,350 |
| Weighted average exercise price | | | $0.34 | $0.07 | - | - | $0.10 | $0.10 |

#### Fair value of options granted

The assessed fair value at grant date of options granted on the 23 June 2009 was $0.001 per option. The fair value was calculated in accordance with AASB 2 Share-Based Payments in reference to the fair value of services rendered. The services received by the Company for capital raising fees were fair valued based on historical fees and market rates of 5% of total capital raised.

The assessed fair value at grant date of options granted on 1 August 2008 was $0.14 per option and $0.01 for options issued on the 15 December 2008. The fair value at grant date is independently determined using a Black Scholes option pricing model that takes into account the exercise price, the term of the option, the impact of dilution, the share price at grant date and expected price volatility of the underlying share, the expected dividend yield and the risk free interest rate for the term of the option.

Options are granted for no consideration and vest based on conditions determined by the board at general meeting. Vested options issued on the 1 August 2008 are exercisable up to 1 August 2012 after vesting and;

| | |
|---|---|
| Exercise price | $0.60 |
| Term of the option | 4 years |
| Underlying share price | $0.34 |
| Standard deviation of returns | 65.0% |
| Risk free interest rate | 6.06% |

# NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

## 29. Share-Based Payments (Cont'd)

### (b) Options: Consultants and Advisors (Cont'd)

Options are granted for no consideration and vest based on conditions determined by the board at general meeting. Vested options issued on the 15 December 2008 are exercisable up to 15 December 2010 after vesting and;

| | |
|---|---|
| Exercise price | $0.60 |
| Term of the option | 2 years |
| Underlying share price | $0.13 |
| Standard deviation of returns | 65% |
| Risk free interest rate | 4.35% |

The expected price volatility is based on the historic volatility at the time of issue (based on the remaining life of the options), adjusted for any expected changes to future volatility due to publicly available information.

### (c) Expenses arising from share based payment transactions

| | Consolidated | | Parent | |
|---|---|---|---|---|
| | 2009 $ | 2008 $ | 2009 $ | 2008 $ |
| Options issued under employee option plan | 1,724,502 | 2,553,245 | 1,724,502 | 2,553,245 |
| Options issued to consultants and advisors[(i)] | 83,019 | - | 83,019 | - |
| | 1,807,521 | 2,553,245 | 1,807,521 | 2,553,245 |

(i) The options were issued to consultants and advisors for sub-underwriting fees in relation to the capital raising during the year and were measured with reference to the fair value of the services rendered. The expense arising from the share based payment was recognised through equity as a share issue cost.

## 30. New Accounting Standards and Interpretations

The following Australian Accounting Standards have been issued or amended and are applicable to the parent and consolidated entity but are not yet effective. They have not been adopted in preparation of the financial statements at reporting date.

These are outlined in the table below.

| Reference | Title | Summary | Application date of standard | Impact on Company Financial Report | Application date for Company |
|---|---|---|---|---|---|
| AASB 8 | Operating Segments | New standard replacing disclosure requirements of AASB 114. | 1 January 2009 | As this is a disclosure standard only there will be no impact on the amounts disclosed. The company does not currently required to report on segments. | 1 July 2009 |
| AASB 123 | Borrowing Costs | Revised standard requiring the capitalisation of all borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset. | 1 January 2009 | As it is the Company's current policy to capitalise interest on qualifying assets, there will be no impact on the Company's financial statements. | 1 July 2009 |
| AASB 101 | *Presentation of Financial Statements* | Amendments to presentation and naming of the financial statements. | Annual reporting periods commencing on or after 1 January 2009 | As this is a disclosure standard only, there will be no impact on amounts recognised in the financial statements. However, there will be various changes to the way financial statements are presented and various changes to names of individual financial statements. | 1 July 2009 |
| Amendments to IFRS 7 | *Amendments to IFRS 7 Financial Instruments: Disclosures* | Requires additional disclosures about financial instruments fair values and liquidity risk. | Periods commencing on or after 1 January 2009 | As this is a disclosure standard only, there will be no impact on amounts recognised in the financial statements. However, various additional disclosures will be required about fair values of financial instruments and the entity's liquidity risk. No comparative disclosures are required in the first year that these amendments are applied. | 1 July 2009 |
| AASB 127 | *Consolidated and Separate Financial Statements* | The revised standard clarifies that changes in ownership interest which result in control being retained are accounted for within equity as transactions with owners. Losses will be attributed to the non-controlling interest even if this results in a debit balance for the non-controlling interest. Investments retained where there has been a loss of control will be recognised at fair value at date of sale. | Periods commencing on or after 1 July 2009 | As there is no requirement to retrospectively restate the effect of these revisions, there is unlikely to be any impact on the financial statements when this revised standard is first adopted. | 1 July 2009 |

