

Notes to the Group financial statements

Year ended 31 December 2008

Note 1. Segmental reporting

In the opinion of the Directors, the operations of the Group comprise one class of business, oil and gas exploration, development and production and the sale of hydrocarbons and related activities. The Group also operates within four geographical markets, Europe, Africa, South Asia and South America.

The following tables present revenue, profit and certain asset and liability information regarding the Group's business segments for the years ended 31 December 2008 and 2007.

	Africa £'000	Europe £'000	South Asia £'000	South America £'000	Unallocated £'000	Total £'000
2008						
Sales revenue by origin	475,672	204,602	11,399	-	-	691,673
Segment result	137,387	50,615	(31,854)	(40,474)	-	115,674
Profit on disposal of subsidiaries						213,268
Profit on disposal of oil and gas assets						30,614
Unallocated corporate expenses						(59,861)
Operating profit						299,695
Gain on hedging instruments						42,927
Finance revenue						3,928
Finance costs						(47,238)
Profit before tax						299,312
Income tax expense						(73,069)
Profit after tax						226,243
Total assets	2,229,704	495,163	65,290	100,624	41,508	2,932,289
Total liabilities	(651,311)	(213,050)	(19,494)	(31,783)	(707,476)	(1,623,114)
Other segment information						
Capital expenditure:						
Property, plant and equipment	103,710	39,990	4,408	-	7,036	155,144
Intangible exploration and evaluation assets	293,618	34,445	11,589	12,131	-	351,783
Depletion, depreciation and amortisation	(110,647)	(81,978)	(5,749)	-	(3,933)	(202,307)
Impairment losses recognised in income	(18,220)	-	(8,085)	-	-	(26,305)
Exploration costs written off	(146,916)	(12,582)	(26,729)	(40,474)	-	(226,701)

	Africa £'000	Europe £'000	South Asia £'000	South America £'000	Unallocated £'000	Total £'000
2007						
Sales revenue by origin	371,883	258,838	8,482	–	–	639,203
Segment result	144,886	78,979	1,827	(4,419)	–	221,273
Loss on disposal of subsidiaries						(597)
Unallocated corporate expenses						(31,628)
Operating profit						189,048
Loss on hedging instruments						(29,267)
Finance revenue						3,095
Finance costs						(48,673)
Profit before tax						114,203
Income tax expense						(61,609)
Profit after tax						52,594
Total assets	1,344,226	553,340	66,465	112,008	15,163	2,091,202
Total liabilities	(527,843)	(242,597)	(13,870)	(37,731)	(556,491)	(1,378,532)
Other segment information						
Capital expenditure:						
Property, plant and equipment	115,012	86,960	6,096	–	4,145	212,213
Intangible exploration and evaluation assets	152,129	32,587	4,411	4,745	–	193,872
Depletion, depreciation and amortisation	(98,379)	(101,359)	(3,286)	–	(2,781)	(205,805)
Impairment losses recognised in income	(13,834)	–	–	–	–	(13,834)
Exploration costs written off	(45,862)	(12,504)	(1,450)	(4,419)	–	(64,235)

Unallocated expenditure and net liabilities include amounts of a corporate nature and not specifically attributable to a geographic area, including tax balances and the Group debt.

Note 2. Total revenue

	2008 £'000	2007 £'000
Sales revenue		
Oil and gas revenue from the sale of goods	800,715	619,607
(Loss)/profit on realisation of cash flow hedges	(119,258)	2,058
	681,457	621,665
Tariff income	10,216	17,538
Total operating revenue	691,673	639,203
Finance revenue	3,928	3,095
Total revenue	695,601	642,298

Note 3. Operating profit

	2008 £'000	2007 £'000
Operating profit is stated after charging:		
Staff costs (see note 4 below)	46,015	33,632
Depletion and amortisation	198,374	203,024
Impairment of property, plant and equipment	26,305	13,834
Depreciation of other fixed assets	3,933	2,781
Exploration write off	226,701	64,235
Share-based payment charge	7,862	5,388
Gain/(loss) on hedging instruments	42,927	(29,267)
Operating lease rentals	5,098	4,798
Auditors' remuneration (see below)	781	767

	2008 £'000	2007 £'000
Audit services:		
Fees payable to the Company's auditors for the audit of the Company's annual accounts	176	168
Audit of the Company's subsidiaries pursuant to legislation	402	358
	578	526
Tax services:		
Compliance services	-	68
Advisory services	18	6
	18	74
Other non-audit services:		
Services related to corporate finance transactions	82	119
Other services	103	48
	185	167
Total	781	767

Note 4. Staff costs

The average monthly number of employees (including Executive Directors) employed by the Group worldwide was:

	2008 Number	2007 Number
Administration	265	156
Technical	206	121
Total	471	277

Staff costs in respect of those employees was as follows:

	2008 £'000	2007 £'000
Salaries	41,507	30,442
Social security costs	2,272	1,750
Pension costs	2,236	1,440
	46,015	33,632

A proportion of the Group's staff costs shown above is recharged to the Group's joint venture partners and a proportion is capitalised into the cost of fixed assets under the Group's accounting policy for exploration, evaluation and production assets.

Included in salaries is a charge for share-based payments of £7,862,000 (2007: £5,388,000).

Details of Directors' remuneration, Directors' transactions and Directors' interests are set out in the part of the Directors' Remuneration Report described as having been audited and form part of these financial statements.

Note 5. Finance costs

	2008 £'000	2007 £'000
Interest on bank overdrafts and loans	36,556	43,561
Interest on obligations under finance leases	241	288
Total borrowing costs	36,797	43,849
Less amounts included in the cost of qualifying assets	(5,999)	(7,431)
	30,798	36,418
Finance and arrangement fees	6,368	3,646
Unwinding of discount on decommissioning provision (note 20)	10,072	8,609
	47,238	48,673

Borrowing costs included in the cost of qualifying assets during the year arose on the general borrowing pool and are calculated by applying a capitalisation rate of 5.36% (2007: 7.74%) to cumulative expenditure on such assets.

Note 6. Taxation on profit on ordinary activities

(a) Analysis of charge in period

The tax charge comprises:

	2008 £'000	2007 £'000
Current tax		
UK corporation tax	38,541	2,328
Foreign taxation	77,034	27,768
Total corporate tax	115,575	30,096
UK petroleum revenue tax	1,382	11,048
Total current tax	116,957	41,144
Deferred tax		
UK corporation tax	(10,355)	21,631
Foreign taxation	(37,385)	229
Total corporate tax	(47,740)	21,860
UK petroleum revenue tax	3,852	(1,395)
Total deferred tax (note 20)	(43,888)	20,465
Total tax expense	73,069	61,609

(b) Factors affecting tax charge for period

As the Group earns a significant portion of its profits in the UK, the tax rates applied to profit on ordinary activities in preparing the reconciliation below is the standard rate of UK corporation tax applicable to the Group's oil and gas activities plus the rate of Supplementary corporation tax (SCT).

