Tethys Petroleum Limited

Consolidated Financial Statements
December 31, 2009
(in thousands of US dollars)

Management Report

The accompanying consolidated financial statements and all the information in the annual report are the responsibility of management. The consolidated financial statements have been prepared by management in accordance with the accounting policies described in the notes to the financial statements. In the opinion of management, the consolidated financial statements have been prepared within acceptable limits of materiality and are in accordance with International Financial Reporting Standards, appropriate in the circumstances, as issued by the International Accounting Standards Board. The consolidated financial information contained elsewhere in the annual report has been reviewed to ensure consistency with that in the consolidated financial statements.

Management has developed and maintains systems of internal accounting controls, policies and procedures in order to provide reasonable assurance as to the reliability of the financial records and the safeguarding of assets.

External auditors, appointed by the shareholders of the Company, have examined the consolidated financial statements and have expressed an opinion on the consolidated statements. Their report is included with the consolidated financial statements.

The Board of Directors of the Company has established an Audit Committee, consisting of independent non-management directors, to review consolidated financial statements with management and the auditors. The Board of Directors has approved the consolidated financial statements on the recommendation of the Audit Committee.

"Dr. D. Robson"
Chief Executive

"B. Murphy"
Chief Financial Officer

March 31, 2010

PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers LLP
Chartered Accountants
111 5 Avenue SW, Suite 3100
Calgary, Alberta
Canada T2P 5L3
Telephone +1 403 509 7500
Facsimile +1 403 781 1825

March 31, 2010

AUDITORS' REPORT

To the Shareholders of
Tethys Petroleum Limited

We have audited the consolidated statements of financial position of Tethys Petroleum Limited as at December 31, 2009, December 31, 2008 and January 1, 2008 and the consolidated statements of comprehensive loss, changes in equity and cash flows for each of the years ended December 31, 2009 and 2008. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2009, December 31, 2008 and January 1, 2008 and the results of its operations and its cash flows for each of the years ended December 31, 2009 and 2008 in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board.

PricewaterhouseCoopers LLP

Chartered Accountants
Calgary, Alberta

"PricewaterhouseCoopers" refers to PricewaterhouseCoopers LLP, an Ontario limited liability partnership, or, as the context requires, the PricewaterhouseCoopers global network or other member firms of the network, each of which is a separate legal entity.

Tethys Petroleum Limited

Consolidated Statement of Financial Position

(in thousands of US dollars)

	Note	As at December 31		As at January 1
		2009 $	2008 $	2008 (note 26) $
Non-current assets				
Property, plant and equipment	12	73,171	65,422	38,327
Intangible assets	11	24,378	16,105	7,335
Investments	13	659	587	318
Trade and other receivables	14	5,171	6,357	5,814
Loan receivable from jointly controlled entity	15	21,727	0	0
		125,106	88,471	51,794
Current assets				
Inventories		2,368	213	-
Trade and other receivables	14	2,311	2,664	1,360
Cash and cash equivalents	16	7,297	22,200	26,692
		11,976	25,077	28,052
Total assets		137,082	113,548	79,846
Equity attributable to shareholders				
Share capital	20	13,455	6,639	4,511
Share premium	20	153,748	138,598	94,972
Other reserves		27,775	25,147	20,728
Accumulated deficit		(88,374)	(66,654)	(44,470)
Total equity		106,604	103,730	75,741
Non-current liabilities				
Deferred gain on sale of assets to jointly controlled entity	15	3,659	-	-
Financial liabilities - borrowings	17	9,324	5,096	-
Shares to be issued		3,750	-	-
Deferred taxation	9	598	-	-
Trade and other payables	18	808	523	776
Asset retirement obligations	19	206	465	1,050
		18,345	6,084	1,826
Current liabilities				
Financial liabilities - borrowings	17	1,086	853	-
Derivative financial instruments - warrants	17	1,053	146	-
Derivative financial instruments – interest rate swap	17	95	-	-
Deferred revenue		3,113	-	-
Trade and other payables	18	6,786	2,735	2,279
		12,133	3,734	2,279
Total liabilities		30,478	9,818	4,105
Total shareholders' equity and liabilities		137,082	113,548	79,846
Commitments and contingencies	25			

The notes on pages 1 to 58 form part of these consolidated financial statements. The financial statements on pages 1 to 63 were approved by the Board on 31 March 2010 and were signed on its behalf.

"Dr. D. Robson"
Chief Executive

"B. Murphy"
Chief Financial Officer

Tethys Petroleum Limited

Consolidated Statement of Comprehensive Loss

(in thousands of US dollars, except for per share amounts)

	Note	Year ended December 31, 2009 $	2008 $
Sales and other operating revenues	6	8,559	5,360
Finance income		76	832
Total revenue and other income		8,635	6,192
Production expenditures		(3,405)	(1,334)
Depreciation, depletion and amortization		(3,238)	(4,333)
Exploration and evaluation expenditure written off		(887)	(2,292)
Listing expenses		(1,652)	-
Administrative expenses	7	(16,880)	(17,915)
Foreign exchange gains (loss) net		(2,397)	(3,060)
Fair value gain / (loss) on derivative financial instrument		(479)	929
Loss from jointly controlled entity	15	(1,000)	-
Finance costs		(203)	(371)
Loss before taxation		**(21,506)**	**(22,184)**
Taxation	9	(214)	-
Net loss and comprehensive loss for the year attributable to shareholders		**(21,720)**	**(22,184)**
Loss per share attributable to shareholders			
Basic and diluted	10	(0.20)	(0.40)

No dividends were paid or are declared for the year (2008 – $Nil).

The notes on pages 1 to 58 form part of these consolidated financial statements.

Tethys Petroleum Limited

Consolidated Statement of Changes in Equity
(in thousands of US dollars)

		Attributable to shareholders					
	Note	**Share capital $**	**Share premium $**	**Accumulated deficit $**	**Option reserves $**	**Warrant reserves $**	**Total equity $**
Balance at January 1, 2008	20	4,511	94,972	(44,470)	4,173	16,555	75,741
Comprehensive loss for the year		-	-	(22,184)	-	-	(22,184)
Transactions with shareholders							
Issue of share capital	20	2,128	47,872	-	-	-	50,000
Cost of share issue		-	(4,246)	-	-	-	(4,246)
Share-based payments		-	-	-	4,419	-	4,419
Total transactions with shareholders		2,128	43,626	-	4,419	-	50,173
Balance at January 1, 2009		6,639	138,598	(66,654)	8,592	16,555	103,730
Comprehensive loss for the year		-	-	(21,720)	-	-	(21,720)
Transactions with shareholders							
Issue of share capital	20	6,816	17,245	-	-	-	24,061
Cost of share issue		-	(2,095)	-	-	-	(2,095)
Share-based payments		-	-	-	2,628	-	2,628
Total transactions with shareholders		6,816	15,150	-	2,628	-	24,594
At December 31, 2009		13,455	153,748	(88,374)	11,220	16,555	106,604

The option reserve and warrant reserve are denoted together as “other reserves” on the consolidated statement of financial position. These reserves are non distributable.

The notes on pages 1 to 58 form part of these consolidated financial statements.

Tethys Petroleum Limited

Consolidated Statement of Cash Flows

(in thousands of US dollars)

	Note	Year ended December 31, 2009 $	2008 $
Cash flow from operating activities			
Loss before taxation		(21,506)	(22,184)
Adjustments for			
Share based payments	8	2,628	4,419
Net finance cost (income)		127	(461)
Unsuccessful exploration and evaluation expenditures	11	887	2,292
Depreciation, depletion and amortization	12	3,238	4,333
Fair value gain (loss) on derivative financial instrument		479	(929)
Net unrealised foreign exchange loss		1,120	1,277
Loss from jointly controlled entity		1,000	-
Deferred revenue		3,113	-
Net change in non-cash working capital	24	(1,160)	(844)
Net cash used in operating activities		(10,074)	(12,097)
Cash flow from investing activities			
Interest received		76	832
Expenditure on exploration and evaluation assets		(22,648)	(6,519)
Expenditures on property, plant and equipment		(9,573)	(36,288)
Investment in restricted cash		(72)	(269)
Acquisition of subsidiary, net of cash received		532	-
Sale of subsidiaries, net of cash disposed		(112)	-
Movement in advances to construction contractors		829	1,548
Value added tax receivable		(670)	(2,091)
Net change in non-cash working capital	24	1,273	(217)
Net cash used in investing activities		(30,365)	(43,004)
Cash flow from financing activities			
Proceeds from issuance of short-term borrowings	17	2,500	-
Repayment of short-term borrowings		(2,500)	-
Proceeds from issuance of long-term borrowings	17	5,020	7,430
Repayment of long-term borrowings	17	(856)	(579)
Interest paid on long-term borrowings and other non-current payables		(152)	(380)
Other non-current liabilities	18	(109)	(253)
Proceeds related to shares to be issued		3,750	-
Proceeds from issuance of equity, net of issue costs	20	17,906	45,754
Net cash generated from financing activities		25,559	51,972
Effects of exchange rate changes on cash and cash equivalents		(23)	(1,363)
Net decrease in cash and cash equivalents		(14,903)	(4,492)
Cash and cash equivalents at beginning of the year		22,200	26,692
Cash and cash equivalents at end of the year		7,297	22,200

The notes on pages 1 to 58 form part of these consolidated financial statements.

1 General information

Tethys Petroleum Limited and its subsidiaries (collectively "Tethys" or "the Company") are headquartered in Guernsey, British Isles. The domicile of Tethys Petroleum Limited was moved from Guernsey, British Isles to the Cayman Islands on July 17, 2008, where it is incorporated. The address of the Company's registered office is 89 Nexus Way, Camana Bay, Grand Cayman, Cayman Islands. Tethys is an oil and gas Company operating within the Republic of Kazakhstan, Republic of Uzbekistan and the Republic of Tajikistan. Tethys' principal activity is the acquisition of and development of crude oil and natural gas fields.

The Company has its primary listing on the Toronto Stock Exchange (TSX).

Statement of compliance

These consolidated financial statements have been prepared on a going concern basis under the historical cost convention except as modified by the revaluation of available for sale financial assets, and financial assets and financial liabilities at fair value through the statement of comprehensive loss and are in accordance with International Financial Reporting Standards (IFRSs) and International Financial Reporting Interpretations Committee (IFRIC) interpretations issued by the International Accounting Standards Boards ("IASB") and effective or issued and early adopted as at the time of preparing these financial statements.

The March 31, 2009 interim consolidated financial statements were the Company's first interim financial statements prepared under IFRS, with a transition date to IFRS of January 1, 2008. Consequently the comparative figures for 2008 and the Company's statement of financial position as at January 1, 2008 have been restated from accounting principles generally accepted in the United States of America ('US GAAP') to comply with IFRS. The reconciliations to IFRS from the previously published US GAAP financial statements are explained in note 26 of these financial statements by the IASB.

The preparation of financial statements in conformity with IFRS requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on management's best knowledge of the amount, event or actions, actual results ultimately may differ from those estimates. Areas where estimates are significant to the consolidated financial statements are disclosed in note 4.

2 Summary of significant accounting policies

Basis of preparation

The consolidated financial statements for the year ended December 31, 2009 have been prepared in accordance with International Financial Reporting Standards ("IFRS") and IFRIC Interpretations and are in accordance with IFRS 1 - First-time Adoption of IFRS. The consolidated financial statements have been prepared under the historical cost convention, as modified by the revaluation of financial assets and financial liabilities (including derivative instruments) at fair value through profit and loss.

The consolidated financial statements are presented in United States Dollars and all amounts are rounded to the nearest thousand (US$'000) except where otherwise indicated. Foreign operations are included in accordance with the policies set out in this note.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Company's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in note 4.

Since inception, the Company has incurred significant losses from operations and negative cash flows from operating activities, and has an accumulated deficit at December 31, 2009. The Company has significant short-term and longer term contractual commitments that will necessitate cash outflows. In the first three months of 2010 the Company raised in $58.35 million. In the longer term, the ability of the Company to successfully carry out its business plan will be dependent upon its ability not only to maintain the current level of gas and oil production but also to achieve further production of commercial oil and gas and to control the costs of operating and capital expenditures. The Company completed an Initial Public Offering (IPO) of equity securities on the Toronto Stock Exchange (TSX) on June 27, 2007. The Company subsequently issued additional capital for gross proceeds of $50 million on June 27, 2008 and $20 million on June 19, 2009 that generated sufficient funds to secure its future at least in the short term. If in the future, the Company is unable to generate significant revenues and cash flows from operations it may need to seek further funding from its shareholders or alternative sources. There can be no assurances that management will be successful with these initiatives. While these factors create doubt about the Company's ability to continue as a going concern, management is confident of achieving the Company's short term plans.

The financial statements have been prepared on the basis that the Company will continue to operate as a going concern, which contemplates the realization of assets and the settlement of liabilities and commitments in the normal course of business. These financial statements do not reflect adjustments in the carrying values of assets and liabilities reported, revenue or expenses and the classification used on the statement of financial position, that would be necessary if the going concern assumption was not appropriate. Such adjustments could be material.

Foreign Operations

Tethys' future operations and earnings will depend upon the results of Tethys' operations in the Republic of Kazakhstan, Uzbekistan and Tajikistan. There can be no assurance that Tethys' will be able to successfully conduct such operations, and a failure to do so would have a material adverse effect on Tethys' financial position, results of operations and cash flows. Also, the success of Tethys' operations will be subject to numerous contingencies, some of which are beyond management control. These contingencies include general and regional economic conditions, prices for crude oil and natural gas, competitions and changes in regulation. Since Tethys' is dependent on international operations, Tethys' will be subject to various additional political, economic and other uncertainties. Among other risks, Tethys' operations may be subject to the risks and restrictions on transfer of funds, import and export duties, quotas and embargoes, domestic and international customs and tariffs, and changing taxation policies, foreign exchange restrictions, political conditions and regulations.