# NOTES TO THE FINANCIAL STATEMENTS (Cont'd)

## 30. New Accounting Standards and Interpretations (Cont'd)

| Reference | Title | Summary | Application date of standard | Impact on Company Financial Report | Application date for Company |
|---|---|---|---|---|---|
| AASB 3 | Business Combinations | Released as part of long term international convergence project between IASB and FASB. The revised standard introduces more detailed guidance on accounting for step acquisitions, adjustments to contingent consideration, assets acquired that the purchaser does not intend to use, reacquired rights and share-based payments as part of purchase consideration. Also, all acquisition costs will have to be expensed instead of being recognised as part of goodwill. | Periods commencing on or after 1 July 2009 | As there is no requirement to retrospectively restate comparative amounts for business combinations undertaken before this date, there is unlikely to be any impact on the financial statements when this revised standard is first adopted.<br><br>However, due to the nature of some of the changes in the revised standard, business combinations that the entity undertakes after this date may in future impact negatively on the results of the entity. For example, acquisition costs will have to be expensed instead of being recognised as part of goodwill.<br><br>Specific changes in respect of step acquisitions and sell downs may introduce situations whereby adopting the revised standard may improve profitability. | 1 July 2009 |
| AASB 2008-1 | *Amendments to AASB 2 – Share-based Payments – Vesting Conditions and Cancellations* | The definition of vesting conditions has changed and the accounting treatment clarified for cancellations to share-based payment arrangements by the counterparty. This is to ensure that conditions other than performance conditions do not result in a 'true up' of the share-based payment expense and are treated in a manner similar to market conditions. | Periods commencing on or after 1 January 2009 | To date the entity has not issued any options to employees that include non-vesting conditions and as such there will be no impact on the financial statements when this revised standard is adopted for the first time. | 1 July 2009 |
| AASB 2008-7 | *Amendments to Australian Accounting Standards – Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate [AASB 1, AASB 118, AASB 121, AASB 127 and AASB 136]* | Removal of the definition of the "cost method" in AASB 127, meaning that pre and post-acquisition dividends no longer need to be differentiated and all dividends are to be recognised as revenue. However, whenever a dividend is received from a subsidiary, associate or jointly controlled entity, an impairment test will be required under AASB 136 where there is an indicator for impairment, i.e. where: | Periods commencing on or after 1 January 2009 | There will be no impact as these requirements are only required to be applied prospectively for periods commencing on or after 1 January 2009. However, any pre-acquisition dividends received after this date may result in additional impairment charges on investments in subsidiaries, associates and jointly controlled entities. This is because such amounts would previously have been written off directly against the cost of the investment, whereas in future they will be recognised as revenue which may result in the investment being stated at an amount exceeding recoverable amount. | 1 July 2009 |
| AASB 136 | *Impairment of Assets* | Additional disclosure requirements about discounted cash flow assumptions used for the fair value less costs to sell method. | Periods commencing on or after 1 January 2009 | There will be no financial impact when these amendments are first adopted because these amendments relate to additional disclosure requirements only. | 1 July 2009 |

All other pending standards issued between the previous annual report and the current reporting dates have no application to either parent or consolidated entity.