The difference between the total current tax charge shown above and the amount calculated by applying the standard rate of UK corporation tax applicable to UK upstream profits (30%) plus the rate of SCT in respect of UK upstream profits (20%) to the profit before tax is as follows:

	2008 £'000	2007 £'000
Group profit on ordinary activities before tax	299,312	114,203
Tax on group profit on ordinary activities at a combined standard UK corporation tax and SCT rate of 50% (2007: 50%)	149,656	57,102
Effects of:		
Expenses not deductible for tax purposes	938	12,056
Utilisation of tax losses not previously recognised	1,863	–
Net losses not recognised	118,371	50,706
Petroleum revenue tax (PRT)	5,234	9,654
UK corporation tax deductions for current PRT	(2,617)	(4,827)
Adjustments relating to prior years	(379)	(5,613)
Income taxed at a different rate	(29,849)	(7,321)
Income not subject to corporation tax	(170,148)	(50,148)
Group total tax expense for the year	73,069	61,609

The Group's profit before taxation will continue to be subject to jurisdictions where the effective rate of taxation differs from that in the UK. Furthermore, unsuccessful exploration expenditure is often incurred in jurisdictions where the Group has no taxable profits, such that no related tax benefit arises. Accordingly, the Group's tax charge will continue to depend on the jurisdictions in which pre-tax profits and exploration costs written off arise.

The Group has tax losses of £155 million (2007: £131 million) that are available indefinitely for offset against future taxable profits in the companies in which the losses arose. Deferred tax assets have not been recognised in respect of these losses as they may not be used to offset taxable profits elsewhere in the Group.

Note 7. Dividends

	2008 £'000	2007 £'000
Declared and paid during year		
Final dividend for 2007: Stg4p (2006: Stg3.5p) per ordinary share	28,690	25,051
Interim dividend for 2008: Stg2p (2007: Stg2p) per ordinary share	14,483	14,355
Dividends paid	43,173	39,406
Proposed for approval by shareholders at the AGM		
Final dividend for 2008: Stg4p (2007: Stg4p) per ordinary share	29,316	28,784

The proposed final dividend is subject to approval by shareholders at the Annual General Meeting and has not been included as a liability in these financial statements.

Note 8. Earnings per ordinary share

Basic earnings per ordinary share amounts are calculated by dividing net profit for the year attributable to ordinary equity holders of the parent by the weighted average number of ordinary shares outstanding during the year.

Diluted earnings per ordinary share amounts are calculated by dividing net profit for the year attributable to ordinary equity holders of the parent by the weighted average number of ordinary shares outstanding during the year plus the weighted average number of ordinary shares that would be issued if employee and other share options were converted into ordinary shares.

	2008 €'000	2007 €'000
Earnings		
Net profit attributable to equity shareholders	223,211	50,887
Effect of dilutive potential ordinary shares	-	-
Diluted net profit attributable to equity shareholders	223,211	50,887
	2008	2007
Number of shares		
Basic weighted average number of shares	723,355,745	717,025,714
Dilutive potential ordinary shares	8,675,224	14,348,042
Diluted weighted average number of shares	732,030,969	731,373,756

Note 9. Intangible exploration and evaluation assets

	2008 €'000	2007 €'000
At 1 January	956,580	820,437
Acquisition of subsidiaries (note 26)	-	48,959
Additions	351,783	193,872
Disposals	(40,149)	-
Transfer to assets held for sale (note 18)	-	(11,398)
Amounts written off	(226,701)	(64,235)
Transfer from/(to) property, plant and equipment (note 10)	368	(15,442)
Currency translation adjustments	375,896	(15,613)
At 31 December	1,417,777	956,580

The amounts for intangible exploration and evaluation assets represent active exploration projects. These amounts will be written off to the Income Statement as exploration costs unless commercial reserves are established or the determination process is not completed and there are no indications of impairment. The outcome of ongoing exploration, and therefore whether the carrying value of exploration and evaluation assets will ultimately be recovered, is inherently uncertain.

Amounts written off include an impairment charge calculated in accordance with IAS 36 – Impairment of assets of €60.1 million (2007: £nil). This impairment has resulted from lower reserves estimates following a change in the most likely development plans and lower assumed oil prices following the fall in oil prices in the second half of the year. In calculating this impairment, management has used a range of assumptions, including a long-term oil price of \$80 per barrel and a 15% pre-tax discount rate.

Note 10. Property, plant and equipment

	Oil and gas assets £'000	Other fixed assets £'000	Total £'000
Cost			
At 1 January 2007	1,357,292	9,996	1,367,288
Acquisition of subsidiaries (note 26)	(39,489)	–	(39,489)
Additions	208,068	4,145	212,213
Transfer from intangible exploration and evaluation fixed assets (note 9)	15,442	–	15,442
Currency translation adjustments	(19,291)	273	(19,018)
At 1 January 2008 (<i>as restated*</i>)	1,522,022	14,414	1,536,436
Additions	148,109	7,035	155,144
Disposals	(33,752)	(258)	(34,010)
Transfer to intangible exploration and evaluation fixed assets (note 9)	(368)	–	(368)
Currency translation adjustments	319,287	1,886	321,173
At 31 December 2008	1,955,298	23,077	1,978,375
Depreciation, depletion and amortisation			
At 1 January 2007	428,521	4,399	432,920
Charge for the year	203,024	2,781	205,805
Impairment loss	13,834	–	13,834
Currency translation adjustments	(6,769)	230	(6,539)
At 1 January 2008 (<i>as restated*</i>)	638,610	7,410	646,020
Charge for the year	198,374	3,933	202,307
Impairment loss	26,305	–	26,305
Disposals	(25,951)	(111)	(26,062)
Currency translation adjustments	142,197	1,234	143,431
At 31 December 2008	979,535	12,466	992,001
Net book value			
At 31 December 2008	975,763	10,611	986,374
At 31 December 2007 (<i>as restated*</i>)	883,412	7,004	890,416

* The 2007 comparatives have been restated due to an asset held for sale being reclassified during 2008 (see note 18).

Additions include capitalised interest of £5,999,000 (2007: £7,431,000).

The carrying amount of the Group's oil and gas assets includes an amount of £9,833,000 (2007: £8,147,000) in respect of assets held under finance leases.

Other fixed assets include leasehold improvements, motor vehicles and office equipment.

The 2008 impairment loss relates to the Chinguetti field in Mauritania and the Chachar field in Pakistan (2007: Chinguetti field in Mauritania). The recoverable amount of the Chinguetti field in Mauritania was determined by estimating its value in use. In calculating this impairment, management used a production profile based on proven and probable reserves estimates and a range of assumptions, including an oil price assumption equal to the forward curve in 2009 and 2010 and \$80 per barrel thereafter and a 12.5% pre-tax discount rate. The recoverable amount of the Chachar field in Pakistan was determined by reference to its disposal value less costs to sell.

Depletion and amortisation for oil and gas properties is calculated on a unit-of-production basis, using the ratio of oil and gas production in the period to the estimated quantities of commercial reserves at the end of the period plus production in the period, generally on a field-by-field basis. Commercial reserves estimates are based on a number of underlying assumptions including oil and gas prices, future costs, oil and gas in place and reservoir performance, which are inherently uncertain. Commercial reserves estimates are based on a Group reserves report produced by an independent engineer. However, the amount of reserves that will ultimately be recovered from any field cannot be known with certainty until the end of the field's life.