Changes in accounting policy and disclosures

(a) New and amended standards adopted by the Company

The following new and amended accounting standards are mandatory and relevant for the Company for the first time for these financial statements:

- IFRS 7 'Financial instruments – Disclosures' (amendment). This amendment requires enhanced disclosures about fair value measurement and liquidity risk. In particular, the amendment requires disclosure of fair value measurements by level of a fair value measurement hierarchy.
- IFRS 8, 'Operating segments'. IFRS 8 replaces IAS 14, 'Segment reporting'. It requires a 'management approach' under which segment information is presented on the same basis as that used for internal reporting purposes.
- IAS 23 (amendment), 'Borrowing costs' requires an entity to capitalise borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset (one that takes a substantial period of time to get ready for use or sale) as part of the cost of that asset. The option of immediately expensing those borrowing costs has been removed. This has no impact on the Company as its policy has always been to capitalise borrowing cost on qualifying assets.
- IFRS 2 (amendment), 'Share-based payment'. The amended standard deals with vesting conditions and cancellations. It clarifies that vesting conditions are service conditions and performance conditions only. Other features of a share-based payment are not vesting conditions. These features would need to be included in the grant date fair value for transactions with employees and others providing similar services; they would not impact the number of awards expected to vest or valuation thereof subsequent to grant date. All cancellations, whether by the entity or by other parties, should receive the same accounting treatment. The amended standard does not have a material impact on the Company's financial statements.

(b) Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the Company

The following standards and amendments to existing standards have been published and are mandatory for the Company's accounting periods beginning on or after January 1, 2010 or later periods, but the Company has not early adopted them:

- IFRS 2, 'Share-based payments' – provides further guidance on determining the classification of share based payment awards in consolidated and separate financial statements and is linked to the application of IFRS 3 (revised). The amendments are effective for annual periods beginning on or after July 1, 2009. The amendment will not result in a material impact on the Company's financial statements.

- IFRS 3 (revised) 'Business combinations' is effective for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after July 1, 2009.

  The revised standard continues to apply the acquisition method to business combinations, with some significant changes. For example, all payments to purchase a business are to be recorded at fair value at the acquisition date, with contingent payments classified as debt subsequently re-measured through the statement of comprehensive loss. There is a choice on an acquisition-by-acquisition basis to measure the minority interest in the acquiree either at fair value or at the minority interest's proportionate share of the acquiree's net assets. All acquisition-related costs should be expensed. The Company will apply IFRS 3 (revised) to all business combinations from January 1, 2010.

- IFRS 8, 'Operating Segments' which provides further requirements for disclosure of information about segment assets and is effective for periods beginning on or after January 1, 2010 has no impact on disclosure of segment assets currently reported by the Company.

- IFRS 9, 'Financial Instruments' was issued in November 2009 as the first step in its project to replace IAS 39 'Financial Instruments: Recognition and Measurement'. IFRS 9 introduces new requirements for classifying and measuring financial assets that must be applied starting January 1, 2013, with early adoption permitted. The IASB intends to expand IFRS 9 during the intervening period to add new requirements for classifying and measuring financial liabilities, de-recognition of financial instruments, impairment and hedge accounting. The Company is currently assessing the impact of this standard.

- IAS 27 (revised) 'Consolidated and Separate Financial Statements'; requires the effects of all transactions with non-controlling interests to be recorded in equity if there is no change in control and these transactions will no longer result in goodwill or gains and losses. The standard also specifies when control is lost. Any remaining interest in the entity is remeasured to fair value, and a gain or loss is recognised in profit or loss. The Company will apply this standard prospectively to transactions with non-controlling interests from January 1, 2010. The amendment will not result in a material impact on the Company's financial statements.

- IAS 38 (amendment), 'Measurement of non-current assets (or disposal groups) classified as held-for-sale'. The amendment is part of the IASB's annual improvements project published in April 2009 and the Company will apply IAS 38 (amendment) from the date IFRS 3 (revised) is adopted. The amendment clarifies guidance in measuring fair value of an intangible asset acquired in a business combination and it permits the grouping of intangible assets as a single asset if each asset has similar useful economic lives. The amendment will not result in a material impact on the Company's financial statements.

- IFRIC 17, 'Distributions of non-cash assets to owners', clarifies how an entity should measure distributions of assets, other than cash, when it pays dividends to its owners and is effective for annual periods beginning on or after July 1, 2009. The amendment will not result in a material impact on the Company's financial statements.

Basis of consolidation

Subsidiaries
Subsidiaries are all entities over which the Company has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. Subsidiaries are fully consolidated from the date on which control is transferred to the Company.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Company. The cost of acquisition is measured at the fair value of assets given, equity instruments issued and debt incurred or assumed at the date of acquisition, being the date on which the Company gains control. The excess of the cost over the fair value of the Company's share of identifiable net assets acquired is recorded as goodwill. If the cost is less than the fair value of net assets acquired, the difference is recognised directly in the statement of comprehensive loss. All subsidiaries, as listed in note 23, have been consolidated into the Company's consolidated financial statements.

Inter-Company transactions, balances and unrealised gains or losses between subsidiaries are eliminated. The financial statements of the subsidiaries are prepared using consistent accounting policies and reporting date as of the Company.

Joint ventures

The Company's interests in jointly controlled entities are accounted for using the equity method of accounting. Under the equity method, the investment in a jointly controlled entity is carried in the statement of financial position at cost plus post-acquisition charges in the Company's share of net assets of the jointly controlled entity, less distributions received and less any impairment in value of the investment. The Company's statement of comprehensive loss reflects the Company's share of the results after tax of the jointly controlled entity.

When the Company's share of losses in the jointly controlled entity equals or exceeds its interest in the entity, including any other unsecured receivables, the Company does not recognise further losses, unless it has incurred obligations or made payments on behalf of the jointly controlled entity. Financial statements of jointly controlled entities are prepared for the same reporting year as the Company.

The Company recognises the portion of gains or losses on the sale of assets by the Group to the joint venture that is attributable to the other parties in the joint venture. The Company does not recognise its share of profits or losses that results from the purchase of assets by the Group from the joint venture until when the asset is resold or, where relevant, as the asset is depreciated by the jointly controlled entity.

In circumstances where the significant risks and rewards of ownership of non-monetary assets transferred have not been transferred to the jointly controlled entity, the associated gain or loss is unrealised and , thus, not recognised in profit or loss but recognised as a deferred gain on the statement of financial position. The deferred gain is recognised in the statement of comprehensive loss when the asset is resold or, where to relevant, as the asset is depreciated by the jointly controlled entity.

Accounting policies of the joint venture are consistent with accounting policies adopted by the Company.

Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-maker has been identified as the Executive directors that make strategic decisions.

Foreign currency translation

The consolidated financial statements are presented in US Dollars, which is the Company's functional and reporting currency.

All monetary assets and liabilities denominated in foreign currencies are translated into US dollars at the rate of exchange in effect at the reporting date. Non-monetary assets are translated at historical exchange rates.

Revenue and expense items (excluding depreciation and amortization which are translated at the same rates as the related assets) are translated at the average rate of exchange.

Exchange gains and losses arising on translation are taken to the statement of comprehensive loss.

Oil and gas exploration and evaluation expenditure

Oil and natural gas exploration and evaluation expenditures are accounted for using a modified 'successful efforts' method of accounting. Costs are accumulated on a field-by-field basis. Exploration and evaluation expenditures, including license acquisition costs, are capitalised as exploration and evaluation assets when incurred. Expenditure directly associated with an exploration well is capitalised until the determination of reserves is evaluated. If reserves are not identified, these costs are charged to expense. All other associated exploration and evaluation expenditure are carried forward as an asset in the statement of financial position where the rights of tenure of the property are current and it is considered probable that the costs will be recouped through successful development of the property, or alternatively by its sale. Capitalised exploration and evaluation expenditure is written down to its recoverable amount where the above conditions are no longer satisfied.

If it is determined that a commercial discovery has not been achieved in relation to the property, all other associated costs are written down to their recoverable amount. If commercial reserves are found, exploration and evaluation assets are tested for impairment and transferred to development tangible and intangible assets. No depreciation and/or amortisation is charged during the exploration and evaluation phase.

Oil and gas properties

Oil and gas properties are stated at cost, less accumulated depreciation and accumulated impairment losses.

Expenditure on the construction, installation or completion of infrastructure facilities such as platforms, pipelines and the drilling of development wells, including unsuccessful development or delineation wells, is capitalised within oil and gas properties, as long as the facts and circumstances indicate that the field has commercially viable reserves.

The initial cost of an asset comprises its purchase price or construction cost, any costs directly attributable to bringing the asset into operation, the initial estimate of the asset retirement obligation, and for qualifying assets, borrowing costs. The purchase price or construction cost is the aggregate amount paid and the fair value of any other consideration given to acquire the asset. The capitalised value of a finance lease is also included within property, plant and equipment.

Where commercial production in an area of interest has commenced, oil and gas properties are depreciated on a unit-of-production basis over the proved and probable reserves of the field concerned, except in the case of assets whose useful life is shorter than the lifetime of the field, in which case the straight-line method is applied. Rights and concessions are depleted on the unit-of-production basis over the total proved and probable reserves of the relevant area. The unit-of-production rate for the amortisation of field development costs takes into account expenditures incurred to date, together with future development expenditure to develop the proved and probable reserves. Changes in factors such as estimates of proved and probable reserves that affect unit-of-production calculations do not give rise to prior year financial period adjustments and are dealt with on a prospective basis.

Other property, plant and equipment

Property, plant and equipment are carried at cost less accumulated depreciation. Depreciation is charged so as to write off the cost of these assets less residual value over their estimated useful economic lives, for the following classes of assets:

Drilling rigs and related oil and gas equipment	Unit of production	3,650 operating days
Smaller rig related equipment	Straight line	6 – 8 years
Vehicles	Straight line	4 years
Computer equipment	Straight line	3 years
Office equipment	Straight line	5 years

Intangible assets

Production enhancement contracts

Production enhancement contracts are stated at cost less accumulated amortisation and have a finite useful life. Amortization is calculated using a unit-of-production basis over the estimated incremental production entitlement expected to be received over the life of the contract.

Impairment of non-financial assets

Exploration and evaluation costs are tested for impairment when reclassified to oil and gas properties or whenever facts and circumstances indicate potential impairment. An impairment loss is recognised for the amount by which the exploration and evaluation expenditure's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of the exploration and evaluation expenditure's fair value less costs to sell and their value in use.

Values of oil and gas properties and other property, plant and equipment are reviewed for impairment when indicators of such impairment exist. If any indication of impairment exists an estimate of the asset's recoverable

amount is calculated. Individual assets are grouped for impairment assessment purposes at the lowest level at which there are identifiable cash flows that are largely independent of the cash flows of other groups of assets. An asset group's recoverable amount is the higher of its fair value less costs to sell and its value in use. Where the carrying amount of an asset group exceeds its recoverable amount, the asset group is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are adjusted for the risks specific to the asset group and are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money.

If the carrying amount of the asset exceeds its recoverable amount, the asset is impaired and an impairment loss is charged to the statement of comprehensive loss so as to reduce the carrying amount to its recoverable amount (i.e. the higher of fair value less cost to sell and value in use).

For assets excluding goodwill, an assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the Company makes an estimate of the recoverable amount. A previously recognised impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. If that is the case the carrying amount of the asset is increased to its recoverable amount. That increased amount cannot exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years.

Asset retirement obligation (ARO)

Provision is made for the present value of the future cost of abandonment of oil and gas wells and related facilities. This provision is recognised when a legal or constructive obligation arises.

The estimated costs, based on engineering cost levels prevailing at the reporting date, are computed on the basis of the latest assumptions as to the scope and method of abandonment. Provisions are measured at the fair value of the expenditures expected to be required to settle the obligation using a pre-tax rate, updated at each reporting date that reflects current market assessments of the time value of money and the risks specific to the obligation. The corresponding amount is capitalised as part of exploration and evaluation expenditure or oil and gas properties and is amortised on a unit-of-production basis as part of the depreciation, depletion and amortisation charge. Any adjustment arising from the reassessment of estimated cost of ARO is capitalised, whilst the charge arising from the accretion of the discount applied to the ARO is treated as a component of finance costs.

Financial instruments

Financial assets and financial liabilities are recognised on the Company's statement of financial position when the Company becomes party to the contractual provisions of the instrument. Financial assets are de-recognised when the contractual rights to the cashflows from the financial asset expire or when the contractual rights to those assets are transferred. Financial liabilities are de-recognised when the obligation specified in the contract is discharged, cancelled or expired.

Investments

Investments comprise restricted current balances that are held on deposit with banks in the Republic of Kazakhstan in respect of the Company's asset retirement obligations (ARO) in this country and are classified as non-current. They are carried at fair value with gains or losses taken to the statement of comprehensive loss.

Trade receivables, loans and other receivables

Trade receivables, loans and other receivables, which are non-derivative financial assets that have fixed or determinable payments that are not quoted in an active market, are classified as loans and receivables. They are included in current assets, except for maturities greater than 12 months after the reporting date, which are classified as non-current assets. The Company's loans and receivables comprise trade and other receivables in the statement of financial position.

Loans and receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest rate method, net of any impairment.

A provision for impairment of trade receivables is established when there is objective evidence that the Company will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments (more than 60 days overdue) are considered indicators that the trade receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the loss is recognised in the statement of comprehensive loss. When a trade receivable is uncollectible, it is written off against the allowance account for trade receivables.

Cash and cash equivalents

Cash and cash equivalents comprise cash in hand, deposits held at call with banks and other short-term highly liquid investments with original maturities of three months or less. These are carried at fair value with gains or losses recognized through statement of comprehensive loss.

Financial liabilities - borrowings

Borrowings are initially recognised at the fair value of the consideration received less directly attributable transaction costs. After initial recognition, interest bearing loans and borrowings are subsequently measured at amortised cost using the effective interest method. Gains and losses are recognised in the statement of comprehensive loss when the liabilities are derecognised as well as through the amortisation process.

Trade payables

Trade payables are obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Accounts payable are classified as current liabilities if payment is due within one year or less. If not, they are presented as non-current liabilities. Trade payables are measured at amortised cost using the effective interest method.