## 31. Company Details

**The registered office of the Company is:**

945 Wellington Street
West Perth WA 6005
Australia

Tel: (08) 9322 7600

Fax: (08) 9322 7602

**The principal places of business are:**

Australian Head Office
32 Delhi Street
West Perth WA 6008
Australia

Tel: (08) 6467 8800

Fax: (08) 6467 8801

**Philippines Office**

NorAsian Energy Limited
4th Floor F&M Lopez Building II
109 Carlos Palanca Street
Legaspi Village 1229 Makati City
Republic of Philippines

**Turkish Representative Office**

C/- Petrako Petroleum Trade & Consulting Inc.
Koza Cad.5 Sok 4/6
Cankaya, 06700, GOP Ankara,
Gaziosmanpasa
Republic of Turkey

# DIRECTORS' DECLARATION

In the Directors' opinion:

(a) the financial statements, comprising the income statement, balance sheet, cash flow statement, statement of recognised income and expense, accompanying notes, are in accordance with the Corporations Act 2001, and:

(i) comply with Accounting Standards, the Corporations Regulations 2001 and other mandatory professional reporting requirements; and

(ii) give a true and fair view of the financial position as at 30 June 2009 and of the performance for the year ended on that date of the company, and the consolidated entity.

(b) there are reasonable grounds to believe that the company will be able to pay its debts as and when they become due and payable; and

(c) The remuneration disclosures included in pages 36 to 45 of the directors' report (as part of the audited Remuneration Report), for the year ended 30 June 2009, comply with section 300A of the *Corporations Act* 2001.

(d) The Directors have been given the declarations required by section 295A.

This declaration is made in accordance with a resolution of the Board of Directors and is signed for and on behalf of the directors by;

I Macliver

**Mr I Macliver**

**Director**

**23 September 2009**

# INDEPENDENT AUDIT REPORT

**Independent Audit Report to the Members of Otto Energy Limited**

BDO Kendalls

BDO Kendalls Audit & Assurance (WA) Pty Ltd
128 Hay Street
SUBIACO WA 6008
PO Box 700
WEST PERTH WA 6872
Phone 61 8 9380 8400
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ABN 79 112 284 787

**INDEPENDENT AUDITOR'S REPORT**
**TO THE MEMBERS OF OTTO ENERGY LIMITED**

We have audited the accompanying financial report of Otto Energy Limited, which comprises the balance sheet as at 30 June 2009, and the income statement, statement of changes in equity and cash flow statement for the year ended on that date, a summary of significant accounting policies, other explanatory notes and the directors' declaration of the entity comprising the disclosing entity 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 and fair presentation of the financial report in accordance with Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Act 2001*. This responsibility includes establishing and maintaining internal controls relevant to the preparation and fair presentation of the financial report that is free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances. In Note 2, the directors also state, in accordance with Accounting Standard AASB101 Presentation of Financial Statements, that compliance with the Australian equivalents to International Financial Reporting Standards ensures that the financial report, comprising the financial statements and notes, complies with International Financial Reporting Standards.

**Auditor's Responsibility**

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation 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* would be in the same terms if it had been given to the directors at the time that this auditor's report was made.

# INDEPENDENT AUDIT REPORT (Cont'd)

## Independent Audit Report to the Members of Otto Energy Limited (Cont'd)

BDO Kendalls

**Auditor's Opinion**

In our opinion:

(a) the financial report of Otto Energy Limited is in accordance with the *Corporations Act 2001*, including:
  (i) giving a true and fair view of the company's and consolidated entity's financial position as at 30 June 2009 and of their performance for the year ended on that date; and
  (ii) complying with Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Regulations 2001*; and

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

**Material Uncertainty Regarding Continuation as a Going Concern**

Without qualification to the above, we draw attention to Note 1 in the financial report which indicates that Otto Energy Limited incurred a net loss of $57,348,777 during the year ended 30 June 2009. The company is dependant upon cash flow generated from production of the Galoc Oil Field and repatriation of those revenues to Otto Energy Limited. If this does not occur the company may be required to seek additional funding through debt, equity or other means to continue its activities. These conditions, along with other matters as set forth in Note 1, indicate the existence of a material uncertainty which may cast significant doubt about the consolidated entity's ability to continue as a going concern and whether it will be able to realise its assets and extinguish its liabilities in the normal course of business and at the amounts stated in the financial report.

**Report on the Remuneration Report**

We have audited the Remuneration Report included within the Directors' Report for the year ended 30 June 2009. The directors of the company are responsible for the preparation and presentation of the Remuneration Report in accordance with section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with Australian Auditing Standards.