Note 11. Investments

	2008 £'000	2007 £'000
Unlisted investments	447	447

The fair value of these investments is not materially different from their carrying value.

Principal subsidiary undertakings

At 31 December 2008 the Company's principal subsidiary undertakings, all of which are included in the consolidated Group financial statements, were:

Name	%	Country of operation	Country of registration
Directly held			
Tullow Oil SK Limited	100	United Kingdom	England & Wales
Tullow Oil SPE Limited	100	United Kingdom	England & Wales
Tullow Group Services Limited	100	United Kingdom	England & Wales
Tullow Oil Limited	100	Ireland	Ireland
Tullow Overseas Holdings B.V.	100	Netherlands	Netherlands
Tullow Gabon Holdings Limited	50	Gabon	Isle of Man
Indirectly held			
Tullow (EA) Holdings Limited	100	Isle of Man	British Virgin Islands
Tullow Oil International Limited	100	Channel Islands	Jersey
Tullow Pakistan (Developments) Limited	100	Pakistan	Jersey
Tullow Bangladesh Limited	95	Bangladesh	Jersey
Tullow Côte d'Ivoire Limited	100	Côte d'Ivoire	Jersey
Tullow Côte d'Ivoire Exploration Limited	100	Côte d'Ivoire	Jersey
Tullow India Operations Limited	100	India	Jersey
Tullow Madagascar Limited	100	Madagascar	Jersey
Tullow Ghana Limited	100	Ghana	Jersey
Tullow Angola B.V.	100	Angola	Netherlands
Tullow Congo Limited	100	Congo	Isle of Man
Tullow Equatorial Guinea Limited	100	Equatorial Guinea	Isle of Man
Tullow Kudu Limited	100	Namibia	Isle of Man
Tullow Uganda Limited	100	Uganda	Isle of Man
Tullow Gabon Holdings Limited	50	Gabon	Isle of Man
Tullow Oil Gabon SA	100	Gabon	Gabon
Tulipe Oil SA	50	Gabon	Gabon
Hardman Chinguetti Production (Pty) Limited	100	Mauritania	Australia
Hardman Petroleum (Mauritania) (Pty) Limited	100	Mauritania	Australia
Planet Oil (Mauritania) Limited	100	Mauritania	Guernsey
Tullow Uganda Operations Limited	100	Uganda	Australia
Tullow Hardman Holdings B.V.	100	Netherlands	Netherlands
Tullow South Africa (Pty) Limited	100	South Africa	South Africa

The principal activity of all companies relates to oil and gas exploration, development and production.

Note 12. Inventories

	2008 £'000	2007 £'000
Warehouse stocks and materials	27,943	16,927
Oil stocks	9,907	7,970
	37,850	24,897

Inventories includes a provision of £2,400,000 (2007: Enil) for warehouse stock and materials where it is considered that the net realisable value is lower than the original cost.

Note 13. Other current assets

	2008 £'000	2007 £'000
Other debtors	45,606	27,214
Prepayments	5,518	2,458
VAT recoverable	9,084	3,679
	60,208	33,351

Note 14. Cash and cash equivalents

	2008 £'000	2007 £'000
Cash at bank and in hand	241,513	69,357
Short-term deposits	69,507	12,867
	311,020	82,224

Cash and cash equivalents includes an amount of £36,000,000 (2007: £8,254,000) which is a reserve held on fixed term deposit in support of a Letter of Credit facility which relates to the Group's share of certain decommissioning and FPSO costs and an amount of £152,972,000 (2007: £24,453,000) which the Group holds as operator on behalf of joint venture partners.

Note 15. Trade and other payables**Current liabilities**

	2008 £'000	2007 (as restated*) £'000
Trade payables	129,693	65,922
Other payables	30,938	9,174
Deferred income (take or pay)	722	722
Accruals	138,241	86,032
PAYE and social security	17,507	6,649
VAT and other similar taxes	10,189	10,064
Current portion of finance lease (note 19)	2,925	2,063
	330,215	180,626

Non-current liabilities

	2008 £'000	2007 £'000
Other payables	–	9,051
Non-current portion of finance lease (note 19)	6,089	6,535
	6,089	15,586
– After one year but within five years	6,089	14,872
– After five years	–	714
	6,089	15,586

* The 2007 comparatives have been restated due to an asset held for sale being reclassified during 2008 (see note 18).

Trade and other payables are non-interest bearing except for finance leases (note 19).

Note 16. Financial liabilities

	2008 £'000	2007 £'000
Current		
Short-term borrowings	210,528	9,793
Non-current		
Term loans repayable		
– After one year but within two years	393,257	282,275
– After two years but within five years	95,784	257,997
	489,041	540,272

Group bank loans are stated net of unamortised arrangement fees of £11,806,000 (2007: £11,635,000).

Short-term borrowings, term loans and guarantees are secured by fixed and floating charges over the oil and gas assets (note 10) of the Group.

Interest rate risk

The interest rate profile of the Group's financial assets and liabilities, excluding trade and other receivables and trade and other payables, at 31 December 2008 was as follows:

	Stg £'000	Euro £'000	US\$ £'000	Other £'000	Total £'000
Cash at bank at floating interest rate	55,711	1,251	240,157	9,450	306,569
Cash at bank on which no interest is received	21	20	3,997	413	4,451
Fixed rate debt	–	–	(34,533)	–	(34,533)
Floating rate debt	–	–	(676,842)	–	(676,842)
Net cash/(debt)	55,732	1,271	(467,221)	9,863	(400,355)

The profile at 31 December 2007 for comparison purposes was as follows:

	Stg £'000	Euro £'000	US\$ £'000	Other £'000	Total £'000
Cash at bank at floating interest rate	37,004	390	39,328	472	77,194
Cash at bank on which no interest is received	713	–	2,529	1,788	5,030
Fixed rate debt	(25,000)	–	(75,101)	–	(100,101)
Floating rate debt	(40,000)	–	(421,599)	–	(461,599)
Net (debt)/cash	(27,283)	390	(454,843)	2,260	(479,476)

Floating rate debt comprises bank borrowings at interest rates fixed in advance from overnight to three months at rates determined by US Dollar LIBOR and Sterling LIBOR. Fixed rate debt comprises bank borrowings at interest rates fixed in advance for periods greater than three months or bank borrowings where the interest rate has been fixed through interest rate hedging. The Borrowing Base Facility incurs interest on outstanding debt at Sterling or US Dollar LIBOR plus a margin ranging from 100 basis points to 240 basis points depending on utilisation and concentration of non-OECD assets. The outstanding debt is repayable in variable amounts (determined semi-annually) over the period to 31 August 2012, or such time as is determined by reference to the remaining reserves of the assets, whichever is earlier. There is no requirement under the Borrowing Base Facility to hedge interest rate exposure to Sterling LIBOR and US Dollar LIBOR. The Borrowing Base Facility states that consideration should be given to hedging at least 30% of the interest rate exposure to fluctuations in LIBOR for Sterling and US Dollars in respect of loans under the facility, net of relevant cash balances.