Equity instruments

Equity instruments issued by the Company are recorded at the proceeds received net of direct issue costs.

Derivative financial instruments

Derivative financial instruments are initially recognized at fair value on the date a derivative contract was entered into and are subsequently remeasured at their fair value with changes in the fair value immediately recognised in the statement of comprehensive loss.

Derivatives embedded in other financial instruments or other host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of the host contract. Contracts are assessed for embedded derivatives when the Company becomes a party to them, including at the date of a business combination.

Derivative contracts qualifying for the 'own-use' treatment

An 'own-use' contract is one that was entered into and continues to be held for the purpose of the receipt or delivery of the non financial item in accordance with the entity's expected purchase, sale or usage requirements. Contracts that are for the Company's own use are exempt from the requirements of IAS39.

Inventories

Inventories consist of refined oil products, spare parts and consumable materials and are shown at the lower of cost and net realisable value. Cost is determined on a weighted average cost method for refined oil products and the first-in-first-out method for spare parts and consumable materials inventories.

Taxation including deferred taxation

The tax expense represents current tax and deferred tax.

Current tax is based on the taxable profits for the year. The Company's current tax is calculated using tax rates that have been enacted or substantively enacted by the reporting date.

Deferred income tax is recognised, using the liability method, on temporary differences arising between the bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction, other than a business combination, that at the time of the transaction affects neither the accounting nor taxable profit or loss. Deferred income tax assets are recognised to the extent that it is probable that the future taxable profit will be available against which the temporary differences can be utilised and the carry forward of unused tax credits and unused tax losses can be utilised.

Deferred income tax is determined using tax rates (and laws) that have been enacted or substantively enacted by the reporting date and are expected to apply when the related deferred tax asset is realised or the deferred income tax liability settled.

Share–based payments

The Company operates a number of equity-settled, share-based compensation plans, under which the entity receives services from employees as consideration for equity instruments (options and warrants) of the Company. The fair value of the employee options and warrants granted in exchange for the employee services, is recognised as an expense. The total amount to be expensed is determined by reference to the fair value of the options granted, excluding the impact of any non-market service and performance vesting conditions. Non-market vesting conditions are included in assumptions about the number of options that are expected to vest. When options vest in instalments over the vesting period, each instalment is accounted for as a separate arrangement. At each reporting date, the entity revises its estimates of the number of options that are expected to vest. It recognises the impact of the revision of original estimates, if any, in the statement of comprehensive loss, with a corresponding adjustment to equity.

The proceeds received net of any directly attributable transaction costs are credited to share capital and share premium when the options are exercised.

Provisions

Provisions are recognised when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the Company expects some or all of a provision to be reimbursed, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain. The expense relating to any provision is presented in the statement of comprehensive loss, net of any reimbursement. The increase in the provision due to passage of time is recognized as interest expense.

Revenue recognition

Revenue comprises the fair value of the consideration received or receivable for the sale of natural gas and oil products in the ordinary course of the Company's activities and is recognized when the amount can be reliably measured, it is probable that future economic benefits will flow to the entity, and when specific criteria have been met for each of the Company's activities as described below. Revenue is shown after eliminating sales within the Company

Revenue from natural gas sales is recognized when the gas has been lifted and the risk of loss transferred to a third-party purchaser and is shown net of royalties, Mineral Extraction Tax (MET) and value-added tax. Revenue from refined product sales is recognized upon delivery and is shown net of value-added tax. All payments received before delivery are recorded as deferred revenue until delivery has occurred.

The Company recognises finance income earned on the Company's cash and cash equivalents and short term investments on an accrual basis.

Barter transactions

Where goods or services are exchanged for goods or services of a dissimilar nature, the revenue is measured at the fair value of the goods or services received, adjusted by the amount of cash or cash equivalents received or

paid. If the fair value of the goods or services received cannot be reliably measured, the revenue is measured at the fair value of the goods or services given up, again adjusted by the amount of cash or cash equivalents received.

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of a qualifying capital asset or project under construction are capitalised and added to the asset or project cost during construction until such time as the asset or project is substantially ready for its intended use. Where funds are specifically borrowed to finance an asset or project, the amount capitalised represents the actual amount of borrowing cost incurred. Where funds used to finance an asset or project form part of general borrowings, the amount capitalised is calculated by using a weighted average of rates applicable to relevant general borrowings of the Company during the period. All other borrowing costs are recognised in the statement of comprehensive loss in the period in which they are incurred.

Leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases are charged to the statement of comprehensive loss on a straight-line basis over the period of the lease.

Business combinations

Business combinations are accounted for using the purchase method of accounting. The cost of an acquisition is measured as the cash paid and the fair value of other assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. The acquired identifiable assets, liabilities and contingent liabilities are measured at their fair values at the date of acquisition. Any excess of the cost of acquisition over the net fair value of the identifiable assets, liabilities and contingent liabilities acquired is recognized as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognized directly in the statement of comprehensive loss.

Goodwill represents the excess of the cost of an acquisition over the fair value of the Company’s share of the net identifiable assets of the acquired subsidiary at the date of acquisition. Goodwill on acquisitions of subsidiaries is included in ‘intangible assets’. Goodwill is tested annually for impairment and carried at cost less accumulated impairment losses. Impairment losses on goodwill are not reversed. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

Goodwill is allocated to cash-generating units for the purpose of impairment testing. The allocation is made to those cash-generating units or groups of cash-generating units that are expected to benefit from the business combination in which the goodwill arose identified according to operation segment.

Fair value

The fair value of investments, trade and other receivables, trade and other payables approximate their carrying amounts due to the short term maturity of the instruments. Loan receivables, long term debt and other non-current liabilities have been recorded at amortized cost using the effective interest rate method.

3 Financial risk management

The Company's activities expose it to a variety of financial risks: market risk, credit risk and liquidity risk. The Company's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Company's financial performance.

Risk management is carried out by senior management, in particular, the Executive Board of Directors.

a) Financial risk factors

Credit risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to financial instruments fails to meet its contractual obligations. Credit risk arises from the Company's cash and cash equivalents and accounts receivable balances.

With respect to the Company's financial assets the maximum exposure to credit risk due to default of the counter party is equal to the carrying value of these instruments. The maximum exposure to credit risk as at the reporting date is:

	December 31 2009 $	December 31 2008 $
Trade receivables	905	1,124
Cash and cash equivalents	7,297	22,200
Investments	659	587
Loan receivable from jointly controlled entity	21,727	-
	30,588	23,911

Concentration of credit risk associated with the above trade receivable balances in Kazakhstan is as a result of contracted sales to only one customer during the year. The Company does not believe it is dependent upon this customer for sales due to the nature of gas products and the associated market. The Company's sales in Kazakhstan commenced in December 2007 and the Company has not experienced any credit loss to date. At December 31, 2009 the trade receivable amounted to $905,000, none of which was greater than 60 days overdue. The Company has therefore not recorded a provision against this amount as it does not consider the balance to be impaired.

In Uzbekistan, the Company makes use of five customers. Full payment is required before delivery of the oil and therefore there is limited exposure to credit risk in this country.

Although a significant amount of the deposits at financial institutions are not covered by bank guarantees, the Company does not believe there to be a significant risk of credit loss as the counterparties are banks with high credit ratings (A- or equivalent) assigned by international ratings agencies (Fitch and Standard and Poors).

The Company is exposed to credit risk in relation to its loan receivable from a jointly controlled entity to the extent that the jointly controlled entity fails to meet its contractual obligations. The Company does not believe that the balance is impaired at the reporting date. The carrying amount of the loan receivable represents the maximum exposure to credit risk.

Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. This risk relates to the Company's ability to generate or obtain sufficient cash or cash equivalents to satisfy these financial obligations as they become due. Since inception, the Company has incurred significant consolidated losses from operations and negative cash flows from operating activities, and has an accumulated deficit at December 31, 2009.

The Company's processes for managing liquidity risk includes preparing and monitoring capital and operating budgets, co-ordinating and authorizing project expenditures and ensuring appropriate authorization of contractual agreements. The budget and expenditure levels are reviewed on a regular basis and updated when circumstances indicate change is appropriate. The Company seeks additional financing based on the results of these processes.

	Less than 1 year	1-3 years	4-5 years	Thereafter	Total
	$	$	$	$	$
Trade and other payables	6,786	808	-	-	7,594
Financial liabilities - borrowings (note 17)	1,086	9,324	-	-	10,410
Commitments (note 25)	5,790	173	2,600	-	8,563
Share of purchase commitments related to joint venture (note 15)	2,137	-	-	-	2,137
Operating lease commitments (note 25)	415	363		-	778
Total expected cash outflow	16,214	10,668	2,600	-	29,482

The timing of cash outflows relating to financial liabilities and commitments at the reporting date are summarized below:

There can be no assurance that debt or equity financing will be available or sufficient to meet the Company's requirements or if debt or equity financing is available, that it will be on terms acceptable to the Company. The

inability of the Company to access sufficient capital for its operations could have a material adverse impact on the Company's financial condition, results of operations and prospects.

Market risk

Market risk is the risk of loss that may arise from changes in market factors such as commodity prices, interest rate and foreign exchange rates.

Commodity price risk

Commodity price risk arises from the effect that fluctuations of future commodity process may have on the price received for sales of gas and refined oil products. The marketability and price of natural gas and oil that is produced and may be discovered by the Company will be affected by numerous factors that are beyond the control of the Company.

Natural gas prices are subject to wide fluctuations, the Company has entered into a fixed price contract for sales of gas from the Kyzyloi field in Kazakhstan. However, any material decline in natural gas prices could result in a reduction of Tethys' future net production revenues and impact on the commercial viability of the Company's existing and future oil and gas discoveries. It may become uneconomic to produce from some wells as a result of lower prices, which could result in a reduction in volumes and the value of Tethys' gas reserves, if the Company elected not to produce from certain wells at lower prices.

Any material decline in refined oil product prices could result in a reduction of the Company's Uzbekistan net production revenue.

All of these factors could result in a material decrease in the Company's net production revenue causing a reduction in its acquisition and development activities.

The impact of changes in commodity price is assessed in note 4.

Interest rate risk

Interest rate risk is the risk that the value of a financial instrument will be affected by changes in market interest rates. Existing long term debt is agreed at fixed interest rates and consequently has limited exposure to changes in market interest rates.

The Company is exposed to interest rate risk on short term deposits to the extent that the significant reductions in market interest rates would result in a decrease in the interest earned by the Company. A change of 1% in the interest rate would have had an immaterial change in the interest earned both in the current or prior year.

(tabular amounts in thousands of US dollars)

As at the reporting date the Company's interest rate profile was:

At December 31, 2009	Fixed rate financial instruments $	Floating rate financial instruments $	**Total** $
Cash and cash equivalents	-	7,297	7,297
Financial liabilities - borrowings	10,410	-	10,410
Interest rate swap	95	-	95
	10,505	7,297	17,802

At December 31, 2008	Fixed rate financial instruments $	Floating rate financial instruments $	Total $
Cash and cash equivalents	1,832	20,368	22,200
Financial liabilities - borrowings	5,949	-	5,949
	7,781	20,368	28,149

Foreign exchange risk

The Company is exposed to risks resulting from fluctuations in foreign currency exchange rates. A material change in the value of any such foreign currency could result in a material adverse effect on the Company's cash flow and future profits. The Company is exposed to exchange rate risk to the extent that balances and transactions denominated in a currency other than the US dollar. In addition, a significant portion of expenditures in Kazakhstan and Tajikistan are denominated in local currency, the Tenge and Somoni, respectively. The Company is not currently using exchange rate derivatives to manage exchange rate risks but is attempting to negotiate exchange rate stabilization conditions in new local Tenge denominated service and supply contracts in Kazakhstan.

The Company holds the majority of its cash and cash equivalents in US dollars. However, the Company does maintain deposits in other currencies, as disclosed in the following table, in order to fund ongoing general and administrative activity and other expenditure incurred in these currencies.

The carrying amounts of the Company's significant foreign currency denominated monetary assets and liabilities at the reporting dates are as follows:

In US$ equivalent 2009	**CAD**	**GBP**	**EUR**	**SOMONI**	**KZT**
Cash and cash equivalents	52	132	83	11	187
Trade and other receivables	-	34	2	-	5,393
Trade and other payables	(35)	(318)	-	-	(561)
Financial liabilities - borrowings	-	(383)	-	-	-
Net exposure	**17**	**(535)**	**85**	**11**	**5,019**

In US$ equivalent 2008	CAD	GBP	EUR	SOMONI	KZT
Cash and cash equivalents	3,514	2,859	162	19	193
Trade and other receivables	-	-	-	-	5,967
Trade and other payables	(40)	(240)	(5)	-	(344)
Financial liabilities - borrowings	-	(365)	-	-	-
Net exposure	**3,474**	**2,254**	**157**	**19**	**5,816**

The following table details the Company's sensitivity to a 10% weakening in US dollars against the respective foreign currencies, which represents management's assessment of a reasonable change in foreign exchange rates.

	CAD	GBP	EUR	SOMONI	KZT
2009 Effect in US$'000					
Profit or (loss) before tax	-	(20)	10	-	500
2008 Effect in US$'000					
Profit or (loss) before tax	340	260	20	-	580

A 10% strengthening of the US dollar against the currencies above at December 31, 2009 would have had an equal but opposite effect on the amounts shown above, assuming all other variables remained constant.

b) Capital risk management

The Company's capital structure is comprised of shareholders' equity and debt.

The Company's objectives when managing capital is to maintain adequate financial flexibility to preserve its ability to meet financial obligations, both current and long term. The capital structure of the Company is managed and adjusted to reflect changes in economic conditions.

The Company funds its expenditures on commitments from existing cash and cash equivalent balances, primarily received from issuances of shareholders equity and some debt financing. None of the outstanding debt is subject to externally imposed capital requirements.