**Auditor's Opinion**

In our opinion, the Remuneration Report of Otto Energy Limited for the year ended 30 June 2009, complies with section 300A of the *Corporations Act 2001*.

**BDO Kendalls Audit and Assurance (WA) Pty Ltd**

BDO Kendalls

**Brad McVeigh**
Director

Dated this 23rd day of September 2009
Perth, Western Australia

# CORPORATE GOVERNANCE STATEMENT

In fulfilling its obligations and responsibilities to its various stakeholders, the Board is a strong advocate of corporate governance. This statement outlines the principal corporate governance procedures of Otto Energy Limited (Otto Energy or the Company). The Board of Directors supports a system of corporate governance to ensure that the management of Otto Energy is conducted to maximise shareholder wealth in a proper and ethical manner.

### ASX Corporate Governance Council Recommendations

The Board has adopted corporate governance policies and practises consistent with the ASX Corporate Governance Council's "Corporate Governance Principles and Recommendations 2nd edition" ("Recommendations") where considered appropriate for a company of Otto Energy's size and nature. Such policies include, but are not limited to the Board Charter, Board Committee Charters, Code of Conduct, Trading in Securities, Continuous Disclosure, Shareholder Communication and Risk Management Policies. Further details in respect to the Company's corporate governance practises are summarised below and copies of Company's corporate governance policies are available of the Company's web site at www.ottoenergy.com.

The Board sets out below its "if not why not" report in relation to matters of corporate governance where the Company's practise departs from the Recommendations. All Recommendations have been applied for the financial year ended 30 June 2009 unless set out below.

Recommendation 2.4 requires listed entities to establish a nomination committee. During the year, the Company did not have a separately established nomination committee. Given the current size of the Board, the Board considers that this function is efficiently achieved with full Board support, in accordance with the guidelines set out in the Board's Charter.

Recommendation 4.2 requires the audit committee be structured such that it consists of: only non-executive directors, a majority of independent directors, is chaired by and independent chair, who is not the chair of the board and have at least three members. The Company's audit committee during the year comprised two Non-executive, independent Directors, Messrs Ian Macliver and Rick Crabb. Given the current size and technical expertise of the Board an audit committee comprising only two Directors was considered appropriate for the Company.

Recommendation 8.1 states that the board should establish a remuneration committee. During the year, the Company did not have a separately established remuneration committee. Given the number of Directors on the Board and the size of the Company, the Board considers that this function can efficiently be performed by the full Board.

In relation to the above, the Board believes it has implemented suitable practices and procedures in respect of Corporate Governance considering the size of the Board and the size and maturity of the Company. The Board wishes to acknowledge that nothing has come to its attention which would lead the Board to conclude that its current practices and procedures are not appropriate for an organisation of this size and maturity.

# CORPORATE GOVERNANCE STATEMENT (Cont'd)

**Roles of the Board and Management**

The Board considers that the essential responsibilities of the Directors are to oversee Otto's activities for the benefit of its shareholders, employees and other stakeholders and to protect and enhance shareholder value.

The Board has a Charter, which clearly establishes the relationship between the Board and management and describes their functions and responsibilities.

The key responsibilities of the Board include:

- contributing to the development of and approving corporate strategy;
- appoint and review the performance of the Managing Director/Chief Executive Officer;
- reviewing and approving business plans, the annual budget and financial plans including available resources and major capital expenditure initiatives;
- arrange for effective budgeting and financial supervision;
- ensure that effective and appropriate reporting systems in place will, in particular, assure the Board that financial, operational, compliance and risk management controls function adequately;
- ensure that appropriate audit arrangements are in place; and
- reporting to shareholders.

**Board Structure**

The composition of the Board shall be determined in accordance with the following principles and guidelines:

- the Board shall comprise at least 3 Directors, increasing where additional expertise is considered desirable in certain areas;
- the Chairman should be non executive;
- the Board should not comprise a majority of Executive Directors; and
- Directors should bring characteristics which allow a mix of qualifications, skills and experience.

The terms and conditions of the appointment and retirement of Directors are set out in a letter of appointment which covers remuneration, expectations, terms, the procedures for dealing with conflicts of interest and the availability of independent professional advice.