The Hardman Bridge Facility is now a US\$200 million (£138.1 million) revolving facility which is repayable in full on 31 December 2009. The facility incurs interest on outstanding debt at US Dollar LIBOR plus a margin ranging from 300 basis points increasing in quarterly 25 basis point increments until expiry in December 2009. There is no requirement under the Hardman Bridge Facility to hedge interest rate exposure to US Dollar LIBOR. The Hardman Bridge Facility states that consideration should be given to hedging at least 30% of the interest rate exposure to fluctuations in LIBOR for US Dollars in respect of loans under the facility, net of relevant cash balances.

At the end of December 2008, the headroom under the facilities amounted to US\$335 million (£231.4 million); US\$235 million (£162.3 million) under the Borrowing Base and US\$100 million (£69.1 million) under the Hardman Bridge Facility. At the end of December 2007, the headroom under the two facilities was US\$457 million (£228.8 million); US\$307 million (£153.7 million) under the Borrowing Base and US\$150 million (£75.1 million) under the Hardman Bridge Facility.

The Group is exposed to floating rate interest rate risk as entities in the Group borrow funds at floating interest rates. The Group hedges its floating rate interest rate exposure on an ongoing basis through the use of interest rate derivatives, namely interest rate swaps, interest rate collars and interest rate caps. All interest rate derivatives currently in place were put in place for a three-year period in May 2008 and expire in May 2011. The interest rate swap currently in place has a swap rate of 3.4375% for a current notional principal of US\$50 million (£34.5 million). The effect of the interest rate collar currently in place limits the exposure to US Dollar LIBOR at varying rates (maximum of 4.3%) over the life of the derivative for a current notional principal of US\$50 million (£34.5 million). The combined mark-to-market position as at the 2008 year end was £2,089,000 (2007: £104,000). The interest rate hedges are included in fixed rate debt in 2008 and were included in the floating rate debt table in 2007 as there was non-material differences between book and fair values for the mark-to-markets on the hedges in place at the time.

Foreign currency risk

Wherever possible, the Group conducts and manages its business in Sterling (UK) and US Dollars (all other countries), the functional currencies of the industry in the areas in which it operates. A natural hedge exists in the majority of the Group's oil and gas income and expenditure, which are denominated in US Dollars and Sterling respectively. The Group's borrowing facilities are also denominated in Sterling and US Dollars, which further assists in foreign currency risk management. From time to time the Group undertakes certain transactions denominated in foreign currencies. These exposures are managed by executing foreign currency financial derivatives, typically to manage exposures arising on corporate transactions such as acquisitions and disposals. There were no foreign currency financial derivatives in place at the 2008 year end. Cash balances are held in other currencies to meet immediate operating and administrative expenses or to comply with local currency regulations.

As at 31 December 2008, the only material monetary assets or liabilities of the Group that were not denominated in the functional currency of the respective subsidiaries involved were US\$930 million (£642.3 million) cash drawings under the US\$1,350 million Borrowing Base Facility and US\$100 million (£69.1 million) cash drawings under the US\$200 million Hardman Bridge Facility. As at 31 December 2007 the only material assets or liabilities that were not denominated in the functional currency of the respective subsidiaries involved were US\$570 million (£285.4 million) cash drawings under the US\$1,350 million Borrowing Base facility and US\$400 million (£200.3 million) cash drawings under the \$550million Hardman Bridge Facility. These US Dollar cash drawings at 31 December 2008 continue to be held as a hedge against US Dollar denominated net assets in subsidiaries.

The carrying amounts of the Group's foreign currency denominated monetary assets and monetary liabilities at the reporting date are £444.5 million (2007: £452.2 million).

Foreign currency sensitivity analysis

The Group is mainly exposed to fluctuation in the US Dollar. The Group measures its market risk exposure by running various sensitivity analyses including 20% favourable and adverse changes in the key variables. The sensitivity analyses include only outstanding foreign currency denominated monetary items and adjusts their translation at the period end for a 20% change in foreign currency rates.

As at 31 December 2008, a 20% increase in Sterling against the US Dollar would have resulted in a decrease in foreign currency denominated liabilities and equity of £133.1 million (2007: £49.4 million 10% increase) and a 20% decrease in Sterling against US Dollar would have resulted in an increase in foreign currency denominated liabilities and equity of £199.7 million (2007: £60.3 million 10% decrease).

Liquidity risk

The Group manages the liquidity requirements by the use of both short and long-term cash flow projections, supplemented by maintaining debt financing plans and active portfolio management. Ultimate responsibility for liquidity risk management rests with the Board of Directors, which has built an appropriate liquidity risk management framework for the management of the Group's short, medium and long-term funding and liquidity management requirements.

The Group closely monitors and manages its liquidity risk. Cash forecasts are regularly produced and sensitivities run for different scenarios including, but not limited to, changes in commodity prices and different production rates from the Group's portfolio of producing fields. The Group normally seeks to ensure that it has a minimum ongoing capacity of £200 million for a period of at least 12 months to safeguard the Group's ability to continue as a going concern.

Following the equity placing announced in January 2009 and securing the US\$2 billion financing in March 2009, the Group's forecasts and projections show that there is significant capacity and financial flexibility for the 12 months from the date of this Annual Report and Accounts.

Although there is considerable economic uncertainty at the present time, after taking account of the above, the directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the Annual Report and Accounts.

Note 17. Financial instruments**Financial risk management objectives**

The Group holds a portfolio of commodity derivative contracts, with various counterparties, covering both its underlying oil and gas businesses. In addition, the Group holds a small portfolio of interest rate and foreign exchange derivatives. The use of financial derivatives is governed by the Group's policies approved by the Board of Directors. Compliance with policies and exposure limits is reviewed by the internal auditors on a regular basis. The Group does not enter into or trade financial instruments, including derivative financial instruments, for speculative purposes.

Fair values of financial assets and liabilities

The Group considers the carrying value of all the financial assets and liabilities to be materially the same as the fair value.

The Group has no material financial assets that are past due.

Fair values of derivative instruments

Under IAS 39 all derivatives must be recognised at fair value on the Balance Sheet with changes in such fair value between accounting periods being recognised immediately in the Income Statement, unless the derivatives have been designated as cash flow or fair value hedges. The fair value is the amount for which the asset or liability could be exchanged in an arm's length transaction at the relevant date. Fair values are determined using quoted market prices (marked-to-market values) where available. To the extent that market prices are not available, fair values are estimated by reference to market-based transactions, or using standard valuation techniques for the applicable instruments and commodities involved.

The Group's derivative instrument book and fair values were as follows:

Assets/(liabilities):	Less than one year £'000	One to three years £'000	Total 2008 £'000	Less than one year £'000	One to three years £'000	Total 2007 £'000
Cash flow hedges						
Gas derivatives	(5,666)	(5,161)	(10,827)	(7,573)	(13,489)	(21,062)
Oil derivatives	26,523	35,662	62,185	(81,832)	(55,046)	(136,878)
Interest rate derivatives	(868)	(1,221)	(2,089)	(104)	–	(104)
	19,989	29,280	49,269	(89,509)	(68,535)	(158,044)

Market risk

The Group's activities expose it primarily to the financial risks of changes in commodity prices, foreign currency exchange rates and interest rates.