Financing decisions are made by management and the Board of Directors based on forecasts of the expected timing and level of capital and operating expenditure required to meet the Company's commitments and development plans. Factors considered when determining whether to issue new debt or to seek equity financing include the amount of financing required, the availability of financial resources, the terms on which financing is available and consideration of the balance between shareholder value creation and prudent financial risk management.

Net debt is calculated as total borrowings (including 'current and non-current borrowings' as shown in the consolidated statement of financial position) less cash and cash equivalents. Total capital is calculated as 'equity' as shown in the consolidated statement of financial position plus net debt.

At December 31	**2009**	2008
	$	$
Total financial liabilities - borrowings (Note 17)	10,410	5,949
Less: cash and cash equivalents	(7,297)	(22,200)
Net debt / (funds)	3,113	(16,251)
Total equity	167,203	145,237
Total capital	170,316	128,986

If the Company is in a net debt position, the Company will assess whether the projected cash flow is sufficient to service this debt and support ongoing operations. Consideration will be given to reducing the total debt or raising funds through an alternative route such as the issuing of equity.

The Company is not currently subject to any externally imposed capital restrictions.

c) Fair value estimation

Effective January 1, 2009, the Company adopted the amendment to IFRS 7 for financial instruments that are measured in the reporting date at fair value, this requires disclosure of fair value measurements by level of the following fair value measurement hierarchy:

Level 1: Quoted prices (unadjusted) in active markets for identical assets and liabilities. The Company does not have any assets or liabilities that require Level 1 inputs.

Level 2: Inputs other than quoted prices included within Level 1 that are observable, either directly or indirectly. For the Company, Level 2 inputs include prices that can be corroborated with other observable inputs for substantially the complete term of the contract.

Level 3: Unobservable inputs. For the Company, Level 3 inputs include production and price assumptions that are not based on observable market data (unobservable inputs) or are reliant on adjustments or interpolations are made by management to an otherwise standard valuation model.

As at December 31, 2009 the Company’s only financial liabilities measured at fair value on a recurring basis were the warrant liability and interest rate swap described in Note 17, the measurement inputs of which is designated as Level 2 and Level 3 respectively.

At December 31, 2009, the interest rate swap described in Note 17 is classified as Level 3 in the fair value hierarchy. The inputs required to measure the fair value of the interest rate swap include production and price assumptions that are reliant on adjustments or interpolation made by management to an otherwise standard valuation model. A reconciliation from the beginning balance to the ending balance of the interest rate swap has been included at Note 17.

4 Critical judgements and accounting estimates

The preparation of financial statements requires management to make certain judgements, accounting estimates and assumptions that affect the amounts reported for assets and liabilities as at the reporting date and the amounts reported for revenues and expenses during the year. The nature of estimation means that actual outcomes could differ from those estimates. Accordingly, the impact of these estimates, assumptions and judgments on the consolidated financial statements in future periods could be material. The key sources of estimation uncertainty that have a significant risk of causing material adjustment to the carrying amounts of assets and liabilities are discussed below.

Going Concern

The assessment of the Company's ability to execute its strategy by funding future working capital requirements involves judgement. The Directors monitor future cash requirements to assess the Company's ability to meet these future funding requirements. Further information regarding going concern is outlined in note 2.

Recoverability of asset carrying values

The Company assesses its property plant and equipment, including intangible exploration and evaluation assets, for possible impairment if there are events or changes in circumstances that indicate that carrying values of the assets may not be recoverable, or at least at every reporting date. Such indicators include changes in the Company's business plans, changes in commodity prices, evidence of physical damage and, for oil and gas properties, significant downward revisions of estimated recoverable volumes or increases in estimated future development expenditure.

If there are low oil prices or natural gas prices during an extended period the Company may need to recognize significant impairment charges. The assessment for impairment entails comparing the carrying value of the cash-generating unit with its recoverable amount, that is, value in use. Value in use is usually determined on the basis of discounted estimated future net cash flows. Determination as to whether and how much an asset is impaired involves management estimates on highly uncertain matters such as future commodity prices, the effects of inflation on operating expenses, discount rates, production profiles and the outlook for regional market supply-and-demand conditions for crude oil, natural gas and refined products.

At the reporting date, an impairment test was carried out on the Akkulka and Kyzyloi, gas fields in accordance with the accounting policy stated in note 2. The recoverable amounts of the fields have been determined based on value in use calculations. These calculations require the use of estimates. The present value of future cash flows was computed on an pre-tax basis by applying forecast prices of gas reserves to estimated future production of proved and probable gas reserves, less estimated future expenditures to be incurred in developing and producing the proved and probable reserves. The present value of estimated future net revenues is computed using a discount factor of 10%. The discount rate used is pre-tax and reflects the specific risks relating to the underlying cash generating unit.

The value in use calculation assumes natural gas sales prices in US$/Mcf as follows:

	2010 $	2011 $	2012 $	2013 $	2014 $	2015 $	2016 $	2017 $	2018 $	2019 $	2020 $	2021 $	2022 $	2023 $
Natural gas US$/Mcf														
Kyzyloi	0.90	0.90	0.90	4.41	4.91	5.37	5.62	5.84	6.04	6.25	6.45	6.63	6.81	7.0
Akkulka	0.90	3.38	3.90	4.41	4.91	5.37	5.62	5.84	6.04	6.25	6.45	6.63	-	-

The above price estimates are lower than those previously expected by the Company, which is a reflection of the current gas market uncertainty in Central Asia. As at the reporting date and at the date of approval of these consolidated financial statements, the gas price remains the subject of negotiations which have not been finalised. This is a source of measurement uncertainty in the Company's impairment test since there can be no assurance as to what price will be achieved.

The current price estimates for the Kyzyloi field results in an excess of recoverable amount over the carrying value of the Kyzyloi cash generating unit of $13.3 million. The current price estimates for the Akkulka field results in excess of recoverable amount over the carrying value of the Akkulka cash generating unit of $17.6 million.

If the forecast prices applied to the Kyzyloi impairment test were to reduce by US$0.10 per Mcf below the assumed price of US$4.41 (from 2013) per Mcf, the excess of recoverable amount over the carrying value of the Kyzyloi field would be reduced by approximately $639,000 for each $US 0.10 diminution of actual price realised.

If the forecast prices applied to the Akkulka impairment test were to reduce by US$0.10 per Mcf below the assumed price of US$3.38 per Mcf, the excess of recoverable amount over the carrying value of the Akkulka field would be reduced by approximately $883,000 for each $US 0.10 diminution of actual price realised.

Oil and gas reserves

Proved and probable oil and gas reserves are used in the units of production calculation for depletion as well as the determination of the timing of well closure costs and impairment analysis. There are numerous uncertainties inherent in estimating oil and gas reserves. Assumptions that are valid at the time of estimation may change significantly when new information becomes available. Changes in the forecast prices of commodities, exchange rates, production costs or recovery rates may change the economic status of reserves and may ultimately result in the reserves being restated.

The Company makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. Such estimates and assumptions are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Asset retirement obligation

Provisions for environmental clean-up and remediation costs associated with the Company's drilling operations are based on current legal and constructive requirements, technology, price levels and expected plans for

remediation. Actual costs and cash outflows can differ from estimates because of changes in laws and regulations, public expectations, prices, discovery and analysis of site conditions and changes in clean-up technology.

Income taxes

The Company is subject to income taxes in numerous jurisdictions. Significant judgement is required in determining the worldwide provision for income taxes. There are many transactions and calculations for which the ultimate tax determination is uncertain. The Company recognises liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the current and deferred income tax assets and liabilities in the period in which such determination is made.

Fair value of derivative and other financial instruments

The fair value of financial instruments that are not traded in an active market is determined by using valuation techniques. The Company uses its judgement to select a variety of methods and make assumptions that are mainly based on market conditions existing at the end of each reporting period.

Other significant areas of judgement

The estimates, assumption and judgments made in relation to the fair value of stock based compensation and warrants and the associated expense recognition is subject to measurement uncertainty. The estimated fair value of financial assets and liabilities, by their very nature, are subject to measurement uncertainty.

5 Segmental Reporting

Geographical segments

Management has determined the operating segments based on the reports reviewed by the executive directors that are used to make strategic decisions. Reports provided to the executive directors with respect to segment information are measured in a manner consistent with that of the financial statements. The assets and liabilities are allocated based on the operations of the segment and for assets, the physical location of the asset.

The executive directors consider the business from predominantly a geographic perspective and the Company currently operates in three geographical markets: Kazakhstan, Tajikistan and Uzbekistan.

In Kazakhstan, the Company is producing gas from the Kyzyloi field and is undertaking exploration and evaluation activity in the Akkulka and Kulbas fields. In Tajikistan, the Company is currently undertaking exploration and evaluation activity and in Uzbekistan, the Company operates under the North Urtabulak Production Enhancement Contract, which gives incremental production rights to increase the production volume of oil from wells on the North Urtabulak Oil Field.

The Company also operates a corporate segment which acquired a number of drilling rigs and related oil and gas equipment which will be utilised in Kazakhstan, Tajikistan, and Uzbekistan and possibly throughout the rest of Central Asia.

The segment results for the year ended December 31, 2009 are as follows:

	Kazakhstan $	Tajikistan $	Uzbekistan $	Other and Corporate $	Consolidated $
Gas sales	3,828	-	-	-	3,828
Refined product sales	-	-	4,731	-	4,731
Other income	3,230	-	-	1,824	5,054
Segment revenue	**7,058**	**-**	**4,731**	**1,824**	**13,613**
Inter-segment revenue	(3,230)	-	-	(1,824)	(5,054)
Revenue from external customers	**3,828**	**-**	**4,731**	**-**	**8,559**
Loss from jointly controlled entity	-	(1,000)	-	-	(1,000)
(Loss)/ profit before taxation	**(5,165)**	**(3,040)**	**478**	**(13,779)**	**(21,506)**
Taxation	(64)	-	(145)	(5)	(214)
Net (loss)/profit attributable to shareholders	**(5,229)**	**(3,040)**	**333**	**(13,784)**	**(21,720)**

Sales in the Kazakhstan segment were made to a single customer. Sales in the Uzbekistan segment were to five customers. Sales to three of those customers representing greater than 10% of total segment revenue were $2,600,000, $763,000 and $712,000.

Borrowing costs of $2,100,503 were incurred during the year. These borrowing costs were capitalised in the Tajikistan segment ($1,387,702), Kazakhstan segment($356,173) and Uzbekistan segment ($154,270). The remaining $202,358 was expensed through the statement of comprehensive loss.

Amortisation of $1,106,830 of assets held in the Corporate segment were capitalised in Kazakhstan: $460,451 and Tajikistan: $646,379.

(tabular amounts in thousands of US dollars)

Segment results for the year ended December 31, 2008 are as follows:

	Kazakhstan	Tajikistan	Uzbekistan	Other and Corporate	Consolidated
	$	$	$	$	$
Gas sales	5,360	-	-	-	5,360
Refined product sales	-	-	-	-	-
Other income	4,210	-	-	2,115	6,325
Segment revenue	**9,570**	**-**	**-**	**2,115**	**11,685**
Inter-segment revenue	(4,210)	-	-	(2,115)	(6,325)
Revenue from external customers	**5,360**	**-**	**-**	**-**	**5,360**
Loss before taxation	**(9,450)**	**(629)**		**(12,105)**	**(22,184)**
Taxation	-	-	-	-	-
Net loss attributable to shareholders	**(9,450)**	**(629)**	**-**	**(12,105)**	**(22,184)**

Sales in the Kazakhstan segment were made to a single customer.

No borrowing costs incurred on loans within the Corporate segment were capitalised between segments.

No amortisation of assets held in the Corporate segment were capitalised between segments.

The segment assets and liabilities as at December 31, 2009 and capital expenditures for the year then ended are as follows:

	Kazakhstan	Tajikistan	Uzbekistan	Other and Corporate	Consolidated
	$	$	$	$	$
Total assets	72,152	21,984	11,015	31,931	137,082
Total liabilities	1,914	3,759	6,992	17,813	30,478
Cash expenditure on exploration & evaluation assets, property, plant and equipment	8,553	16,942	3,709	3,017	32,221
Depreciation, depletion & amortization	2,497	138	603	-	3,238

Total assets for Tajikistan include the Company's investment in the joint venture (note 15).
Included in Kazakhstan liabilities are payables in relation to exploration and evaluation assets of $411,202.

The segment assets and liabilities at December 31, 2008 and capital expenditures for the year ended December 31, 2008 are as follows:

	Kazakhstan $	Tajikistan $	Uzbekistan $	Other and Corporate $	Consolidated $
Total assets	68,240	2,801	-	42,507	113,548
Total liabilities	1,844	154	-	7,820	9,818
Cash expenditure on exploration & evaluation assets, property, plant and equipment	21,604	2,633	-	18,570	42,807
Depreciation, depletion & amortization	4,182	51	-	100	4,333

Included in Kazakhstan liabilities are payables in relation to exploration and evaluation assets of $33,618.

The segment assets and liabilities at January 1, 2008 are as follows:

	Kazakhstan $	Tajikistan $	Uzbekistan $	Other and Corporate $	Consolidated $
Total assets	50,737	207	-	28,902	79,846
Total liabilities	2,321	-	-	1,784	4,105

The segment assets attributable to the Kazakhstan segment consist mainly of capital additions related to the Kyzyloi and Akkulka fields, including the installation of pipelines linking these fields to the Bhukara-Urals trunk line, as well as the costs of exploration pending determination of the Kul-Bas field.

The segment assets attributable to the Tajikistan segment consist of the costs of exploration pending determination of the Tajikistan production sharing contract.

The segment assets attributable to the Uzbekistan segment consist mainly of well costs related to the North Urtabulak field. These other intangible assets have been recognized at provisional fair value as described in note 21.

The other and corporate segment assets consist mainly of oil and gas equipment such as drilling rigs and related equipment and cash and cash equivalents. The other and corporate segment liabilities consist mainly of the loans obtained to finance the purchase of two drilling rigs, more fully disclosed in note 17.