The chairman reviews the performance of all Directors each year.

**Director Independence**

Directors are expected to bring independent views and judgement to the Board's deliberations. In response to the ASX Principles, the Board Charter requires the Board to include a majority of non executive independent directors and a non executive independent chairman.

In considering whether a Director is independent, the Board has had regard to the independence criteria outlined in Recommendation 2.1 and other facts, information and circumstances that the Board considers to be material. Of the five non executive Directors, four of the non-executive Directors are regarded as independent.

Dr Jaap Poll is not considered to be an independent director as he does not satisfy item 2 of the relationships affecting a Directors independence outlined in Box 2.1 of the Recommendations as within the last three years Dr Poll was employed in an executive capacity as Managing Director of the Company.

It is noted that Mr Macliver is a principal of Grange Consulting Group and Max Capital Pty Ltd, which provides company secretarial, corporate advisory and financial support services to the Company. In considering whether Mr Macliver is independent, the Board took into account the principal amount of fees paid to Grange Consulting Group and Max Capital which is not considered material. It is noted that Mr Macliver did not vote on any resolution in respect of the services provided and the fees payable to Grange Consulting Group and/or Max Capital. In addition, there are no other aspects of the relationship with Grange Consulting Group and/or Max Capital that could materially interfere with or be likely to interfere with the exercise by Mr Macliver of unfettered and independent judgement as a Director.

**Meetings of the Board**

The Board meets at least six times a year to consider the business of Otto Energy, its financial performance and other operational issues.

**Retirement and Re-election**

The Constitution of the Company requires one third of the Directors to retire from office at each Annual General Meeting. Directors who have been appointed by the Board are required to retire from office at the next Annual General Meeting and are not taken into account in determining the number of Directors to retire at that Annual General Meeting. Directors cannot hold office for a period in excess of three years or later than the third Annual General Meeting following their appointment without submitting themselves for re-election (excluding the Managing Director). Retiring Directors are eligible for re-election by shareholders.

When a vacancy exists, for whatever reason, or where it is considered that the Board would benefit from the services of a new Director with particular skills, the Board will select appropriate candidates with relevant qualifications, skills and experience. External advisers may be used to assist in such a process. The Board will then appoint the most suitable candidate who must stand for election at the next general meeting of shareholders.

**Nomination and appointment of new Directors**

Recommendations of candidates for new Directors are made by the Board as a whole.

**Review of Performance**

The Board reviews its performance and composition on an annual basis to ensure that it has the appropriate mix of expertise and experience. Given the size and nature of the Company's activities the Board reviews the performance of Directors and the composition of the Board, at regular intervals during the year.

**Directors' Remuneration**

The remuneration of Non-executive Directors is different to that of Executives. Executive Directors receive a salary and may receive other benefits.

Non-executive Directors receive a set fee per annum, in addition to their statutory superannuation entitlements, and are fully reimbursed for any out of pocket expenses necessarily incurred in carrying out their duties. When reviewing Director's fees the Board takes into account any changes in the size and scope of Otto Energy's activities.

The Board will review the remuneration and policies applicable to all Directors on an annual basis. Remuneration levels will be competitively set to attract the most qualified and experienced Directors and senior Executives. Where necessary the Board will obtain independent advice on the appropriateness of remuneration packages.

The structure and disclosure of the Company's remuneration policies for Directors are set out in the Directors Report.

# CORPORATE GOVERNANCE STATEMENT (Cont'd)

**Board Access to Information**

All Directors have unrestricted access to all employees of the Company and, subject to the law, access to all company records and information held by and employee/s and/or external advisers. The Board receives regular detailed financial and operational reports to enable it to carry out its duties.

Each Director may, with the prior written approval of the Chairman, obtain independent professional advice to assist the Director in the proper exercise of powers and discharge of duties as a Director or as a member of a Board Committee. The Company will reimburse the Director for the reasonable expense of obtaining that advice.

**Board Committees**

The Board, where appropriate, may establish a number of committees to assist in carrying out its responsibilities in an effective and efficient manner.