Oil and gas prices

The Group uses a number of derivative instruments to mitigate the commodity price risk associated with its underlying oil and gas revenues. Such commodity derivatives will tend to be priced using pricing benchmarks, such as Brent Dated, D-1 Heren and M-1 Heren, which correlate as far as possible to the underlying oil and gas revenues respectively. The Group hedges its estimated oil and gas revenues on a portfolio basis, aggregating its oil revenues from substantially all of its African oil interests and its gas revenues from substantially all of its UK gas interests.

At 31 December 2008, the Group's oil hedge position was summarised as follows:

Oil hedges	H1 2009	H2 2009	2010	2011
Volume – bopd	14,414	14,000	6,500	1,000
Average Price* – \$/bbl	59.68	60.42	78.80	69.40

* Average hedge prices are based on market prices as at 31 December 2008 and represent the current value of hedged volumes at that date.

At 31 December 2008, the Group's gas hedge position was summarised as follows:

Gas hedges	H1 2009	H2 2009	2010	2011
Volume – mmscfd	64.4	44.4	17.8	3.7
Average Price* – p/therm	57.74	54.30	56.94	63.16

* Average hedge prices are based on market prices as at 31 December 2008 and represent the current value of hedged volumes at that date.

As at 31 December 2008, all of the Group's oil and gas derivatives have been designated as cash flow hedges. The Group's oil and gas hedges have been assessed to be 'highly effective' within the range prescribed under IAS 39 using regression analysis on oil and ratio analysis on gas. There is, however, a degree of ineffectiveness inherent in the Group's oil hedges arising from, among other factors, the discount on the Group's underlying African crude relative to Brent and the timing of oil liftings relative to the hedges. There is also a degree of ineffectiveness inherent in the Group's gas hedges which arise from, among other factors, field production performance on any day.

Income statement hedge summary

The changes in the fair value of hedges which are required to be recognised immediately in the Income Statement for the year were as follows:

	2008 £'000	2007 £'000
Gain/(loss) on hedging instruments:		
Cash flow hedges		
Gas derivatives		
Ineffectiveness	103	(533)
Time value	4,289	(9,989)
	4,392	(10,522)
Oil derivatives		
Ineffectiveness	8,183	(2,380)
Time value	30,352	(10,476)
	38,535	(12,856)
Fair value through profit and loss		
Foreign exchange derivatives	–	(5,889)
Total net gain/(loss) for the year in Income Statement	42,927	(29,267)

The following table summarises the deferred (losses)/gains on derivative instruments, net of tax effects, recorded in hedge reserve (note 23) for the year:

	2008 £'000	2007 £'000
Deferred amounts in hedge reserve		
At 1 January	(131,993)	(52,213)
Amounts recognised in profit for the year	(42,927)	23,917
Deferred gains/(losses) before tax arising during the year	206,219	(133,615)
Deferred tax movement taken directly to equity	(2,326)	29,918
	160,966	(79,780)
At 31 December	28,973	(131,993)

	2008 £'000	2007 £'000
Deferred amounts in hedge reserve net of tax effects		
Cash flow hedges		
Gas derivatives	(3,644)	(7,191)
Oil derivatives	34,111	(124,706)
Interest rate derivatives	(1,494)	(96)
	28,973	(131,993)

Note 17. Financial instruments continued

Financial derivatives

The Group internally measures its market risk exposure by running various sensitivity analyses, including utilising 10% favourable and adverse changes in the key variables.

Oil and gas sensitivity analysis

The following analysis, required by IFRS 7, is intended to illustrate the sensitivity to changes in market variables, being Dated Brent oil prices and UK D-1 Heren and M-1 Heren natural gas prices. The sensitivity analysis, which is used internally by management to monitor financial derivatives, has been prepared using the following assumptions:

- the pricing adjustments relate only to the point forward mark-to-market (MTM) evaluations;
- the price sensitivities assume there is no ineffectiveness related to the oil and gas hedges; and
- the sensitivities have been run only on the intrinsic element of the hedge as management consider this to be the material component of the MTM oil and gas hedges.

As at 31 December 2008, a 10% increase in the dated Brent oil price curve would have decreased equity by approximately £22 million (2007: £49 million), a 10% decrease would have increased equity by approximately £27 million (2007: £43 million).

As at 31 December 2008, a 10% increase in the UK D-1 Heren and M-1 Heren natural gas price curves would have decreased equity by approximately £10.5 million (2007: £14 million), a 10% decrease would have increased equity by approximately £10.3 million (2007: £12 million).

Interest rate sensitivity analysis

As at 31 December 2008, the interest rate derivative position was out-of-the-money to an amount of £2.1 million (2007: £104,000) and due to immateriality no sensitivity analysis has been performed on the position.

FX sensitivity analysis

As at 31 December 2008 and 31 December 2007, there were no foreign exchange derivatives outstanding.

Credit risk

Credit risk refers to the risk that the counterparty will fail to perform or fail to pay amounts due, resulting in financial loss to the Group. The primary activities of the Group are oil and gas exploration and production. The Group has a credit policy that governs the management of credit risk, including the establishment of counterparty credit limits and specific transaction approvals. The Group limits credit risk by assessing creditworthiness of potential counterparties before entering into transactions with them and continuing to evaluate their credit worthiness after transactions have been initiated. The Group attempts to mitigate credit risk by entering into contracts that permit netting and allow for termination of the contract upon the occurrence of certain events of default. The Group's exposure and the credit ratings of its counterparties are continuously monitored and the aggregate value of transactions concluded is spread amongst approved counterparties.

The Group does not have any significant credit risk exposure to any single counterparty or any group of counterparties having similar characteristics. The maximum financial exposure due to credit risk on the Group's financial assets, representing the sum of cash and cash equivalents, investments, derivative assets, trade receivables and other current assets, as at 31 December was £490.2 million (2007: £207.4 million).

Note 18. Assets held for sale

On 31 January 2008 and 5 November 2007, the Group entered into sale agreements to dispose of Tullow Congo Ltd and its 40% interest in the Ngosso Permit in Cameroon respectively. The latter was successfully completed in July 2008.

However, the proposed divestment of Tullow Congo Ltd was not concluded as government approvals for the transfer of the asset were not received within a reasonable timeframe. The 2007 balance sheet has consequently been restated as the asset is no longer classified as an asset held for sale. In addition, in accordance with IFRS 5 – Non-current assets held for sale and discontinued operations, the carrying value of the asset has been adjusted for any depletion or amortisation that would have been recognised had the asset not been originally classified as held for sale. The impact of the restatement on 2007 net assets is £nil and the impact on the income statement is £nil.

The major classes of assets and liabilities comprising the operations classified as held for sale are as follows:

	2008 £'000	2007 (as restated*) £'000
Property, plant and equipment	–	–
Intangible exploration and evaluation assets	–	11,398
Trade and other receivables	–	445
Total assets classified as held for sale	–	11,843
Trade and other payables	–	–
Decommissioning provisions	–	–
Total liabilities directly associated with assets classified as held for sale	–	–
Net assets of disposal group	–	11,843

* The 2007 comparatives have been restated due to an asset held for sale being reclassified during 2008.