(tabular amounts in thousands of US dollars)

6 Revenue

	Year ended	
	December 31, 2009 $	**December 31, 2008 $**
Gas sales	3,828	5,360
Refined product sales	4,731	-
	8,559	5,360

Revenue has been grossed up for non-monetary transactions, namely marketing commission of $141,426 (2008: nil) and utility services of $752,807 provided with respect to Uzbekistan (2008: nil). The corresponding expenses are shown within administrative and production expenses respectively.

7 Administrative expenses

Administrative expenses by nature	Year ended	
	December 31, 2009 $	**December 31, 2008 $**
Staff expenses	5,469	4,517
Share-based payments	2,628	4,419
Travel expenses	2,590	3,099
Professional fees	1,909	1,695
Office costs	1,835	2,311
Other administrative expenses	2,449	1,874
	16,880	17,915

Key management personnel have been identified as the board of directors and eight senior managers. Details of key management remuneration are shown in note 23.

8 Share-based payments

The Company has adopted a stock incentive plan referred to as the “2007 Long Term Stock Incentive Plan” pursuant to which the Company may grant stock options to any director, employee or consultant of the Company, or any subsidiary or Vazon Energy Limited (collectively, “Service Providers”).

The maximum number of Ordinary Shares reserved for issuance under the plan equals 12% (2008 – a specific number of shares: 7,511,670) of the outstanding Ordinary Shares. The plan is administered by the Compensation and Nomination Committee of the Board of Directors. Options may be granted pursuant to recommendations of the Compensation and Nomination Committee. The Compensation and Nomination Committee may determine the vesting schedule and term, provided that options may not have a term exceeding ten years. Subject to any resolution passed by the Compensation and Nomination Committee, options will terminate three months after an option holder ceases to be a Service Provider.

The exercise price of options granted under the plan may not be less than the closing price of Ordinary Shares on the principal stock exchange where the Ordinary Shares are listed as of the date of the option grant. The plan contains amendment provisions which allow amendments to the plan by the Board of Directors, without shareholder approval, for amendments of a "housekeeping" nature, changes to vesting or termination provisions, and discontinuance of the plan. The plan also provides that outstanding options will vest immediately on the occurrence of a "change of control" (as defined in the plan). Options granted under the plan are only assignable to certain related entities of an option holder or otherwise with the consent of the Company.

Under the plan, the options vest in three tranches with one third vesting immediately, one third after one year and one third after two years. These options are equity settled share based payment transactions.

Stock options

The following table summarizes the stock option activity under the 2007 Long Term Stock Incentive Plan.

	Number of options	**Weighted average exercise price $**
Outstanding at January 1, 2008	4,497,000	2.76
Granted	2,274,000	2.51
Forfeited	(96,000)	2.75
Exercised	-	n/a
Expired	-	n/a
Outstanding at December 31, 2008	6,675,000	2.67
Exercisable at December 31, 2008	3,692,000	2.71
Outstanding at January 1, 2009	6,675,000	2.67
Granted	5,808,000	0.71
Forfeited	(281,000)	0.94
Exercised	-	n/a
Expired	(496,000)	2.43
Outstanding at December 31, 2009	11,706,000	1.75
Exercisable at December 31, 2009	7,325,666	2.20

(tabular amounts in thousands of US dollars)

The following table lists the options outstanding at December 31, 2009 by exercise price.

	Exercise price $	Options outstanding	Weighted average remaining term (in years)	Options exercisable	Weighted average remaining term (in years)
	0.60	5,056,000	4.72	1,685,333	4.68
	0.88	120,000	4.84	40,000	4.84
	2.50	2,330,000	5.58	1,443,333	5.53
	2.75	4,182,000	4.53	4,139,000	4.52
	3.18	18,000	4.93	18,000	4.93
Total		11,706,000	4.81	7,325,666	4.76

The fair value of the liability is estimated using the Black-Scholes pricing model using the following average assumptions:

	December 31, 2009	December 31, 2008
Weighted average fair value	$0.2841	$1.5493
Risk free rate	1.74%	3.32%
Expected term	3 years	4 years
Volatility	97.9%	73.5%
Dividend	Nil	Nil
Weighted average share price	$0.51	$2.66

In estimating expected volatility, the Company considers the historical volatility of the share price of similar entities over the most recent period that is commensurate with the expected option term.

(tabular amounts in thousands of US dollars)

Warrants

The following table summarizes the warrant activity for the year ended December 31, 2009.

	Number of warrants	**Weighted average exercise price $**
Outstanding at January 1,2008	10,203,658	4.73
Granted	1,433,298	2.33
Forfeited	-	n/a
Exercised	-	n/a
Expired	-	n/a
Outstanding at December 31, 2008	11,636,956	4.43
Exercisable at December 31, 2008	11,636,956	4.43
Outstanding at January 1, 2009	11,636,956	4.44
Granted	2,500,000	0.60
Forfeited	-	n/a
Exercised	-	n/a
Expired	(1,353,501)	4.13
Outstanding at December 31, 2009	12,783,455	3.73
Exercisable at December 31, 2009	12,783,455	3.73

During the year ended December 31, 2009, there were 2,500,000 (2008 – 1,433,298) warrants issued in connection with loan financing (note 17.2).

Of the warrants outstanding at the beginning of the year, 8,857,504 relate to warrants granted to the Company's executive officers. 7,504,003 of these warrants remain outstanding and exercisable at December 31, 2009.

There are no performance conditions attached to the warrants and all the granted warrants were immediately vested. Warrants are equity settled share based payment transactions.

In estimating expected volatility, the Company considers the historical volatility of the share price of similar entities over the most recent period that is commensurate with the expected warrant term.

(tabular amounts in thousands of US dollars)

The following table lists the warrants outstanding at December 31, 2009 by exercise price.

Exercise price $	Warrants outstanding	Weighted average remaining term (in years)	Warrants exercisable	Weighted average remaining term (in years)
1.25	638,298	1.94	638,298	1.94
2.50	3,436,154	8.82	3,436,154	8.82
3.25	795,000	1.20	795,000	1.20
5.50	2,255,835	1.49	2,255,835	1.49
6.88	3,158,168	2.99	3,158,168	2.99
0.60	2,500,000	0.96	2,500,000	0.96
Total	12,783,455	3.73	12,783,455	3.73

As at December 31, 2009, there was no unrecognized compensation expense related to unvested warrants.

9 Taxation

Tethys is domiciled in the Cayman Islands which has no Company income tax.

At December 31, 2009, in Kazakhstan the Company had $10.3 million (2008 $4.1 million) and in Uzbekistan $2.0 million (2008 $2.2 million) of tax carry – forward losses, that would be available to offset against any future taxable profit. No deferred tax asset has been recognised in respect of $10.3 million of losses in Kazakhstan (2008 - $4.1 million). In 2009 the Company has not been able to utilise any of the losses in Kazakhstan, previously unrecognised, through the statement of comprehensive loss. Of the $10.3 million losses in Kazakhstan with no deferred tax asset, substantially all expire in various amounts from 2012 to 2016. Uzbekistan tax carry - forward losses of $2.0 million have no fixed expiry date.

The temporary differences comprising the net deferred income tax liability as at December 31, 2009 are as follows:

	December 31, 2009 $
Capital assets	(1,078)
Tax losses	325
Other	155
Net deferred tax liability	(598)

(tabular amounts in thousands of US dollars)

The provision for income taxes is different from the expected provision for income taxes for the following reasons:

	$
Loss before income taxes	(21,506)
Income tax rate	20%
Expected income tax expense (recovery)	(4,301)
Increase (decrease) resulting from:	
Non-deductible expenses	535
Impact of effective tax rates in other foreign jurisdictions	2,616
Rate reduction on future income taxes	139
Losses and tax assets not utilised/recognised	1,155
Other	70
	214
Current income tax expense (recovery)	-
Deferred tax expense (recovery)	214
	214

10 Loss per share

Basic and diluted loss per share

	Loss for the year $	Weighted average number of shares (thousands)	Per share amount $
Year ended December 31, 2009			
Loss attributable to ordinary shareholders – Basic and diluted	(21,720)	106,450	(0.20)
Year ended December 31, 2008			
Loss attributable to ordinary shareholders – Basic and diluted	(22,184)	55,988	(0.40)

Basic loss per share is calculated by dividing the loss attributable to shareholders of the Company by the weighted average number of ordinary shares in issue during the year. Diluted per share information is calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares. Potential ordinary shares including share options and warrants, are considered to be anti-dilutive and have therefore been excluded from the diluted per share calculation.

Subsequent to the year end, the Company issued further shares as disclosed in note 22.

(tabular amounts in thousands of US dollars)

11 Intangible assets

	Other intangible asset $	Exploration and evaluation assets $	Total $
At January 1, 2008			
Cost	-	7,335	7,335
Accumulated amortisation and impairment	-	-	-
Net book amount	-	7,335	7,335
Year ended December 31, 2008			
Opening net book amount	-	7,335	7,335
Additions	-	10,622	10,622
Amounts written off to exploration and evaluation costs	-	(1,852)	(1,852)
Amortisation charge	-	-	-
Closing net book amount	-	16,105	16,105
At December 31, 2008			
Cost	-	16,105	16,105
Accumulated amortisation and impairment	-	-	-
Net book amount	-	16,105	16,105
Year ended December 31, 2009			
Opening net book amount	-	16,105	16,105
Additions through acquisition of subsidiary	5,553	-	5,553
Additions	-	23,289	23,289
Disposal of subsidiaries at book amount	-	(19,176)	(19,176)
Amounts written off to exploration and evaluation costs	-	(887)	(887)
Amortisation charge	(506)	-	(506)
Closing net book amount	5,047	19,331	24,378
At December 31, 2009			
Cost	5,553	19,331	24,884
Accumulated amortisation and impairment	(506)	-	(506)
Net book amount	5,047	19,331	24,378
Asset retirement obligation asset at net book amount included in above			
At December 31, 2009	-	47	47
At December 31, 2008	-	126	126
At January 1, 2008	-	-	-

Borrowing costs of $1,387,000 (2008 – nil) have been capitalised within exploration and evaluation assets during the year. The effective weighted average interest rate of the relevant borrowings was 22% (2008 – nil). The

effective interest rate is higher than the nominal rate due to the cost of associated warrants (Note 17.2) and royalties (Note 17.3). For the year ended December 31, 2009 $779,389 (2008 - $371,716) was capitalised from administrative expenses.

12 Property, plant and equipment

	Oil and gas properties $	Oil and gas equipment $	Vehicles $	Office and computer equipment $	Total $
At January 1, 2008					
Cost	35,499	2,057	579	386	38,521
Accumulated depreciation	(143)	-	(19)	(32)	(194)
Net book amount	35,356	2,057	560	354	38,327
Year ended December 31, 2008					
Opening net book amount	35,356	2,057	560	354	38,327
Additions	12,495	17,983	809	581	31,868
Deletions	(440)	-	-	-	(440)
Depreciation charge	(3,969)	(72)	(168)	(124)	(4,333)
Closing net book amount	43,442	19,968	1,201	811	65,422
At December 31, 2008					
Cost	47,554	20,040	1,388	967	69,949
Accumulated depreciation	(4,112)	(72)	(187)	(156)	(4,527)
Net book amount	43,442	19,968	1,201	811	65,422
Year ended December 31, 2009					
Opening net book amount	43,442	19,968	1,201	811	65,422
Additions	6,908	4,853	98	155	12,014
Additions through acquisition of subsidiary	-	-	-	117	117
Disposal of subsidiaries at book amount	-	-	(162)	(140)	(302)
Depreciation charge	(2,823)	(1,033)	(117)	(107)	(4,080)
Closing net book amount	47,527	23,788	1,020	836	73,171
At December 31, 2009					
Cost	54,462	24,893	1,324	1,099	81,778
Accumulated depreciation	(6,935)	(1,105)	(304)	(263)	(8,607)
Net book amount	47,527	23,788	1,020	836	73,171

(tabular amounts in thousands of US dollars)

	Oil and gas properties $	Oil and gas equipment $	Vehicles $	Office and computer equipment $	Total $
Asset retirement obligation at net book amount included in above:					
At December 31, 2009	18	-	-	-	18
At December 31, 2008	175	-	-	-	175
At January 1, 2008	918	-	-	-	918

	Oil and gas properties $	Oil and gas equipment $	Vehicles $	Office and computer equipment $	Total $
Asset under construction at net book amount included in above					
At December 31, 2009	25,858	-	-	-	25,858
At December 31, 2008	23,251	3,210	-	-	26,461
At January 1, 2008	17,105	1,879	-	-	18,984

Assets under construction as at December 31, 2009 and December 31, 2008 includes the cost of developing the Akkulka concession and tie-in pipeline and are not being depreciated until commencement of production.

Borrowing costs of $513,000 have been capitalised to oil and gas properties in the current year (2008 - $712,000). The effective weighted average interest rate of the relevant borrowing was 19.58%, (2008 22.7 %). The effective interest rate is higher than the nominal rate due to the cost of associated warrants (note 17.2). For the year ended December 31, 2009 $438,584 (2008 - $41,239) was capitalised from administrative expenses.

13 Investments

	December 31, 2009 $	December 31, 2008 $	January 1, 2008 $
Restricted cash	659	587	318

Restricted cash at December 31, 2009, December 31, 2008, and January 1, 2008 consisted of interest bearing bank deposits held in Kazakhstan. These deposits have been placed to satisfy local Kazakhstan requirements in respect of asset retirement obligations.

(tabular amounts in thousands of US dollars)

14 Trade and other receivables

	December 31, 2009 $	December 31, 2008 $	January 1, 2008 $
Current			
Trade receivables	905	1,124	219
Prepayments	502	900	351
Other receivables	904	640	790
	2,311	2,664	1,360
Non-current			
Advances to construction contractors	333	1,514	3,062
Hong Kong Stock Exchange (HKSE) deferred offering costs	352	-	-
Value added tax receivable	4,486	4,843	2,752
	5,171	6,357	5,814
	7,482	9,021	7,174

Current trade and other receivables are unsecured and non-interest bearing. Normal payment terms for the Company are 30 days. Prepayments primarily relate to prepaid insurance and other corporate operating expense items.