The Board has established an Audit Committee to assist the Board in the discharge of its responsibilities and is governed by the Audit Committee Charter, as approved by the Board.

**Audit Committee**

The Board has an Audit Committee. The Committee monitors internal control policies and procedures designed to safeguard Company assets and to maintain the integrity of financial reporting.

The role of the Committee is to provide a direct link between the Board and the external auditors.

It will also give the Board of Directors additional assurance regarding the quality and reliability of financial information prepared for use by the Board in determining policies or for inclusion in financial statements.

The responsibilities of the Audit Committee include:

- reviewing and reporting to the Board on the annual and half year financial reports, the financial section of quarterly reports and all other financial information published by the Company prior to release to members and other public forums;
- assisting the Board in reviewing the effectiveness of the organisation's internal control environment covering effectiveness and efficiency of operations, reliability of financial reporting, compliance with applicable laws and regulations and monitoring of corporate risk assessment processes;
- co-ordinating the audit with the external auditor including reviews of internal control measures;
- reviewing and approving any significant non-mandatory accounting policy change; and
- recommending to the Board the appointment, removal and remuneration of the external auditors, and review the terms of their engagement, the scope and quality of the audit and the auditor's independence, and consider if appropriate, the rotation of audit partners.

The Audit Committee will review the performance of the external auditors on an annual basis and meet with them at least twice during the year. Nomination of auditors will be at the discretion of the Committee.

The Audit Committee also meets with and receives reports from the external auditors concerning any matters which arise in connection with the performance of their respective roles, including the adequacy of internal controls.

The members of the Audit and Compliance Committee at the date of this report are Mr Ian Macliver (Chairman) and Mr Rick Crabb.

**Audit Process**

As part of the Company's commitment to safeguarding integrity in financial reporting, Otto Energy's accounts are subject to annual audit by an independent, professional auditor, who also reviews the half-yearly accounts. The Auditor attends and is available to answer questions at, the Company's annual general meetings.

**Auditor Independence**

The Company has implemented procedures to monitor the independence and competence of the Company's external auditors. Details of the amounts paid for both audit work and non-audit services are set out in this annual report.

The Board requires that adequate hand-over occurs in the year prior to rotation of an audit partner to ensure an efficient and effective audit under the new partner.

**Business Risks**

The Company is committed to the identification, monitoring and management of risks associated with its business activities and has embedded in its management and reporting systems a number of risk management controls. The Board is charged with implementing appropriate risk management systems within the Company.

The Board will monitor and receive advice on areas of operational and financial risk, and consider strategies for appropriate risk management arrangements.

Specific areas of risk identified initially and which will be regularly considered at Board meetings include operating risks, commodity price volatility and exchange rate risks, environmental risks, title risks, competition, statutory compliance and continuous disclosure obligations.

The Board has received the declaration in accordance with section 295A of the Corporations Act in respect to the financial accounts for the year ended 30 June 2009 which is founded on a sound system of risk management and internal controls and these systems are operating effectively in all material respects in relation to the financial reporting risks.

**Share Trading**

Under the Company's Share Trading Policy, all employees and Directors of the Company and its related companies are prohibited from trading in the Company's shares or other securities if they are in possession of "inside information". Subject to this condition and in light of the ASX's continuous disclosure requirements, trading can occur at any time but subject to conditions surrounding periods prior to the publication of financial results and disclosure documents.

In addition, in order to trade, employees and Directors must advise the Audit Committee of their intention to trade and must also have been advised by one of the Audit Committee Directors that there is no known reason to preclude them trading in the Company's shares or other securities.

# CORPORATE GOVERNANCE STATEMENT (Cont'd)

### Continuous Disclosure

The Company understands and respects that timely disclosure of price sensitive information is central to the efficient operation of the ASX securities market and has adopted a comprehensive policy covering announcements to the Australian Securities Exchange, prevention of selective or inadvertent disclosure, conduct of investor and analysts briefings, media communications, commenting on expected earnings, communications black-out periods and review of briefings and communications. The policy is reviewed periodically and updated as required.

The Company Secretary has responsibility for overseeing and coordinating disclosure of information to the Australian Securities Exchange. The Company Secretary also liaises with the Chairman in relation to continuous disclosure matters. The Chief Executive Officer is responsible for overseeing and coordinating disclosure of information to analysts, brokers and shareholders.