Note 19. Obligations under finance leases

	2008 £'000	2007 £'000
Amounts payable under finance leases:		
– Within one year	3,164	2,294
– Within two to five years	6,329	6,882
	9,493	9,176
Less future finance charges	(479)	(578)
Present value of lease obligations	9,014	8,598
Amount due for settlement within 12 months (note 15)	2,925	2,063
Amount due for settlement after 12 months (note 15)	6,089	6,535

The fair value of the Group's lease obligations approximates the carrying amount. The remaining lease term is three years (2007: four years). For the year ended 31 December 2008, the effective borrowing rate was 2.8 % (2007: 2.8%).

Note 20. Provisions**(i) Decommissioning costs**

	2008 £'000	2007 (as restated) £'000
At 1 January <i>(as restated)</i>	135,139	124,868
New provisions and changes in estimates	9,987	7,252
Disposal of subsidiaries (note 26)	(37,916)	–
Decommissioning payments	(194)	(5,065)
Unwinding of discount (note 5)	10,072	8,609
Currency translation adjustment	16,931	(525)
At 31 December	134,019	135,139

The decommissioning provision represents the present value of decommissioning costs relating to the UK, African and Asian oil and gas interests, which are expected to be incurred up to 2025. These provisions have been created based on Tullow's internal estimates and, where available, operator's estimates. Assumptions, based on the current economic environment, have been made which management believe are a reasonable basis upon which to estimate the future liability. These estimates are reviewed regularly to take into account any material changes to the assumptions. However, actual decommissioning costs will ultimately depend upon future market prices for the necessary decommissioning works required which will reflect market conditions at the relevant time. Furthermore, the timing of decommissioning is likely to depend on when the fields cease to produce at economically viable rates. This in turn will depend upon future oil and gas prices, which are inherently uncertain.

(ii) Deferred taxation

	PRT £'000	UK and overseas corporate taxation £'000	Total £'000
At 1 January 2007	2,751	309,174	311,925
Charged to income statement	(1,395)	21,860	20,465
Acquisition of subsidiary (note 26)	–	9,020	9,020
Hedge movement directly to equity (note 17)	–	(29,918)	(29,918)
Currency translation adjustment	–	(3,877)	(3,877)
At 1 January 2008	1,356	306,259	307,615
Charged to income statement	3,852	(47,740)	(43,888)
Disposal of subsidiary (note 26)	–	7,398	7,398
Hedge movement directly to equity (note 17)	–	2,326	2,326
Currency translation adjustment	–	74,489	74,489
At 31 December 2008	5,208	342,732	347,940

Deferred UK and overseas corporation tax is provided as follows:

	2008 £'000	2007 £'000
Accelerated capital allowances	294,809	175,549
Decommissioning charges	(25,009)	(40,223)
Other temporary differences	(1,557)	174,810
Currency translation adjustment	74,489	(3,877)
Provision	342,732	306,259

No deferred tax has been provided on unremitted earnings of overseas subsidiaries, as the Group has no plans to remit these to the UK in the foreseeable future.

Deferred tax assets are recognised only to the extent it is considered probable that those assets will be recoverable. This involves an assessment of when those deferred tax assets are likely to reverse, and a judgement as to whether or not there will be sufficient taxable profits available to offset the tax assets when they do reverse. This requires assumptions regarding future profitability and is therefore inherently uncertain. To the extent assumptions regarding future profitability change, there can be an increase or decrease in the level of deferred tax assets recognised which can result in a charge or credit in the period in which the change occurs.

Note 21. Reconciliation of changes in equity

	Share capital £'000	Share premium £'000	Other reserves (note 23) £'000	Shares to be issued (note 26) £'000	Retained earnings £'000	Total £'000	Minority interest £'000	Total equity £'000
At 1 January 2007	65,190	126,075	69,791	235,621	269,799	766,476	-	766,476
Total recognised income and expense for the year	-	-	(85,101)	-	50,887	(34,214)	1,707	(32,507)
Acquisition	-	-	-	-	-	-	13,780	13,780
Purchase of treasury shares	-	-	(3,722)	-	-	(3,722)	-	(3,722)
Shares to be issued in respect of Hardman acquisition	6,500	-	229,121	(235,621)	-	-	-	-
New shares issued in respect of employee share options	271	2,390	-	-	-	2,661	-	2,661
Share-based payment charges	-	-	-	-	5,388	5,388	-	5,388
Dividends paid (note 7)	-	-	-	-	(39,406)	(39,406)	-	(39,406)
At 1 January 2008	71,961	128,465	210,089	-	286,668	697,183	15,487	712,670
Total recognised income and expense for the year	-	-	376,420	-	223,211	599,631	9,844	609,475
Purchase of treasury shares	-	-	(11,235)	-	-	(11,235)	-	(11,235)
New shares issued in respect of employee share options	692	5,840	-	-	-	6,532	-	6,532
New shares issued in respect of royalty obligation	635	26,409	-	-	-	27,044	-	27,044
Vesting of PSP shares	-	-	6,857	-	(6,857)	-	-	-
Share-based payment charges	-	-	-	-	7,862	7,862	-	7,862
Dividends paid (note 7)	-	-	-	-	(43,173)	(43,173)	-	(43,173)
At 31 December 2008	73,288	160,714	582,131	-	467,711	1,283,844	25,331	1,309,175

Note 22. Called up equity share capital and share premium account**(a) Authorised**

	2008 £'000	2007 £'000
1,000,000,000 Ordinary shares of Stg10p each	100,000	100,000

(b) Allotted equity share capital and share premium

	Equity share capital allotted and fully paid		Share premium
	Number	£'000	£'000
Ordinary shares of Stg10p each			
At 1 January 2007	651,900,298	65,190	126,075
Issues during the year			
- Exercise of share options	2,711,407	271	2,390
- Hardman acquisition	64,998,817	6,500	-
At 1 January 2008	719,610,522	71,961	128,465
Issues during the year			
- Exercise of share options	6,926,931	692	5,840
- New shares issued in respect of royalty obligation	6,352,114	635	26,409
At 31 December 2008	732,889,567	73,288	160,714

Note 23. Other reserves

	Merger reserve £'000	Foreign currency translation reserve £'000	Hedge reserve £'000	Treasury shares £'000	Total £'000
At 1 January 2007	178,953	(52,972)	(52,213)	(3,977)	69,791
Hedge movement	-	-	(79,780)	-	(79,780)
Currency translation adjustment	-	(5,321)	-	-	(5,321)
Purchase of treasury shares	-	-	-	(3,722)	(3,722)
Merger reserve movement	229,121	-	-	-	229,121
At 1 January 2008	408,074	(58,293)	(131,993)	(7,699)	210,089
Hedge movement (note 17)	-	-	160,966	-	160,966
Currency translation adjustment	-	215,454	-	-	215,454
Vesting of PSP shares	-	-	-	6,857	6,857
Purchase of treasury shares	-	-	-	(11,235)	(11,235)
At 31 December 2008	408,074	157,161	28,973	(12,077)	582,131

During 2007 the Company issued 64,998,817 ordinary shares relating to the acquisition of Hardman Resources. In accordance with the merger provisions of Section 131 of the Companies Act 1985, the Company has transferred the premium on the shares issued of £229.1 million, using the market value at the date of acquisition, to the Merger reserve.