Trade receivables of $905,000 (December 31, 2008 – $1,124,000) are more than thirty days past due but are not considered impaired. The other classes within trade and other receivables do not contain impaired assets.

Non-current advances to construction contractors relate to suppliers who were paid in advance for materials and services relating to both the Akkulka and the Kul-Bas contracts. For the Akkulka contract, the prepayments relate to the drilling of a new well and payments on compressors, pipes and associated construction work that will constitute phase two of the Company's gas production plan. For Kul-Bas the prepayment related primarily to the drilling of a new well.

15 Investment in Joint Venture

The Company has a 51% interest in a jointly controlled entity, Seven Stars Energy Corporation Limited (SSEC). On December 30, 2009 the Company transferred ownership of its three Tajik subsidiaries to SSEC. At December 31, 2009 the Company's investment in the joint venture was $nil.

The consideration received by Tethys' from SSEC was a note receivable in the amount of $21,727,000, which represents Tethys' book value of assets transferred plus an amount for certain costs previously expensed by Tethys' which are recoverable from SSEC.

This transaction resulted in a gain of $4,699,000, which has been deferred on the statement of financial position. This amount has been recorded as a reduction of the investment account in the amount of $1,040,000 (which has reduced the investment account to $nil as at December 31, 2009), with the remaining balance of

$3,659,000 being recorded as a deferred gain. The deferred gain will be recognised in the income when realised.

The following amounts represent the movements in the investment account during the year:

	December 31, 2009 $
Balance, beginning of year	-
Contributions	2,040
Share of losses from jointly controlled entity	(1,000)
Deferred gain on assets sold to jointly controlled entity	(1,040)
Balance, end of year	-

The following tables represent the assets and liabilities of the jointly controlled entity at the year end and its results for the year to December 31, 2009.

	December 31, 2009 $
Assets	
Non-current assets	24,173
Current assets	113
Total assets	24,286
Liabilities	
Non-current liabilities	(21,727)
Accruals	(519)
Total liabilities	(22,246)
Net assets	2,040

	December 31, 2009 $
Revenue	-
Expenses	(1,960)
Loss before tax	(1,960)
51% share of joint venture loss before tax	(1,000)

Commitments

On June 13, 2008, the Company's wholly owned subsidiary, Kulob Petroleum Limited ("KPL"), signed a Production Sharing Contract ("PSC") with the Government of the Republic of Tajikistan. Under the PSC, KPL will recover 100% of its costs from up to 70% of total production (the maximum allowed under the newly approved production sharing legislation of Tajikistan) and the remaining production (termed "Profit Oil and Gas") will be shared 70% to KPL and 30% to the Government whose share includes all taxes, levies and duties. The terms are fixed over the life of the PSC which is a minimum of 25 years.

Pursuant to the PSC, Tethys has committed to funding a work program designed to provide data for a focused exploration of the Contract Area and which will be carried out in two stages (the "Work Program"). The first phase of the Work Program will include geological studies, reprocessing of existing seismic and other geophysical data, acquisition of seismic and other geophysical data and the commencement of initial rehabilitation activities on the Beshtentak and Khoja Sartez fields. The minimum spend commitment under Phase 1 of the contract is US$3,000,000. This expenditure was required to be met within 18 months of the effective date of the contract, which is December 13, 2009. This commitment was satisfied through the payment on January 2, 2009 of $4,925,000 for a contract agreed on November 14, 2008 relating to a seismic survey work program.

The total cost of the seismic work program agreement is $9,850,600, which can be unilaterally terminated at any point by the Company with immediate repayment of amounts remitted in advance of the fulfilled scope of works at the moment of termination, provided the Contractor has reached Stage One Completion. By December 31, 2009, a total of $5,659,652 had been advanced (including the $4,925,000 above). Phase 2 of the seismic survey commenced in October 2009.

The Company's share of Phase 2 commitment is $2,137,383.

16 Cash and cash equivalents

	December 31, 2009 $	December 31, 2008 $	January 1, 2008 $
Cash at bank and in hand	6,788	19,868	983
Short-term deposits	509	2,332	25,709
	7,297	22,200	26,692

Cash at banks earn interest at floating rates based on daily bank deposit rates. Short term deposits are made for varying periods of between one day and three months, depending on the cash requirements of the Company, and earn interest at the respective short term deposit rates.

(tabular amounts in thousands of US dollars)

17 Financial liabilities

17.1 Borrowings

	Effective interest rate %	Maturity date	December 31, 2009 $	December 31, 2008 $	January 1, 2008 $
Current					
Short-term portion of long-term loans	19 – 23 p.a.	2010	1,086	853	-
Non-current					
Long-term loans	19 – 23 p.a.	2011	8,199	5,096	-
		2012	1,125	-	-
			10,410	5,949	-

Financial borrowings relate to financing arrangements that were put in place to fund the acquisition of the Telesto deep drilling rig (Telesto) and the Tykhe drilling rig (Tykhe) in 2008 and the drilling of a new well in Uzbekistan in 2009.

Principal repayments for the loans are as follows:

		Drilling rig loans $	Uzbekistan loans $	Total $
To December 31,	2010	1,464	-	1,464
	2011	4,577	4,100	8,677
	2012	-	1,136	1,136
Remaining principal payments		6,041	5,236	11,277
Less: unamortised debt discount		(503)	(364)	(867)
Balance, end of year		5,538	4,872	10,410
	Current	1,086	-	1,086
	Non-current	4,452	4,872	9,324

The loan to fund Telesto bears interest at a nominal rate of 12%. In addition 795,000 warrants to purchase Tethys shares at CAD$3.25 with a term of three years were issued to lenders. The fair value associated with the warrants issued has been recognised as a debt discount and presented as a direct reduction to the face value of the long-term debt, with the effective interest rate method being used to amortise the discount over the life of the loan. Lenders have security over the shares of Tethys Petroleum Inc. which has no other assets except the drilling rig. No corporate guarantees or security are being provided by Tethys.

The loan to fund Tykhe bears interest at a nominal rate of 15%. In addition 638,298 warrants to purchase Tethys shares at CAD$1.25 with a term of three years were issued to lenders. The fair value associated with

the warrants issued has been recognised as a debt discount and presented as a direct reduction to the face value of the long-term debt, with the effective interest rate method being used to amortise the discount over the life of the loan. Lenders have security over the shares of AOE Tykhe BV which has no other assets except the drilling rig and in addition a corporate guarantee is being provided by Tethys.

During the year the Company obtained a short term loan of $2,500,000 which was fully repaid by June 30, 2009. In connection with the loan financing, 2,500,000 warrants to purchase Tethys shares at CAD$0.60 with a term of 18 months were issued to lenders. The loan was initially measured at fair value and subsequently measured at amortized cost using the effective interest rate method. The fair value of $421,370 associated with the warrants issued has been fully amortised with the effective interest rate method during the year (note 17.2).

Based on the borrowing rates currently available to the Company for long term borrowings with similar terms and average maturities (22%), the fair value of the non-current financial borrowings in relation to the drilling rigs and new well in Uzbekistan approximates its carrying value.

On October 19, 2009 Tethys closed a loan financing for $4.1 million with a group of investors in connection with the drilling of a new well in Uzbekistan. A coupon of 10% per annum is due for the first two months, which is the expected drilling time of the well. Thereupon the lenders will receive 6% per annum coupon and 6.25% of the revenue received by BHCL from sales of the net production from the new well for every $1.0 million invested, calculated monthly and payable quarterly in arrears over a period of up to 24 months. If the well does not produce the investor will receive only the 6% per annum coupon on the funds invested.

On December 14, 2009 in connection with the drilling of the above new well in Uzbekistan the Company further approved the issue of loan notes to a maximum value of $3,000,000 at an issue rate of $0.88 per note and redemption value of $1, resulting in an effective rate of 6.5%. By December 31, 2009, $1,000,000 loan notes had been placed. A royalty of 11.25% is payable to the loan note holders calculated on sales of net production from the new well. The royalty entitlement was identified as an embedded derivative and required to be separated from the loan note. The royalty entitlement has been accounted for as a derivative financial instrument – interest rate swap. Refer to note 17.

Issue of the loan notes was completed via a broker to whom a royalty commission is payable at 4.5% for every $1.0 million placed. The fair value of the commission payable at December 31, 2009 was $42,333. The Company measured the fair value of the commission payables by applying a valuation technique based on the discounted estimated future net cash flows expected to be derived from the royalty entitlement. A discounted cash flow (DCF) method requires management to estimate future cash flows associated with the instrument and then discount those amounts to present value at a rate of return that considers the relative risk of the cash flows (5%). The fair value associated with the royalty entitlement has been recognised as a transaction cost and presented as a direct reduction to the face value of the borrowing with the effective interest rate method being used to amortise the cost over the life of the loan. The commission liability has been included in current trade and other payables.

17.2 Derivative financial instrument - warrants

	December 31, 2009 $	December 31, 2008 $	January 1, 2008 $
Balance, beginning of year	146	-	-
Issued during the year	422	1,163	-
Fair value loss / (gain)	485	(929)	-
Adjustment	-	(88)	-
Balance, end of year	1,053	146	-

The warrant liability represents the financial liability relating to share warrants that are denominated in a currency that is not the Company's functional currency. These warrants were issued in connection with the two rig loans described in note 17.1.

The liability was initially recognised at fair value. As the warrants are denominated in foreign currency, there is a written option for the holder to exchange the foreign currency denominated warrant for a fixed number of functional currency denominated shares. This option is a derivative financial instrument and was initially recognised at fair value and subsequently measured at fair value through income.

The fair value of the liability is estimated using the Black-Scholes pricing model using the following average assumptions:

	December 31, 2009	December 31, 2008
Weighted average fair value	$0.29	$0.15
Exercise price	$1.24	$3.25
Risk free rate	1.46%	2.41%
Expected term	1.18 years	2.56 years
Volatility	87%	85%
Dividend	Nil	Nil

17.3 Derivative financial instruments - interest rate swap

The interest rate swap represents the derivative financial instrument entered into in connection with the Uzbekistan loan financing disclosed in note 17.1 completed in the year. This instrument is a derivative financial instrument and was initially recognised at fair value and subsequently measured at fair value through income. The Company measured the fair value of the liability by applying a valuation technique based on the discounted estimated future net cash flows expected to be derived from the instrument. A discounted cash flow (DCF) method requires management to estimate future cash flows associated with the instrument and then discount those amounts to present value at a rate of return that considers the relative risk of the cash flows (5%).

(tabular amounts in thousands of US dollars)

	December 31, 2009 $	December 31, 2008 $
Balance, beginning of year	-	-
Derivative financial instrument	101	
Gain recognised in the statement of comprehensive loss	(6)	-
Balance, end of year	95	-

18 Trade and other payables

	December 31, 2009 $	December 31, 2008 $	January 1, 2008 $
Current			
Trade payables	4,236	1,117	1,183
Accruals	1,997	414	643
Payables to related parties	35	489	453
Other creditors	518	715	-
	6,786	2,735	2,279
Non-current			
Other non-current payables	808	523	776

Trade payables are non-interest bearing and are normally settled on 30 day terms. Accruals represent mainly fees outstanding to the drilling contractor in Uzbekistan, drilling related fees in Tajikistan and professional fees. Other current creditors consist mainly of local taxes in the Republic of Kazakhstan and the current portion of the Kyzyloi historical costs. All current trade and other payables are interest free and payable within 12 months.

Included within other non-current payables are accruals for historical costs due to the Government of Kazakhstan on the Kyzyloi and Akkulka contracts in Kazakhstan.

Kyzyloi

The principal amount outstanding at December 31, 2009 was $735,053 (2008 – $908,098) and this is to be repaid in quarterly instalments by March 2014. The liability is non-interest bearing. The liability is measured at amortised cost using the effective interest rate method. The net present value of liability using an assumed rate of interest of 10% (2008 – 10%) is $510,455 (2008 – $680,000) of which $101,955 (2008 – $157,000) is current, leaving a non-current balance of $408,500 (2008 – $523,000). The fair value of the liability approximates its carrying value, (2008 - $508,441).

Akkulka

Upon signature of the Akkulka gas production contract on December 23, 2009, the historical cost liability in relation to this field became due. The principal amount outstanding at December 31, 2009 was $933,997 and this is to be repaid in quarterly instalments by June 2018. The liability is non-interest bearing. The liability is measured at amortised cost using the effective interest rate method. The net present value of liability using an

assumed rate of interest of 22% is $414,437 of which $19,581 is current, leaving a non-current balance of $394,856.

Based on the borrowing rates currently available to the Company for loans with similar terms and average maturities, the fair value of the non-current liability relating to historic costs approximates its carrying value.

Principal repayments for both contracts are as follows:

		$
To December 31,	2010	283
	2011	283
	2012	283
	2013	283
	2014	283
	2015 and thereafter	260
Remaining principal payments		1,675
Less: unamortised debt discount		(745)
Balance, end of year		930
	Current	122
	Non-current	808
		930

19 Asset retirement obligations

	Year ended December 31, 2009 **$**
At January 1, 2009	465
Additional obligations incurred	77
Change in estimated cash flow	(358)
Unwinding of discount due to passage of time	22
At December 31, 2009	206

The Company makes provision for the future cost of decommissioning oil and gas production facilities and pipelines on a discounted basis. These costs are expected to be incurred between 2012 and 2022. The provision has been estimated using existing technology at current prices, escalated at 10% (2008 – 10%) and discounted at 11% (2008 – 11%). The economic life and the timing of the asset retirement obligation are dependent on Government legislation, commodity price and the future production profiles of the project. In addition, the estimated cash outflows are subject to inflationary and/or deflationary pressures in the cost of third party service provision.