### Ethical Standards

All Directors, executives and employees are charged with the responsibility to act with the utmost integrity and objectivity, striving at all times to enhance the reputation and performance of the Company.

It is the Board's responsibility to ensure that all staff are aware of the Company's Code of Conduct and to ensure that any individual who does not adhere to these ideals is dealt with appropriately by executive management. Appropriate action may be counselling, disciplinary action or termination of employment.

The Board is responsible for setting the tone of legal, ethical and moral conduct to ensure that the Company is considered reputable by the industry and other outside entities. This involves considering the impact of the Company's decisions on the industry, colleagues and the general community.

### Communications with Shareholders

The Board aims to ensure that shareholders are kept informed of all major developments affecting Otto Energy. Information is communicated to shareholders through the distribution of annual reports; and by presentation to shareholders at the Annual General Meeting, which they are encouraged to attend.

In addition, all reports, including quarterly reports and releases made by Otto Energy throughout the year with respect to its activities are distributed widely via the Australian Securities Exchange and posted on the Company's website located at www.ottoenergy.com.

# ASX ADDITIONAL INFORMATION

Additional information required by the ASX Limited Listing Rules not disclosed elsewhere in this Annual Report is set out below.

## 1. SHAREHOLDINGS

The issued capital of the Company at 22 September 2009 is 1,070,184,721 ordinary fully paid shares. All ordinary shares carry one vote per share. There are no listed options.

| Ordinary Shares | No. of Holders | No. of Shares |
|---|---|---|
| 1 – 1,000 | 56 | 15,211 |
| 1,001 – 5,000 | 447 | 1,437,365 |
| 5,001 – 10,000 | 576 | 4,860,148 |
| 10,001 – 100,000 | 2,197 | 92,866,740 |
| 100,001 and over | 865 | 97,100,257 |
| | 4,141 | 1,070,184,721 |
| Number holding less than a marketable parcel size of 8,065 shares at $0.062 per share | 730 | 2,956,894 |
| **Shareholders by Location** | **No. of Holders** | **No. of Shares** |
| Australian holders | 3,839 | 788,690,867 |
| Overseas holders | 302 | 281,493,854 |
| | 4,141 | 1,070,184,721 |

## 2. TOP 20 SHAREHOLDERS AS AT 22 SEPTEMBER 2009

| | Registered Holders | No. of Shares Held | % Held |
|---|---|---|---|
| 1 | HSBC Custody Nominees (Australia) Ltd* | 220,952,181 | 20.65 |
| 2 | Santo Holding | 210,983,082 | 19.71 |
| 3 | ANZ Nominees Ltd | 44,289,453 | 4.14 |
| 4 | Citicorp Nominees Pty Ltd | 34,544,059 | 3.23 |
| 5 | JP Morgan Nominees Australia Ltd | 25,900,828 | 2.42 |
| 6 | Cable Nominees Pty Ltd | 19,851,270 | 1.85 |
| 7 | YRS Investments Ltd | 13,520,833 | 1.26 |
| 8 | Rick Wayne Crabb & Carol Jean Crabb | 12,000,905 | 1.12 |
| 9 | RBC Dexia Investor Services Australia Nominees Pty Ltd | 11,918,915 | 1.11 |
| 10 | Daly Finance Corp | 8,150,000 | 0.76 |
| 11 | Escot Finance Ltd | 8,150,000 | 0.76 |
| 12 | Berne No 132 Nominees Pty Ltd | 8,000,000 | 0.75 |
| 13 | Marmulla General Pty Ltd | 5,766,615 | 0.54 |
| 14 | Forbar Custodians Ltd | 5,641,240 | 0.53 |
| 15 | Pan Australian Nominees Pty Ltd | 4,339,074 | 0.41 |
| 16 | Zero Nominees Pty Ltd | 4,049,307 | 0.38 |
| 17 | Mr David Chan | 3,954,135 | 0.37 |
| 18 | Zadnik Holdings Pty Ltd | 3,581,375 | 0.33 |
| 19 | Mr Jeffrey Yih Peiri Hing & Mrs Bei Keen Wong | 3,500,000 | 0.33 |
| 20 | Marmulla Holdings Pty Ltd | 3,399,351 | 0.32 |
| | | 652,492,623 | 60.97 |