The foreign currency translation reserve represents exchange gains and losses arising on translation of foreign currency subsidiaries, monetary items receivable from or payable to a foreign operation for which settlement is neither planned nor likely to occur, which form part of the net investment in a foreign operation, and exchange gains or losses arising on long-term foreign currency borrowings which are a hedge against the Group's overseas investments.

The hedge reserve represents gains and losses on hedging instruments classed as cash flow hedges that are determined as an effective hedge.

The treasury shares reserve represents the cost of shares in Tullow Oil plc purchased in the market and held by the Tullow Oil Employee Trust to satisfy awards held under the Group's share incentive plans (see note 27).

Note 24. Minority interest

	2008 £'000	2007 £'000
At 1 January	15,487	-
Additions	-	13,780
Foreign currency translation	6,812	-
Share of profit for the year	3,032	1,707
At 31 December	25,331	15,487

The minority interest relates to Tulipe Oil SA, where the Group acquired a 50% controlling shareholding during 2007.

Note 25. Cash flows from operating activities

	2008 £'000	2007 £'000
Profit before taxation	299,312	114,203
Adjustments for:		
Depletion, depreciation and amortisation	202,307	205,805
Impairment loss	26,305	13,834
Exploration costs written off	226,701	64,235
(Profit)/loss on disposal of subsidiaries	(213,268)	597
Profit on disposal of oil and gas assets	(30,614)	–
Decommissioning expenditure	(194)	(5,065)
Share-based payment charge	7,862	5,388
(Gain)/loss on hedging instruments	(42,927)	29,267
Finance revenue	(3,928)	(3,095)
Finance costs	47,238	48,673
Operating cash flow before working capital movements	518,794	473,842
Decrease/(increase) in trade and other receivables	18,548	(20,472)
Increase in inventories	(12,952)	(11,162)
Increase in trade payables	63,260	4,452
Cash generated from operations	587,650	446,660

Note 26. Acquisition and disposal of subsidiaries and oil and gas assets**(i) Disposal of subsidiary**

Tullow completed the sale of Tullow Oil UK Limited incorporating the 51.68% interest in the Hewett-Bacton complex to ENI in November 2008.

The net assets of Tullow Oil UK Limited at the date of disposal in November 2008 were as follows:-

	2008 £'000
Property, plant and equipment	24,331
Inventories	998
Trade receivables	3,791
Cash and cash equivalents	19
Other creditors	(15,309)
Current tax liability	11,254
Deferred tax liability	7,398
Provisions	(37,916)
Net liability on disposal	(5,434)
Gain on disposal	213,268
Total consideration	207,834
Satisfied by:	
Cash	207,834

(ii) Disposal of oil and gas assets

On 5 November 2007 and 2 April 2008, the Group entered into sale agreements to dispose of its 40% interest in the Ngosso Permit in Cameroon and certain non-core CMS assets in the UK respectively. The disposals were completed in June 2008. The gain on disposal of oil and gas assets amounted to £30,614,000 and total consideration received amounted to £77,530,000.

Note 26. Acquisition and disposal of subsidiaries and oil and gas assets continued**(iii) Acquisition of subsidiaries**

The Group acquired Hardman Resources Limited with effect from 20 December 2006, and completed the acquisition on 10 January 2007. The fair values of the identifiable assets and liabilities were reassessed in 2007, to reflect additional information which has become available concerning conditions that existed at the date of acquisition, in accordance with the provisions of IFRS 3 – Business combinations. The resulting changes to the 2007 financial statements are set out in the following table:

	Fair value as previously reported €'000	2007 Fair value adjustment €'000	2007 Fair value as restated €'000
Intangible exploration and evaluation assets	623,542	48,959	672,501
Property, plant and equipment	86,931	(39,489)	47,442
Inventories	3,866	–	3,866
Other current assets	10,790	–	10,790
Cash and cash equivalents	46,540	–	46,540
Trade and other payables	(11,480)	–	(11,480)
Derivative financial instruments	(1,147)	–	(1,147)
Deferred tax liabilities	(158,842)	(9,020)	(167,862)
Provisions	(5,463)	–	(5,463)
Total cost of acquisition	594,737	450	595,187
Satisfied by:			
Cash			359,566
Shares issued			235,621
			595,187

The principal fair value adjustments are in respect of property, plant and equipment, where Chinguetti commercial reserves have been downgraded by 50%, intangible exploration and evaluation assets where additional fair value has been ascribed to the African and South American assets, and the deferred tax effect of these adjustments.

Due to the inherently uncertain nature of the oil and gas industry and intangible exploration evaluation assets in particular, the assumptions underlying the final assigned values are highly judgemental in nature. The purchase consideration equals the aggregate of the fair value of the identifiable assets and liabilities of Hardman, and therefore no goodwill has been recorded on the acquisition. Deferred tax has been recognised in respect of the fair value adjustments as applicable.

Note 27. Share-based payments**2005 Performance Share Plan (PSP)**

Under the PSP, senior executives can receive conditional awards of rights over whole shares worth up to 200% of salary p.a. (300% in exceptional circumstances). The awards granted in 2008 under the PSP vest subject to a Total Shareholder Return (TSR) based performance condition under which the Company's TSR performance is measured over a fixed three-year period against both the constituents of an Index and a comparator group of oil and gas companies. For awards from March 2008 the Index is the FTSE 100 index (excluding investment trusts); for awards before March 2008, the Index is the FTSE 250 index (excluding investment trusts). Half of an award is tested against the Index and the other half against the comparator group. The test is over a three-year period starting on 1 January prior to grant, and an individual must normally remain in employment for three-years from the date of grant for the shares to vest. No dividends are paid to participants over the vesting period. Further details in relation to the PSP award measurements are provided in the Directors' Remuneration Report.

The shares outstanding under the PSP are as follows:

	2008 PSP shares	2008 Average weighted share price at grant p	2007 PSP shares	2007 Average weighted share price at grant p
Outstanding at 1 January	4,451,474	293.25	2,903,082	251.66
Granted	1,328,692	917.58	1,548,392	371.24
Exercised during the year	(1,747,750)	187.50	–	–
Forfeited/expired during the year	(175,503)	365.75	–	–
Outstanding at 31 December	3,856,913	552.92	4,451,474	293.25
The inputs of the option valuation model were:				
Risk free interest rate		4.4%-4.7% pa		5.3% pa
Expected volatility		39%-41%		33%
Dividend yield		0.7%-0.8% pa		1.5% pa

The expected life is the period from the date of grant to the vesting date. Expected volatility was determined by calculating the historical volatility of the Company's share price over a period commensurate with the expected lifetime of the awards. The weighted average fair value of the awards granted in 2008 was 653.94p per award (2007: 181.57p).

The Group recognised a total expense of £3,974,000 (2007: £2,233,000) in respect of the PSP.

Note 27. Share-based payments continued**2005 Deferred Share Bonus Plan (DSBP)**

Under the DSBP, the portion of any annual bonus entitlement of a senior executive nominated by the Remuneration Committee that is above 75% of base salary (60% for bonuses paid for 2007 and earlier years) is required to be deferred into shares. Shares awarded under the DSBP will normally vest following the end of the period of three financial years commencing with that in which the award is granted.