20 Share capital

	December 31, 2009 Number	December 31, 2008 Number	January 1, 2008 Number
Authorized			
Ordinary shares with a par value of $0.10 each	700,000,000	700,000,000	500,000,000
Preference shares with a par value of $0.10 each	50,000,000	50,000,000	-

Ordinary equity share capital	Number	Share capital	Share premium
Allotted and fully paid		$	$
At January 1, 2008	45,116,696	4,511	94,972
Issued during the year for cash	21,276,596	2,128	43,626
At December 31, 2008	66,393,292	6,639	138,598
At January 1, 2009	66,393,292	6,639	138,598
Issued during the year for purchase of oil and gas equipment	1,400,000	140	701
Issued during the year in connection with finance charges	81,477	8	226
Issued during the year for purchase of a subsidiary	15,000,000	1,500	1,487
Issued during the year for cash	51,680,000	5,168	12,736
At December 31, 2009	134,554,769	13,455	153,748

The preference shares have the rights as set out in the Memorandum and Articles of Association approved at the AGM on April 24, 2008. Significant terms related to preference shares are summarised below:

- May be issued in one or more series;
- Are entitled to any dividends in priority to the ordinary shares;
- Confer upon the holders thereof rights in a winding-up priority to the ordinary shares;
- And may have such other rights, privileges and conditions (including voting rights) as the Board may determine prior to the first allotment of any series of preference shares, provided that if a series of preference shares has no or limited voting rights it shall be designated as such by the Board.

On January 13, 2009, 1,400,000 ordinary shares were issued to a supplier as partial consideration for the purchase of a coil tubing unit. The fair value of the shares issued was determined by reference to the fair value of the goods received at the measurement date.

On April 9, 2009, the Company issued 15,000,000 ordinary shares to Rosehill Energy Limited as consideration for the acquisition of its wholly owned subsidiary. Details of this transaction are disclosed in note 21.

On April 27, 2009, the Company issued 81,477 ordinary shares to Kraken Financial Group Limited, a related party, as consideration for services rendered in connection with the placement of shares of the Company in 2008. The fair value of the shares issued was determined by reference to the fair value of the services received at the measurement date.

On June 19, 2009, the Company issued 51,680,000 ordinary shares for consideration of $17,906,000, net of transaction costs.

As at December 31, 2009 a total of 24,489,455 (December 31, 2008 – 18,311,596) ordinary shares are reserved under the Company's Long Term Stock Incentive Plan and Warrants granted by the Company. Details of the options and warrants are given in note 8.

There are currently no preference shares outstanding (2008 – None).

21 Business combination

On April 9, 2009 the Company acquired 100% of the issued share capital in Baker Hughes (Cyprus) Limited (BHCL), a Company incorporated in Cyprus, which operates under a production enhancement contract relating to the North Urtabulak field in Uzbekistan. Tethys issued 15,000,000 ordinary shares as purchase consideration in the acquisition. The acquisition agreement places a trading restriction on the shares as follows: 7,500,000 cannot be resold until 6 months from the date of issue and the remaining 7,500,000 cannot be resold until 12 months from the date of issue.

The acquired business contributed revenues of $4,731,000 and a net profit before taxation of $477,000 to the Company for the period from April 9, 2009 to December 2009 (note 5). If the acquisition had occurred on January 1, 2009 the revenue of the Company would have been $1,017,371 higher (unaudited) and the net profit before taxation would have been $112,000 higher (unaudited). These amounts have been calculated using the Company's accounting policies and by adjusting the results of the subsidiary to reflect the additional depreciation and amortization that would have been charged assuming the fair value adjustments to property, plant and equipment and intangible assets had applied from January 1, 2009.

The fair value of the shares issued was based on the published price of the shares on the date of acquisition. As the shares were issued with a trading restriction, this resulted in a marketability discount being applied to the published price to arrive at fair value. The marketability discount was valued using the Black Scholes Option Pricing Model using the following assumptions: dividend yield of 0%; expected term of 0.75 years; a risk free interest rate of 0.60% and expected volatility of 121%. This resulted in an adjustment of $2,344,484 to the purchase consideration.

The provisional fair values of identifiable assets and liabilities of BHCL as at the date of acquisition were:

	(Unaudited) Acquiree carrying value $	Preliminary provisional fair value $	As at December 31, 2009, provisional fair value $
Consideration at April 9, 2009			
Equity instruments (15,000,000 ordinary shares)		2,987	2,987
Direct costs related to the acquisition		57	57
Total consideration transferred		3,044	3,044
Recognised amounts of identifiable assets acquired and liabilities assumed			
Cash and cash equivalents	532	532	532
Trade and other receivables	502	502	-
Intangible asset	-	3,820	5,553
Property, plant and equipment	9,373	118	117
Inventory	-	-	753
Deferred revenue	-	-	(1,594)
Current trade and other payables	(1,928)	(1,928)	(1,933)
Deferred income tax liability	-	-	(384)
Total identifiable net assets	8,479	3,044	3,044

Assets and liabilities acquired in a business combination are required to be recognised at fair value. In the absence of an active market for the North Urtabulak Field Production Enhancement Contract, the Company measured the fair value of the asset by applying a valuation technique based on the discounted estimated future net cash flows expected to be derived from the asset. A discounted cash flow (DCF) method requires management to estimate future cash flows associated with the asset and then discount those amounts to present value at a rate of return that considers the relative risk of the cash flows.

Changes recognised in the provisional fair value balances during the year were due to new information obtained about facts and circumstances that existed as of the acquisition date which, if known, would have affected the measurement of the amounts at that date.

The fair value of the acquired assets relating to the Production Enhancement Contract (PEC) for the North Urtabulak field of $5,553,000 is provisional pending completion of the final valuation report for those assets.

There were no business combinations in the year ended December 31, 2008.

22 Events occurring after the reporting period

On November 9, 2009, Tethys announced its submission of a Form A1 listing application to the Hong Kong Stock Exchange (HKSE) with respect to a possible secondary listing of its ordinary shares on the main board of the HKSE estimated to be completed in the first half of 2010. No definite timetable nor the amount of any placement has yet been finalised and there is no guarantee that the Company's application will be successful.

On December 19, 2009 the Company entered into agreements for a non-brokered private placement of 10,000,000 Ordinary Shares for gross proceeds of US$5 million subject to regulatory approval. The sum of $3,750,000 was received on December 22, 2009 with the balance of $1,250,000 received on January 7, 2010. The Ordinary Shares were placed at a price of US$0.50 (CAD$0.53) each. The placements were completed on January 4, 2010.

On January 11, 2010 the Company further announced that it would complete a non-brokered private placement of 12,615,000 Ordinary Shares for gross proceeds of US$10 million subject to regulatory approval. The Ordinary Shares were placed at a price of CAD$0.82 (US$0.79) each. The placement was completed on January 25, 2010.

On February 4, 2010 the Company placed an additional $2 million in loan notes approved by the Company on December 10, 2009 (Note 17.1). These loan notes were in connection with the drilling of the new well in Uzbekistan.

On February 12, 2010 the Company announced an additional private placement of 30,000,000 Ordinary Shares for gross proceeds of CAD$46.5 (US$45.1) million. The Ordinary Shares were placed at an average price of CAD$1.55 (US$0.79) (US$1.50) each. The placement was completed on March 1, 2010.

On February 15, 2010 the Ministry of Energy and Mineral Resources of the Republic of Kazakhstan confirmed its approval of the transfer of 100% of the participatory interest of TethysAralgas LLP in the charter capital of Kul-Bas LLP in favour of its parent Company, Tethys Kazakhstan Limited.

(tabular amounts in thousands of US dollars)

23 Related party transactions

All subsidiaries, as listed below, have been consolidated into the consolidated accounts. A list of the investments in subsidiary undertakings (all of whose operations comprise one class of business, being Oil and Gas Exploration, Development and Production), including the name, proportion of ownership interest, country of operation and country of registration, is given below.

	Percentage	Country of operation	Country of registration
Tethys Uzbekistan BV	100%	Netherlands	Netherlands
Tethys Petroleum Inc.	100%	USA	USA
Tethys Afghanistan Inc.	100%	Dormant	USA
Tethys Kazakhstan Limited	100%	Guernsey	Guernsey
Tethys Aral Gas LLP	100%	Kazakhstan	Kazakhstan
Kul-Bas LLP	100%	Kazakhstan	Kazakhstan
Tethys Munai Gaz LLP	100%	Dormant	Kazakhstan
Tethys Services Kazakhstan LLP	100%	Kazakhstan	Kazakhstan
Asia Oilfield Equipment BV	100%	Kazakhstan/ Tajikistan	Netherlands
Tethys Europa BV	100%	Dormant	Netherlands
AOE Telesto BV	100%	Dormant	Netherlands
AOE Tyke BV	100%	Dormant	Netherlands
AOE Tyke SA	100%	Dormant	Luxemburg
Tethys Services Limited	100%	United Kingdom	United Kingdom
Tethys Caspian Limited	100%	Dormant	Cyprus
Tethys Tajikistan Limited	100%	Tajikistan	Jersey
Imperial Drilling Services Limited	100%	Cayman Islands	Cayman Islands
Seven Stars Energy Corporation	51%	Tajikistan	BVI
Tethyda Limited	100%	Dormant	Cyprus
Baker Hughes (Cyprus) Limited	100%	Uzbekistan	Cyprus
Rosehill Energy Limited	100%	Uzbekistan	Cayman Islands

The Company has an indirect shareholding of the following companies through its share of Seven Stars Energy Corporation:

Tethys Services Tajikistan Ltd.	51%	Tajikistan	Tajikistan
Kulob Petroleum Ltd.	51%	Tajikistan	Jersey
Sogdiana Petroleum Ltd.	51%	Tajikistan	Cayman Islands

Other

Vazon Energy Limited ("Vazon") is a corporation organized under the laws of the Bailiwick of Guernsey, of which Dr. David Robson, Chief Executive Officer, is the sole owner and managing director. Tethys has a management services contract with Vazon that came into effect from June 27, 2007 whereby the services of Dr.

Robson and other Vazon employees are provided to the Company. The total cost charged to Tethys for services from Vazon in the year ended December 31, 2009 was $1,677,113 (2008 – $1,405,028).

Oilfield Production Consultants (OPC) Limited and Oilfield Production Consultants (OPC) USA LLC, both of which have one common director with the Company, has charged Tethys a monthly retainer fee for engineering expertise, provided services relating to the optimization of the existing compressors and those to be installed as part of Phase 2 gas production from Akkulka, and has consulted on certain reservoir modelling work on projects in Tajikistan and Uzbekistan. Total fees for the year ended December 31, 2009 were $497,697 (2008 – $422,770).

Kraken Financial Group (KFG) had a common director with the Company up until 1 September 2009. In 2008, KFG was engaged by the Company to assist in obtaining loan financing in relation to the purchase of both Telesto and Tykhe drilling rigs. As a result of the services provided in connection with the Telesto transaction, KFG received 6% commission of the funds it was responsible for introducing to the Company. This commission was to be taken in the form of 81,477 shares, which were issued in 2009 amounting to $234,000 (which had been recognized as a liability at the end of 2008). No further services were provided by KFG during 2009 (December 31, 2008 - $21,000).

During the year ended December 31, 2008, KFG had acted as broker for Tethys in the placement of various insurance policies, including Directors and Officers, for which the combined annual premiums were $112,615. This service was not provided in 2009.

The remuneration of the key management personnel of the Company, which includes both directors and other officers, is set out below in aggregate.

	Year ended	
	December 31, 2009	**December 31, 2008**
Salaries and short-term employee benefits	3,026	2,926
Share-based payments	2,071	3,062
	5,097	5,988

Transactions with affiliates or other related parties including management of affiliates are recorded at their exchange amount.

(tabular amounts in thousands of US dollars)

24 Changes in working capital

	Year ended December 31, 2009	December 31, 2008
Trade and other receivables	353	(1,304)
Inventories	(2,155)	(213)
Trade and other payables	4,051	456
Change in non-cash working capital	2,249	(1,061)
Non-cash transactions	(2,136)	-
Net changes in non-cash working capital	113	(1,061)

The principal non-cash transaction is related to the issue of shares as consideration for the acquisition discussed in note 21.

Net changes in non-cash working capital are categorized as follows:

	Year ended December 31, 2009	December 31, 2008
Operating activities	(1,160)	(844)
Investing activities	1,273	(217)
Balance	113	(1,061)

25 Commitments and contingencies

Kazakhstan

Kyzyloi Field and the Kyzyloi Field Licence and Production Contract

The Kyzyloi Field Licence and Production Contract for production of gas on the Kyzyloi Field was initially issued by the Kazakh government to the state holding Company Kazakhgas on June 12, 1997 and was transferred to Tethys Aral Gas (TAG) on May 15, 2001. The contract was entered into between the MEMR and TAG on May 5, 2005, initially until June 12, 2007. However, in January 2005, the Ministry of Energy and Mineral Resources (MEMR) agreed to extend the contract until June 2014. Gas production commenced under the contract in December 2007.

The Kyzyloi Field Licence and Production Contract grants TAG exploration and production rights over an area of approximately 70,967 acres (287.2 km^2) and extends down to the base of the Paleogene sequence. Pursuant to the contract, TAG must reimburse the Kazakh government for approximately $1,211,000 in historical costs,

to be paid in equal quarterly instalments from the commencement of production until full reimbursement. Under the latest extension of the Kyzyloi Field Licence and Production Contract, TAG has committed to spending approximately $2.7 million for a workover program over the seven year period until 2014. In November 2009, the Company finalised and agreed the 2010 work program with a commitment of $100,000.

Akkulka Exploration Licence and Contract

The Akkulka Exploration Licence and Contract was entered into between the Kazakh State Committee of Investments and TAG on September 17, 1998. The Akkulka Exploration Licence initially granted TAG exploration rights for a period of five years and both the Akkulka Exploration Licence and Contract were valid until September 17, 2003. On December 9, 2009, TAG entered into an amendment agreement with the MEMR to extend the period of the Akkulka Exploration Licence and Contract from September 17, 2009 until March 10, 2011. Under the amendment agreement, TAG has committed to spending an additional $850,000 over the 18 month period and the 2010 work program for Akkulka was agreed with a capital commitment of $676,700.