* Includes 210,983,082 shares held beneficially by Molton Holdings Ltd

# ASX ADDITIONAL INFORMATION (Cont'd)

## 3. SUBSTANTIAL SHAREHOLDERS AS AT 22 SEPTEMBER 2009

| | | No. of Shares Held | % Held |
|---|---|---|---|
| 1 | Molton Holdings Ltd | 210,983,082 | 19.71 |
| 2 | Santo Holding AG | 210,983,082 | 19.71 |

## 4. UNQUOTED SECURITIES

The unlisted securities of the Company as at 22 September 2009 are 119,855,350 Options, 2,500,000 Performance Shares and 4,000 Converting Performance Shares. The unlisted securities do not carry any right to vote at a general meeting of shareholders.

### Unlisted Options

| No. of Options | | Expiry Date | Exercise Price | No. of Holders |
|---|---|---|---|---|
| 4,083,400 | | 29 May 2011 | $0.20 | 13 |
| 4,333,300 | | 29 May 2011 | $0.30 | 13 |
| 2,333,300 | * | 29 May 2011 | $0.40 | 12 |
| 8,000,000 | | 30 November 2009 | $0.34 | 2 |
| 8,250,000 | | 17 December 2010 | $0.30 | 8 |
| 11,000,000 | | 25 January 2011 | $0.30 | 7 |
| 2,000,000 | * | 10 April 2012 | $0.35 | 2 |
| 2,500,000 | * | 01 August 2012 | $0.60 | 1 |
| 2,000,000 | * | 15 December 2010 | $0.60 | 1 |
| 61,855,350 | | 3 July 2010 | $0.05 | 2 |
| 7,500,000 | * | 30 June 2014 | $0.12 | 1 |
| 6,000,000 | | 8 September 2012 | $0.10 | 3 |
| 119,855,350 | | | | |

* Subject to certain share price and service vesting conditions.

### Performance Shares

| | | No. of Shares Held | % Held |
|---|---|---|---|
| 1 | RW & CJ Crabb <Intermax Trust> | 625,000 | 25.0 |
| 2 | Zadnik Holdings | 625,000 | 25.0 |
| 3 | Dormley Pty Ltd<Poll Family A/c> | 1,250,000 | 50.0 |
| | | 2,500,000 | 100.0 |

### Converting Performance Shares

| | | No. of Shares Held | % Held |
|---|---|---|---|
| 1 | Dormley Pty Ltd<Poll Family A/c> | 4.000 | 100.0 |
| | | 4,000 | 100.0 |

## 5. VOTING RIGHTS

In accordance with the Company's Constitution, on a show of hands every shareholder present in person or by proxy, attorney or representative of a shareholder has one vote and on a poll every shareholder present in person or by proxy, attorney or representative of a shareholder has in respect of fully paid shares, one vote for every share held. No class of option holder has a right to vote, however the shares issued upon exercise of options will rank pari passu with the then existing issued fully paid ordinary shares.

# CORPORATE DIRECTORY

**Directors**
Mr Rick Crabb – Non Executive Chairman
Mr Rufino Bomasang – Non Executive Director
Mr John Jetter – Non Executive Director
Mr Ian Macliver – Non Executive Director
Dr Jaap Poll – Non Executive Director
Mr John Zadnik – Alternate Director for Mr Rick Crabb

**Company Secretary**
Ms Emma McCormack

**Executive Management**
Mr Paul Moore – Chief Executive Officer
Mr Craig Martin – Chief Operating Officer

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**Website**
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**Auditors**
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128 Hay Street
Subiaco WA 6008
Tel: +61 8 9380 8400 Fax: +61 8 9380 8499

**Share Registry**
Computershare Investor Services Pty Ltd
Level 2, 45 St Georges Terrace
Perth WA 6000
Tel: +61 8 9323 2000 Fax :+61 8 9323 2033

**Home Stock Exchange**
Australian Securities Exchange
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ASX Code: OEL

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