The shares outstanding under the DSBP are as follows:

	2008 DSBP shares	2008 Share price at grant	2007 DSBP shares	2007 Share price at grant
Outstanding at 1 January	184,254	375.4p	79,787	348.5p
Granted	96,166	629.5p	104,467	396.0p
Exercised during the year	(79,787)	348.5p	–	–
Outstanding at 31 December	200,633	507.9p	184,254	375.4p
The inputs of the option valuation model were:				
Dividend yield		1.0% pa		1.3% pa

The expected life is the period from the date of grant to the vesting date. The fair value of the awards granted in 2008 was 611.9 p per award (2007: 381.23p).

The Group recognised a total expense of £537,000 (2007: £226,000) in respect of the DSBP.

2000 Executive Share Option Scheme (ESOS)

The only share option scheme operated by the Group during the year was the 2000 ESOS. Options granted under the 2000 ESOS normally only become exercisable following the third anniversary of the date of the grant if the performance condition has been met. The condition requires that the Company's TRS performance over a fixed three-year period must exceed the median company in the constituents of an index. For awards granted from March 2008 the index is the FTSE 100 index (excluding investments trusts); for awards before March 2008 the index is the FTSE 250 index (excluding investments trusts). 100% of the awards will vest if the Company's TSR is above the median of the respective index over the three-year period following grant. Options awarded under the 2000 ESOS before 24 May 2005 are subject to monthly re-testing on a rolling three-year basis if the TSR performance criterion is not met. Options granted on or after 24 May 2005 are not subject to monthly re-testing.

Options have previously been granted under the 1988 ESOS and the 1998 ESOS. Options granted under the 1988 ESOS and the 1998 ESOS are not subject to performance conditions. All awards under the 1988 ESOS and the 1998 ESOS were made prior to 7 November 2002 and therefore, under the IFRS transitional provisions, they have not been accounted for in accordance with IFRS 2 – Share-based payments.

The following table illustrates the number and weighted average exercise prices (WAEP) of, and movements in, share options under the 1988 ESOS, the 1998 ESOS and the 2000 ESOS during the year.

	2008 Number	2008 WAEP p	2007 Number	2007 WAEP p
Outstanding as at 1 January	19,216,684	166.04	19,637,480	129.39
Granted during the year	2,475,251	647.28	2,358,408	396.46
Exercised during the year	(6,926,931)	91.50	(2,711,407)	98.31
Expired during the year	(76,899)	210.37	(67,797)	317.85
Outstanding at 31 December	14,688,105	282.06	19,216,684	166.04
Exercisable at 31 December	7,971,074	121.49	11,410,205	83.83

The weighted average share price at exercise for options exercised in 2008 was 854.25p (2007: 439.32p).

Options outstanding at 31 December 2008 had exercise prices of 61.0p to 754.0p and remaining contractual lives of one to 10 years.

The fair values were calculated using a proprietary binomial valuation model. The principal inputs to the options valuation model were:

Risk free interest rate	2.6-4.1% pa
Expected volatility	38-48%
Dividend yield	0.9-1.3% pa
Employee turnover	From 0% – 5% pa depending on seniority
Early exercise	At rates dependent upon seniority and potential gain from exercise

Expected volatility was determined by calculating the historical volatility of the Company's share price over a period commensurate with the expected lifetime of the awards.

The fair values and expected lives of the options valued in accordance with IFRS 2 were:

Award date	Weighted average exercise price p	Weighted average fair value p	Weighted average expected life from grant date years
Jan – Dec 2006	347.7	109.7	4.4
Jan – Dec 2007	396.9	123.4	4.8
Jan – Dec 2008	647.3	205.8	4.3

The Group recognised a total expense of £3,191,000 (2007: £2,794,000) in respect of the ESOS.

UK & Irish Share Incentive Plans (SIPs)

The SIPs were launched at the beginning of 2004. These are all employee plans, which have been set up in both the UK and Ireland, that enable employees to make contributions out of salary up to prescribed limits each month, which are used by the Plan trustees to acquire Tullow shares ('Partnership Shares'). The Company makes a matching contribution to the trustees to acquire a matching number of Tullow shares ('Matching Shares') on a one-for-one basis. The SIPs have a three month accumulation period.

The fair value of a Matching Share is the market value at grant adjusted for any options included. For this purpose, the grant date is the start of the accumulation period.

For the UK plan, Partnership Shares are purchased at the lower of the market values at the start of the Accumulation Period and the purchase date. For the Irish plan, shares are bought at the market price at the purchase date.

Matching shares vest three years after grant and dividends are paid to the employee during this period.

The Group recognised a total expense of £148,000 (2007: £126,000) for the matching shares and £12,000 (2007: £9,000) for the partnership shares.

Note 28. Operating lease arrangements

	2008 £'000	2007 £'000
Minimum lease payments under operating leases recognised in income for the year	5,098	4,798

At the balance sheet date, the Group had outstanding commitments for future minimum lease payments under non-cancellable operating leases, which fall due as follows:

	2008 £'000	2007 £'000
Minimum lease payments under operating leases		
Due within one year	7,781	5,098
After one year but within two years	7,753	5,229
After two years but within five years	16,769	15,522
Due after five years	976	3,236
	33,279	29,085

Operating lease payments represent rentals payable by the Group for certain of its office properties and a lease for an FPSO vessel for use on the Chinguetti field in Mauritania. Leases on office properties are negotiated for an average of six years and rentals are fixed for an average of six years. The FPSO lease runs for a minimum period of seven years from February 2006 and the contract provides for an option to extend the lease for a further three years at a slightly reduced rate.

Note 29. Capital commitments

The Directors have committed to a budget for capital expenditure for exploration and development of £606.2 million (2007: £445.6 million).

Note 30. Contingent liabilities

At 31 December 2008 there existed contingent liabilities amounting to £73.3 million (2007: £14.1 million) in respect of performance guarantees for committed work programmes.

Note 31. Related party transactions

Transactions with the Directors of Tullow Oil plc are disclosed in the Remuneration Report on pages 66 to 75. Directors are considered to be the only key management personnel as defined by IAS 24 – Related party disclosures.

There are no other related party transactions.

Note 32. Subsequent events

Since the balance sheet date Tullow has continued to progress its exploration, development and business growth strategies.

In January 2009 the Group announced the successful placing and subsequent issue of a total of 66,938,141 new ordinary shares with institutions at 600 pence per share. This represents an increase of approximately 9.1% in Tullow's existing issued share capital. These shares are credited as fully paid and rank pari passu in all respects with existing ordinary shares of 10 pence each in the capital of the Company, including the right to receive all dividends and other distributions declared, made or paid on or in respect of such shares after the date of issue.

In March 2009, the Group announced that it had finalised arrangements for US\$2 billion (£1.4 billion) of new reserve based lending facilities.

In March 2009, the Group announced a major new discovery at Tweneboa, which continues the 100% exploration success record in Ghana.

Note 33. Pension schemes

The Group operates defined contribution pension schemes for staff and Executive Directors. The contributions are payable to external funds which are administered by independent trustees. Contributions during the year amounted to £2,236,000 (2007: £1,440,000). At 31 December 2008, there was a liability of £82,000 (2007: £51,000) for contributions payable included in creditors.