Akkulka Production Contract

On December 23, 2009, TAG and MEMR signed the Akkulka Production Contract giving TAG exclusive rights to produce gas from the Akkulka Block for a period of nine years. Contingent upon commencement of commercial production on the Akkulka contractual territory, a total amount of US$3,500,000 will be due to the Kazakhstan Government as a reimbursement of historical costs previously incurred by the Government in relation to the contractual territory. For that part of the contractual territory from which production will commence in 2010 staged payments over a period of nine years totalling approximately $933,997 will also be due to the Kazakh government for the reimbursement of historical costs (note 18). The 2010 minimum work program was agreed with a capital commitment of $141,400.

Kul-Bas Exploration and Production Contract

The Kul-Bas Exploration and Production Contract was signed between Kul-Bas and the MEMR on November 11, 2005. This contract, which is for a period of 25 years (unless extended by mutual agreement of the parties), with an initial six-year exploration period and a 19-year production period, grants Kul-Bas with exploration and production rights over an original 2,688,695 acres (10,881 km^2) surrounding the Akkulka Block. Pursuant to the original contract, 20% of the area was to be relinquished at the end of the second year of the contract, with 20% to be relinquished annually thereafter up to the end of the six year exploration period. However, in response to an application on behalf of the Company, on April 27, 2009, Amendment 1 to the Kul-Bas Exploration and Production Contract was signed, according to which 20% is relinquished by the end of contract year 2 (completed), 0% in contract year 3 (2008), 10% by the end of contract year 4 (2009), 20% by the end of year 5 (2010) and all remaining contract area, outside commercial discovery areas, by the end of year 6 (2011).

The work program on this area amounted to a total of approximately $7,773,500 over the initial six-year exploration period. The remaining commitment of $2,894,000 relating to the contractual territory is required to be satisfied by November 11, 2011 and is included within the 2010 work program of $3 million which is outlined for one new 4,000 meters exploration well. In addition to the minimum work program commitments, the Kazakhstan Government is to be compensated for the historical costs related to the contractual territory in the amount of US$3,275,780. The Company has previously paid an amount of US$49,137 in relation to this balance. If and when commercial production commences, US$88,666 is due in quarterly instalments until the remaining historical costs of US$3,226,643 has been paid in full.

(tabular amounts in thousands of US dollars)

Tajikistan

Per *Note 15 Investment in Joint Venture* above the Company's share of seismic contract commitment is $2,137,383.

Uzbekistan

In connection with the drilling of a new well (NU116), the Company entered into a Turnkey contract with a fixed commitment of $3,943,976, of which $2,071,988 had been paid prior to the year end. The outstanding balance of $1,871,988 would be paid upon completion of the well which was anticipated to be February 2010.

Operating leases

Operating leases consist primarily of leases for offices. Lease commitments are as follows:

	Total $	Less than 1 year $	1 – 3 years $
Operating leases	779	415	364

2009 expenditure on lease commitments included in the statement of comprehensive loss amounted to $480,552, (2008 - $801,213).

26 Explanation of transition to IFRS

The consolidated financial statements for the year ended December 31, 2009 are the Company's first financial statements prepared under IFRS. For all accounting periods prior to this, the Company prepared its financial statements under generally accepted accounting principles in the United States of America ('US GAAP'). In accordance with IFRS 1 'First time adoption of IFRS', certain disclosures relating to the transition to IFRS are given in this note. These disclosures are prepared under IFRS as set out in the basis of preparation in note 2.

IFRS 1 allows first time adopters to IFRS to take advantage of a number of voluntary exemptions from the general principal of retrospective restatement. The Company has taken the following exemptions:

IFRS 3 Business combinations

This standard has not been applied to acquisitions of subsidiaries that occurred before January 1, 2008, the Company's transition date.

IFRIC 1 Changes in existing decommissioning, restoration and similar liabilities

The Company has elected to apply exemption from full retrospective application of Asset retirement obligations as allowed under IFRS 1. As such the Company has re-measured the provisions as at January 1, 2008 under IAS 37, estimated the amount to be included in the cost of the related asset by discounting the liability to the date at which the liability first arose using best estimates of the pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation, and recalculated the accumulated depreciation, depletion and amortisation under IFRS.

(tabular amounts in thousands of US dollars)

26.1

	Notes	Reconciliation of equity as at January 1, 2008		
		US GAAP $	**Effect of transition to IFRS $**	**IFRS $**
Assets				
Non-current assets				
Intangible assets	a	-	7,335	7,335
Property, plant and equipment	b	37,472	855	38,327
Investments		318	-	318
Trade and other receivables		5,814	-	5,814
		43,604	8,190	51,794
Current assets				
Trade and other receivables		1,360	-	1,360
Cash and cash equivalents		26,692	-	26,692
		28,052	-	28,052
Total assets		71,656	8,190	79,846
Equity and Liabilities				
Equity attributable to shareholders				
Share capital		4,511	-	4,511
Share premium		94,972		94,972
Other reserves	c	20,082	646	20,728
Accumulated deficit	e	(51,625)	7,155	(44,470)
		67,940	7,801	75,741
Non-current liabilities				
Trade and other payables		776	-	776
Asset retirement obligations	d	661	389	1,050
		1,437	389	1,826
Current liabilities				
Trade and other payables		2,279	-	2,279
		2,279	-	2,279
Total liabilities		3,716	389	4,105
Total shareholders' equity and liabilities		71,656	8,190	79,846

(tabular amounts in thousands of US dollars)

Explanation of the effect of the transition to IFRS

The following explains the material adjustments to the statement of financial position as at January 1, 2008:

		$
(a)	Reclassification of cost from property, plant and equipment to intangible assets. In accordance with IAS 16, IAS 38 and IFRS 6 the Company reallocated certain costs relating to unproved properties from property, plant and equipment to intangible assets.	7,661
	Expense pre licence expenditure. On discontinuance of the policy of full cost accounting, expenditure incurred prior to the date on which the Company obtaining legal title to the relevant licences or concessions to explore and develop areas of interest, previously capitalised within the full cost pool, is written off.	(326)
	Net effect –increase in intangible assets	7,335
(b)	Reclassification of cost from property plant and equipment to intangible assets.	(7,661)
	Reverse impairment loss. On transition to IFRS, a previous impairment loss recognised for Kazakhstan oil and gas properties in the year ended December 31, 2007 was reversed. US GAAP establishes a 'cost ceiling' for each cost center which limits the amount of costs that can be capitalized in each cost center. If a cost center's unamortized capitalized costs exceed the ceiling, the net capitalized costs must be written down to the ceiling. In calculating the ceiling limit under US GAAP, the present value of estimated future net revenues is computed by applying current prices of oil and gas reserves to estimated future production of proved oil and gas reserves, less estimated future expenditures to be incurred in developing and producing the proved reserves. The present value of estimated future net revenues is computed using a discount factor of 10% and assuming continuation of existing economic conditions. At the date of transition to IFRS, all CGUs were assessed for impairment by comparing the carrying value of the CGU to the recoverable amount. Recoverable amount was determined as value in use and was calculated as the present value of future cash flows expected to be derived from the CGU. The present value of future cash flows was computed on a pre-tax basis by applying forecast prices of oil and gas reserves to estimated future production of proved and probable oil and gas reserves, less estimated future expenditures to be incurred in developing and producing the proved and probable reserves. The present value of estimated future net revenues is computed using a discount factor of 8%.	12,800
	Expense unsuccessful exploration and evaluation cost. On the discontinuance of full cost accounting, drilling expenditures associated with unsuccessful exploration wells drilled prior to December 31, 2007 were expensed. These costs were previously included in the carrying value of the full cost pool.	(3,799)

		$
	Expense pre licence expenditure. On discontinuance of the policy of full cost accounting, expenditure incurred prior to the date on which the Company obtaining legal title to the relevant licences or concessions to explore and develop areas of interest, which were previously capitalised within the full cost pool, is written off.	(907)
	Increase the carrying value of oil and gas assets due to restatement of the asset retirement obligation. The discounted value of the future cash flows related to funding the Company's asset retirement obligation in relation to oil and gas properties is increased due to a change in the discount rate applied from a risk adjusted rate as required by US GAAP to a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. This results in an addition to the carrying value of oil and gas properties. This increase in carrying value is depreciated over the remaining life of the relevant field in accordance with the Company's depreciation policy.	389
	Reduction in depreciation of oil and gas properties. Each producing field or concession is depreciated separately using the unit of production method based on proved and probable reserves. Under US GAAP depreciation was based on the countrywide full cost pool of all proved properties, both producing and non-producing, and calculated on the unit of production method over only the proved reserves.	33
	Net effect – increase in property, plant and equipment	855
(c)	Adoption of IFRS 2. The expense relating to employee options is recognised individually for each vesting tranche over the applicable vesting period, as opposed to on a straight line method over the total requisite service period as permitted by US GAAP.	646
	Effect - increase option reserve	646
(d)	Increase in asset retirement provision. The provision relating to the cost of future restoration cost of oil and gas properties increases in line with the increase noted in (b) above.	389
	Effect – increase in provisions for asset retirement obligations.	389
(e)	**The cumulative effect of these transition adjustments on the accumulated deficit as at January 1, 2008 is a decrease of:**	**7,155**

(tabular amounts in thousands of US dollars)

26.2

	Notes	Reconciliation of equity as at December 31, 2008		
	Notes	US GAAP $	Effect of transition to IFRS $	IFRS $
Assets				
Non-current assets				
Intangible assets	a	-	16,105	16,105
Property, plant and equipment	b	73,793	(8,371)	65,422
Investments		587	-	587
Trade and other receivables		6,357	-	6,357
		80,737	7,734	88,471
Current assets				
Inventories		213	-	213
Trade and other receivables		2,664	-	2,664
Cash and cash equivalents		22,200	-	22,200
		25,077	-	25,077
Total assets		105,814	7,734	113,548
Equity and Liabilities				
Equity attributable to shareholders				
Share capital		6,639	-	6,639
Share premium		138,598		138,598
Other reserves	c	25,189	(42)	25,147
Accumulated deficit	f	(74,252)	7,598	(66,654)
		96,174	7,556	103,730
Non-current liabilities				
Financial liabilities - borrowings		5,096	-	5,096
Trade and other payables		523	-	523
Asset retirement obligations	d	433	32	465
		6,052	32	6,084
Current liabilities				
Financial liabilities – borrowings		853	-	853
Derivative financial instruments – warrants	e	-	146	146
Trade and other payables		2,735	-	2,735
		3,588	146	3,734
Total liabilities		9,640	178	9,818
Total shareholders' equity and liabilities		105,814	7,734	113,548

The nature of adjustments from US GAAP to IFRS at December 31, 2008 is similar to those at January 1, 2008.

		$
(a)	Reclassification of cost from property, plant and equipment to intangible assets	18,272
	Expense pre licence expenditure	(715)
	Expense unsuccessful exploration cost. On the discontinuance of full cost accounting, drilling expenditures associated with unsuccessful exploration wells drilled during the prior from January 1, 2008 to December 31, 2008 were expensed. These costs were previously included in the carrying value of the full cost pool.	(1,464)
	Increase the carrying value of oil and gas assets due to restatement of the asset retirement obligation on exploration well drilled during the prior from January 1, 2008 to December 31, 2008 due to reduction in the discount rate as described in note 26.1b.	12
	Net effect – increase in intangible assets	16,105
(b)	Reclassification of cost from property plant and equipment to intangible assets	(18,272)
	Reverse impairment loss	12,800
	Expense unsuccessful exploration cost	(3,799)
	Expense pre licence expenditure	(1,347)
	Increase the carrying value of oil and gas assets due to restatement of the asset retirement obligation.	98
	Reduction of depreciation, depletion and amortisation of oil and gas properties	2,149
	Net effect –decrease in Property, plant and equipment	(8,371)
(c)	Adoption of IFRS 2	1,121
	Adoption of IAS 32.	(1,163)
	Net effect –decrease in other reserves	(42)
(d)	Increase in asset retirement obligation. Effect – increase in provision for asset retirement obligation.	32
(e)	Adoption of IAS 32. Effect – increase in Derivative financial instruments – warrants.	146
(f)	**The cumulative effect of these transition adjustments on the accumulated deficit as at December 31, 2008 is a decrease of:**	**7,598**

(tabular amounts in thousands of US dollars)

26.3 **Consolidation reconciliation of comprehensive loss for the year ended December 31, 2008**

	Notes	US GAAP $	Effect of transition to IFRS $	IFRS $
Sales and other operating revenue		5,360	-	5,360
Finance income		832	-	832
Total revenue and other income		6,192		6,192
Production expenditures		(1,334)	-	(1,334)
Depreciation, depletion and amortization	a	(6,449)	2,116	(4,333)
Exploration and evaluation expenditure written off	b	-	(2,292)	(2,292)
Administrative expenses	d	(17,527)	(388)	(17,915)
Foreign exchange gains (loss) net		(3,060)		(3,060)
Fair value gains (loss) on derivative financial instrument	c	-	929	929
Interest	e	(449)	78	(371)
Loss before taxation		**(22,627)**	**443**	**(22,184)**
Taxation		-	-	-
Net loss and comprehensive loss for the year attributable to shareholders		**(22,627)**	**(443)**	**(22,184)**
Loss per share attributable to shareholders				
Basic and diluted		(0.40)		(0.40)

The nature of the adjustments are explained as follows:

		$
(a)	Reduction in the depletion expense for the year	2,116
(b)	Expense unsuccessful exploration wells drilled during the year (note 26.2a)	(1,464)
	Expense pre licence expenditure incurred during the year (note 26.1a)	(388)
	Expense pre licence expenditure incurred during the year (note 26.1b)	(440)
	Net effect – increase in exploration and evaluation expenditure written off	(2,292)
(c)	Fair value gains on derivative financial instrument	929
(d)	Increase in the cost of employee share options for the year	(388)

(e)	Decrease in the accretion charge on the Company's asset retirement obligation due to the transition adjustment (note 26.1d)	78

Restatement of cash flow statement from US GAAP to IFRS

The restatement from US GAAP to IFRS had no significant effect on the reported cash flows generated by the Company. The reconciling items between US GAAP presentation and IFRS presentation have no net effect on the cash flows generate